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Issue Brief Series

Domestic resource mobilization and taxation

International Monetary Fund
World Bank Group

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1. Introduction

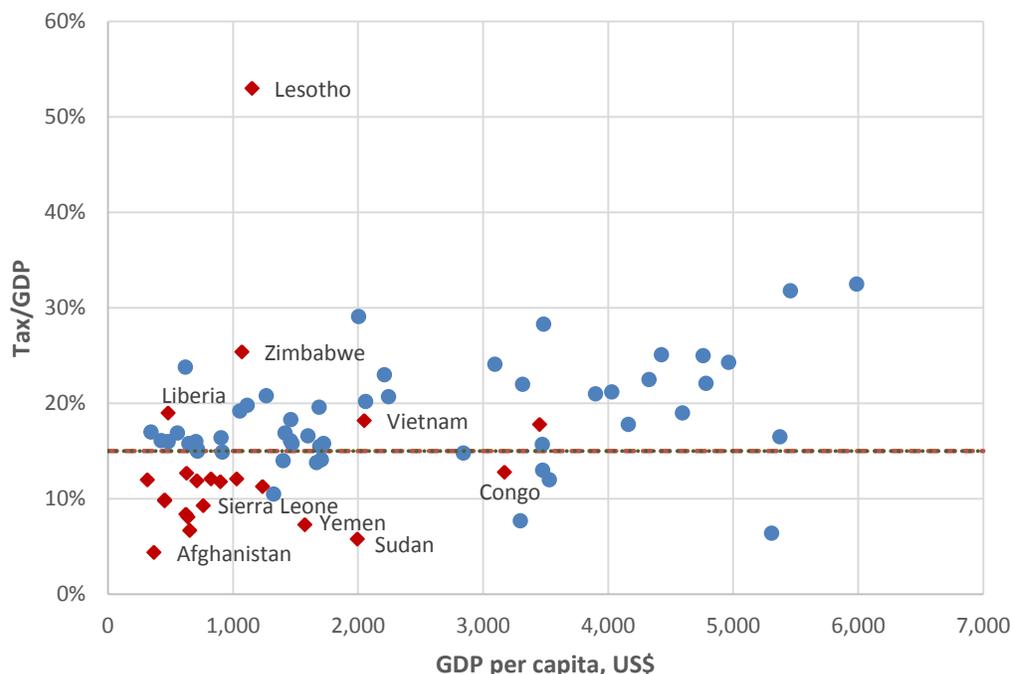
Domestic resources are the largest untapped source of financing to fund national development plans. As clearly recognized by the Addis Agenda, without effective mobilization of domestic resources, the Sustainable Development Goals cannot be achieved. This Issue Brief advises on the current state of play with revenue mobilization targets; updates on the status of tax initiatives aimed to support revenue mobilization; and suggests forward-looking policy options.

2. Stocktaking

2.1. Resource mobilization and domestic targets

The Addis Compact does not set revenue targets but rather suggests “nationally defined targets and timelines” as part of national development strategies (Addis Compact, 22). Nevertheless, total government revenue as percentage of GDP is selected by the SDG’s MoI 17.1 as one of the key monitoring indicators for tracking domestic revenue mobilization efforts.

Figure 1: Tax revenue as percent of GDP for low income and lower middle income countries in 2014

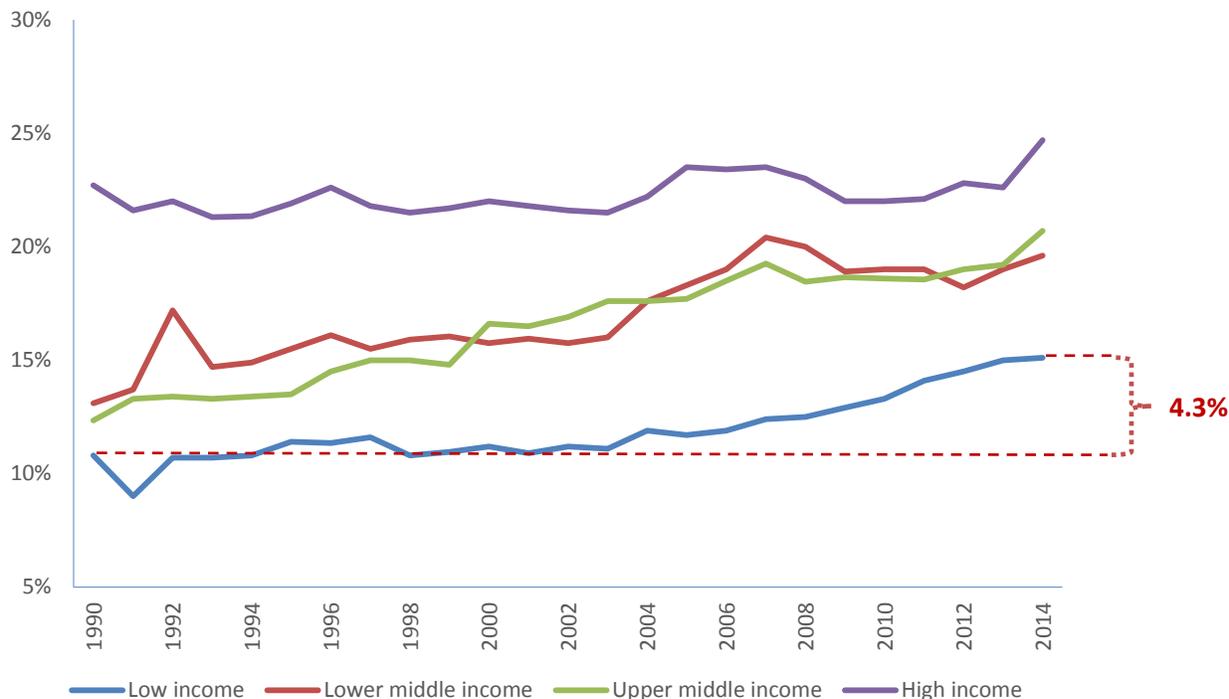


Source: IMF World Revenue Longitudinal Dataset (WoRLD), June 2016 and IMF World Economic Outlook, April 2016.

Note: Red diamonds represent the Least Developed Countries (LDCs) based on the UN OHRLLS classification.

Almost half of low-income countries raised less than 15 percent of GDP in taxes in 2014 (Figure 1). Tax revenues are the lowest in the least developed countries, including those struggling to escape conflict and fragility—about 70% of fragile and conflict affected states have a tax-to-GDP ratio under 15%. The long-term trend, however, is moderately reassuring. On average, tax revenue as percent of GDP of low-income countries grew at a rate of 1.6% annually over 1990-2014 (Figure 2), and the median tax revenue of the low income countries as a group rose by 4.2 percentage points of GDP.

Figure 2: Median tax revenue as a percent of GDP by income grouping, 1990-2014



Source: IMF Revenue Longitudinal Dataset (WoRLD), June 2016. Country classification according to World Bank country income groups.

Two databases have been developed to assist countries and other stakeholders in general better understand how tax policy, administration, and revenue structures evolve over time. This, in turn, will assist countries in adjusting their revenue strategies to meet the SDGs in constantly changing environments, and improve the quality of tax analysis.

WoRLD. As highlighted by the 2016 ITAF report, ensuring consistency in measuring the SDG targets is of key importance. The International Monetary Fund’s (IMF) World Revenue Longitudinal Dataset (WoRLD) is recognized to be as consistent as possible across countries; as such WoRLD has been selected as a basis for monitoring the SDG 17.1. The database covers tax and non-tax revenues for 186 countries; combining in a consistent manner data from two IMF sources -- IMF Government Finance Statistics and World Economic Outlook (WEO) -- and drawing on the OECD’s Revenue Statistics and Revenue Statistics in Latin America and the Caribbean. The initial public release of the database spanned revenue data from 1990 to 2013.

The latest annual update, containing 2014 data, will be released soon; this updated data served as a basis for the analysis presented above.

RA-FIT and ISORA. Increasing domestic resource mobilization will require changes to both tax policies and tax administration. An important role in guiding these efforts can be played by collecting and disseminating comparable world-wide data on revenue administration performance. The IMF's Revenue Administration Fiscal Information Tool (RA-FIT) database began as a response to the need for standard data to help revenue administrations, particularly in low income countries, to better assess and track their performance. RA-FIT includes performance measures across various tax administration functions, including administrative organization, taxpayer identification and registration, filing, revenue controls and post-filing arrangements. For the first time, a single online web-based platform is used to gather revenue administration data across many low and middle income countries not normally readily available. These measures can be benchmarked within and across country groups, for example by income groups, or conflict-affected, or resource dependent states.

The original tool has now been expanded into a more broadly used international survey on tax administration, as a joint endeavour between the Inter-American Center of Tax Administrations (CIAT), the IMF, the Intra-European Organisation of Tax Administrations (IOTA) and the OECD. It provides a core set of questions and definitions that will form the basis of the data collection system each organization will use to gather data on tax administration. This will allow for more efficient data collection, improve comparability of data between countries and organizations, and establish metrics that tax administrations globally could gauge themselves against. A Memorandum of Understanding (MoU) was signed between the IMF, CIAT, IOTA and the OECD on April 16 during the IMF/WBG Spring meetings on a joint-use single survey hosted on the RA-FIT Data Collection Platform. Renamed the International Survey on Revenue Administration (ISORA), the new survey was launched by the four organizations at the Plenary of the OECD's Forum on Tax Administration in Beijing, China in May 2016.

2.2. Tax policy effectiveness, transparency and administration

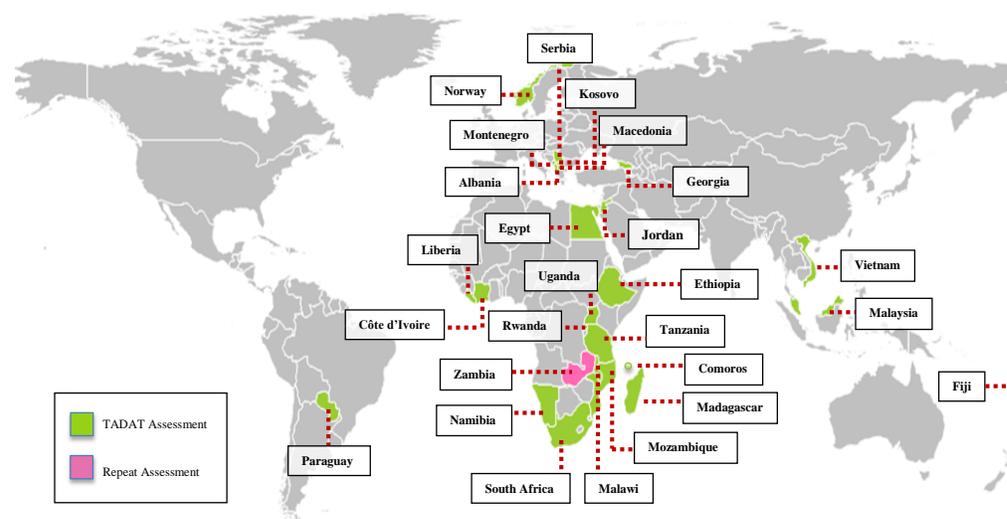
Two analytical tools have, or are being designed to assist countries in the analysis of their revenue policy systems and the performance of their revenue administrations. These tools are not meant to rank countries against each other, but simply to provide solid analysis on which policymakers can act, with some level of understanding (subject to data availability) of the implications not only on revenue, but also on key concern issues such as the distribution of the tax burden, inflation, investment, possible changes in taxpayers' behavior, etc.

Tax Administration Diagnostic Assessment Tool (TADAT). TADAT is an internationally supported diagnostic tool delivering an objective and standardized performance assessment of a country's tax administration system. As of June 2016, 29 TADAT assessments have been

conducted in countries with diverse geographic and socio-economic environments (Figure 3).¹ The assessments help country authorities and other stakeholders to prioritize their tax administration reform agendas and assess progress with reforms.

A number of countries and institutions have started using TADAT assessments to identify their reform objectives and activities, embedding TADAT’s performance outcome areas in their strategic planning process; a case study of Zambia is presented in Box 1.

Figure 3: Geographic coverage of TADAT assessments



Source: TADAT Secretariat

¹ Of these, 17 were conducted during the pilot phase (November 2013 – November 2015), and 12 during January – June 2016. Up-coming assessments include Armenia, Barbados, Democratic Republic of Congo, Guyana, Kenya, Kyrgyz, Romania and Sierra Leone.

Box 1: TADAT assessment results feed into tax administration reform in Zambia

During the 2016 repeat TADAT assessment for Zambia, it was established that the country has taken measures to address some of the weaknesses identified during the assessment conducted in November 2013. Key reforms included: (i) implementation of a comprehensive and structured process of identifying, assessing, prioritizing and mitigating institutional risks; and (ii) creation of a single tiered tax dispute resolution process that is independent of the audit department including the development of objective review procedures.

The IMF's Regional Technical Assistance Center in East Africa (AFE) is using the TADAT framework to establish results-based management baselines as a basis of its tax administration technical assistance drive in the five countries in which assessments have been conducted. The AFE also points out² that it has leveraged TADAT assessment missions to expand its collaboration with donor partners in areas of common interest—particularly in Malawi, Rwanda and Uganda.

Tax Policy Assessment Framework (TPAF). Ahead of the Financing for Development Conference in Addis Ababa, the IMF and the World Bank announced the launch of a new initiative to help member countries strengthen their tax systems. One of the pillars of the initiative calls for the development of “improved diagnostic tools to help member countries evaluate and strengthen their tax policies.”³ To implement this initiative, a tax policy assessment framework (TPAF) is being designed for systematic and structured assessment of tax policy systems, and development of policy options for reform. The purpose of the tool is not to score countries on how well they do in tax system design – simply because tax systems respond not only to revenue objectives, but to a host of other economic and social objectives that may vary across countries – but to provide a solid basis for designing and analysing the consequences of reform options.

² See the 2016 mid-year report, available at http://www.eastafritac.org/index.php?/reports/annual_reports/.

³ Press Release No. 15/330, World Bank and the IMF Launch Joint Initiative to Support Developing Countries in Strengthening Tax Systems, <http://www.imf.org/external/np/sec/pr/2015/pr15330.htm>

Scaling up of resources to support capacity building in tax. Many development partners have committed to a substantial increase of their support for building capacity to enhance revenue mobilization. Notably, the Addis Tax Initiative envisages a doubling of financial resources for such capacity building by 2020. The strategic issues this raises for the design of such support will be considered in a July 2016 report to the G20 by the partners of the new Platform for Collaboration on Tax (the IMF, OECD, UN and World Bank—more detail on the Platform is provided in the Issue Brief on International Tax Cooperation).

3. Policy options: thinking holistically and strategically

Instead of focusing on incremental changes and aiming purely at tax collection, domestic revenue mobilization efforts should take a broader and longer-term perspective. Such efforts should be targeted to create an environment conducive to sustainable revenue mobilization as part of a legitimate social contract between the government and the citizens. That means promoting efficient, effective, equitable and sustainable revenue policy and administration strategies, and strengthened legal framework supporting them. It also means a holistic rather than piecemeal treatment of all revenue aspects, including for example:

- Integrating policy and revenue collection from natural resources into the tax system, rather than treating them as sectoral issues—obviously, the expertise of government personnel in the resource sector is needed for this integration.
- Ensuring consistency of domestic and international tax rules, which means, among other things, that countries should thoroughly study the implications of tax treaties and various negotiation strategies before they embark on new treaty agreements or revise existing ones.
- Using tax policy as a tool to encourage or discourage certain activities only when policy principles and local constraints warrant it. One example is the design of investment tax incentives, which should pay attention to market imperfections, tax administration constraints in policing incentives to prevent abuse, and the effectiveness of incentives in reaching their targets. Proper monitoring of the cost and effectiveness of such policies should be in place, so policymakers can make appropriate policy changes when needed.
- Integrating various aspects of the analysis of tax policies: as noted earlier, it is only about revenue, but also about equity, efficiency, and other possible implications (e.g. how policies change opportunities or incentives for tax avoidance and evasion).

The development of a coherent and sustainable revenue mobilization strategy must truly become a whole-of-the-government effort, ensuring consistency of the country's tax policy with broader national objectives. Feeding into the national development strategy, revenue mobilization should be owned by the country, so that an effective cooperation of the various government arms can ensure a coherent and comprehensive approach, and fruitful

collaboration with external partners and donors. A number of papers⁴ from international organizations are a good starting point for understanding the key challenges that developing countries face in tax policy and administration, and building possible options for reform. Other papers provide guidance in specific areas.⁵

Finally, such holistic approach to policy making requires that tax policy be properly integrated into fiscal management. In that regard, many middle-income and most high-income countries, have found it useful and effective to develop tax policy units within their ministries of finance (or equivalent agencies), that combine economic, legal, and accounting expertise. Together with a deep understanding of their administrative capacities and constraints, countries then build revenue mobilization strategies with a good awareness of their possible implications.

⁴ IMF, 2011, Revenue Mobilization in Developing Countries (IMF: Washington DC); OECD, IMF, UN and WBG, 2011, Supporting the Development of More Effective Tax Systems; IMF, 2015, Current Challenges in Revenue Mobilization: Improving Tax Compliance (IMF: Washington DC).

⁵ IMF, OECD, UN and WBG, 2015, Options for Low Income Countries' Effective and Efficient Use of Tax Incentives for Investment; WBG, forthcoming, Transfer Pricing and Developing Economies: From Implementation to Application.