Preparatory Process for the
Third International Conference on Financing for Development
Substantive informal session: inance

11 November 2014, Trusteeship Council Chamber, United Nations, New York

Domestic public finance is essential to providing public goods and services, increasing equity, and helping manage macroeconomic stability. The Monterrey Consensus emphasized

resources and managing their

of public policy and allows countries to move toward financial autonomy. Governments may also use taxation policy to prioritize real income gains at the bottom of the income

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exemptions on basic goods and services. However, current domestic resource mobilization remains insufficient to meet sustainable development needs, and gaps persist between

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In terms of uses of resources, there are many elements of incorporating sustainable development criteria into fiscal policies, including spending allocation, gender-responsive budgeting, procurement policies, budget transparency and removing harmful subsidies.

Programme

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11 November 2014, Trusteeship Council Chamber, United Nations, New York

Co-Chairs: H.E. Mr. George Wilfred Talbot (Guyana)
H.E. Mr. Geir O. Pedersen (Norway)

Session 1:

10 a.m. to 1 p.m.: Raising domestic resources for sustainable development

Setting the Scene:

- Prof. Atul Kohli, Princeton University

Followed immediately by Q&A

Round table on country experiences with taxation

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Briefing Note

Raising domestic resources

- *Trends and policies*

Domestic finance has grown rapidly in recent years, representing by far the greatest share of financing sources for most countries. Since 2002, public domestic finance in developing countries more than doubled, increasing from US$ 838 billion to US$ 1.86 trillion.[1] Some countries have achieved sustained revenue increases of 4-5 per cent of GDP over just a few years. In absolute terms, this growth mainly reflects developments in middle-income countries. Domestic public finance also doubled in low-income countries, though it remains insufficient to meet sustainable development needs. Tax revenues account for about 10 14 per cent of GDP in low income countries, which is about one third less than in middle income countries, and significantly less than in high income countries, which achieve tax to GDP ratios of 20 - 30 per cent.[2] There is also a significant difference between low-income and middle-income countries. In 2009, tax revenue accounted for 13.6 per cent of GDP in the former, as compared to 19.3 per cent in the latter.[3]

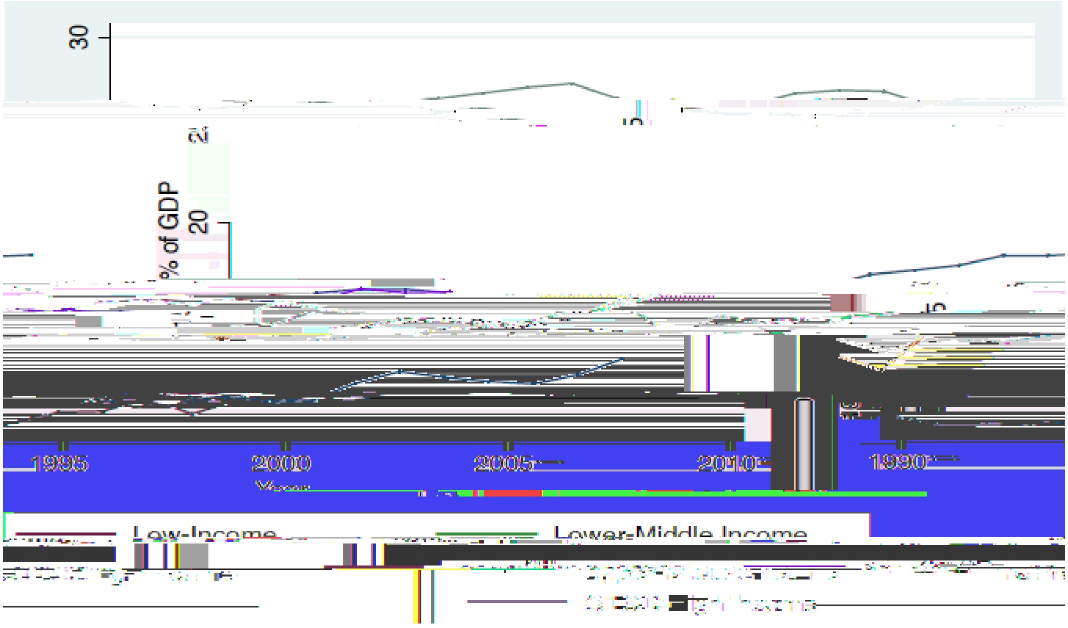
Domestic resource mobilization depends on many factors, such as size of tax base, a

taxed, and commodity prices. While optimal tax policy design is necessarily reflective of a

ocial situation, there are some generally accepted principles of sound public finance management, e.g. tax systems should be fair, efficient and transparent. In general, the tax base should be as wide as possible, while maintaining equity and efficiency. Key indicators of success in tax reform include high level political commitment, administrative and policy reform and strong leadership in the revenue administration.[4]

[1] http://capacity4dev.ec.europa.eu/ffd/document/data-2000-2012-delinked
[2] World Bank, 2013, *Financing for Development post-2015*.
[3] Source: World Bank, World Development Indicators 2013.
[4] Report to the G20 Development Working Group by the IMF, the OECD, UN and World Bank: Supporting the Development of More Effective Tax Systems. http://www.imf.org/external/np/g20/pdf/110311.pdf

Figure: Average tax to GDP ratios by country income level



Notes: OECD High income includes all OECD countries excluding Mexico, Poland and Israel. Non-OECD high income includes Uruguay, Qatar, Aruba, Croatia, Lithuania, Brunei Darussalam, Malta, Trinidad and Tobago, Antigua and Barbuda, Barbados, Singapore, Cyprus, Kuwait, Equatorial Guinea, Hong Kong, St Kitts and Nevis, San Marino, the Bahamas and Bahrain.

Source: Prichard, Cobham, and Goodall, 2014, based on ICTD Government Revenue Dataset

Countries have variable experiences with fiscal reform, and while some experiences are idiosyncratic others can help inform a deeper understanding of the potential for policy reform in other countries. Widening the tax base has been instrumental in recent advances in tax collection in many developing countries, including LDCs and SIDS. Recent improvements in tax collection also reflect increased revenue from value added taxes (VAT), robust receipts from corporate income taxes, and, to a lesser extent, personal income taxes, but also declining trade tax revenues.[5] Value added taxes have spread rapidly in developing countries, often in conjunction with lowering trade taxes; around 150 countries now have a VAT, which typically accounts for around one quarter of all tax revenue. The switch from trade taxes to a VAT has, however, sometimes led to a reduction in total revenues. Concerns have been raised about the distributional impact of value added taxes, as a proportional tax on all consumption is regressive relative to annual income, although the evidence is inconclusive.[6]

Many developing countries have significantly improved their tax administration within the last 2 decades. The average time to prepare, file and pay (or withhold) taxes decreased by almost 20 per cent from 2005 to 2013 in developing countries. Countries that have succeeded in raising revenues have also often used innovative mechanisms and experiments, including the use of lotteries, transparency initiatives, and new technology.

Nonetheless, in many countries, the capacity of tax collection and enforcement remains a concern. In particular, revenue administrations remain affected by under-resourcing,

[5] See UNTT Working Group on Sustainable Development Financing, 2013, The variety of national, regional and international public sources for development finance.

[6] Overall, studies of the incidence of government taxation and spending programmes are characterized by significant uncertainties, particularly in developing countries.

misallocation, and weak mid-level skills. To date, technical assistance to the revenue and customs sector has attracted a minimal share of ODA. In 2012 it is estimated that only $120 million of ODA from OECD DAC donors is targeted at tax-related activities, less than 0.07% of the total.[7] More focus could be placed in responding to national requests for strengthening fiscal management capacity and capacity building for domestic resource mobilization. In addition, examples of successful reforms can inspire policy design elsewhere.

- *International cooperation*

However, it is important to recognize that there are limits on what individual governments can accomplish on their own in the globalized economy. Illicit financial flows (IFFs) are particulalry problematic. The term IFF is characterized by a lack of terminological clarity, but it is generally used to convey three different sources: the proceeds of commercial tax evasion, revenues from criminal activities, and public corruption. IFFs have become a matter of major concern because of the scale and systematic adverse impact of such flows on the development and governance agenda. While improved domestic policies in tax administration are vital to increasing revenue collection for sustainable development investment, there is a limit to what they can achieve based on the existing international policy environment within which IFFs, as well

$1.9 trillion, primarily in developed countries.[8] Similarly, in agriculture, producer support subsidies among OECD members total $259 billion in 2012.[9]

On the policy front, some Member States have introduced more sustainable procurement policies, based on minimum environmental and social standards for public sector suppliers. A small number of countries have reduced or completely removed harmful and inefficient subsidies, such as fossil fuel subsidies. Only 27 per cent of the global population enjoys access to comprehensive social security systems, whereas 73 per cent are covered partially or not at all. Of particular significance are the divergent trends in richer and poorer countries: while many high-income countries are contracting their social security systems, many developing countries are expanding them.[10] To date 172 Member States are party to the United Nations Convention against Corruption.

- *Issues*

A central element of good financial governance is proper planning and execution of the budget. Generally accepted principles of good budgeting address the stages of formulation, approval, execution and audit. These principles should ensure that public spending is consistent with national sustainable development strategies, inclusive of environmental, social, economic, gender, and other goals. The Intergovernmental Committee of Experts on

tax and spending) to address inequalities, fight poverty, improve water and sanitation, and support other social services, in particular to benefit low income, vulnerable and marginalized

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It is common in normative budget policy discussions to ask if specific subsidies continue to be warranted. Countries should review the efficacy of all subsidies as a matter of sound fiscal

inefficient fossil fuel subsidies that encourage wasteful consumption by removing market distortions, in accordance with national circumstances, including by restructuring taxation and phasing out those harmful subsidies, where they exist, to reflect their environmental

specific needs and conditions of developing countries and minimize possible adverse impacts

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Structural vulnerabilities, which affect the poor and other socially excluded groups, women, persons with disabilities, indigenous peoples, migrants, minorities, children, older persons, youth and other marginalized groups, can be reduced by aiming for universal provision of

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[8] The IMF defines consumer subsidies to include two components: a pre-tax subsidy (if the price paid by firms and households is below supply and distribution costs) and a tax subsidy (if taxes are below their efficient level).IMF, 2013, *Energy subsidy reform lessons and implications*, Washington, D.C.

[9] OECD, 2013, *Agricultural Policy Monitoring and Evaluation*, Paris

[10] For more details please see ILO 2014, World Social Protection Report 2014/15: Building economic recovery, inclusive development and social justice.

[11] The Open Working Group agreement is based on the outcome of the Rio+20 conference. Reservations were expressed by several Member States to paragraph 225 of the Rio+20 outcome document, A/CONF.216/16, chapter I, resolution 1, paragraph 225 (see General Assembly 123rd plenary meeting, 2012, A/66/PV.123).