**Backgrounder**

**Aid to Domestic Revenue Mobilization**

**What is aid to Domestic Revenue Mobilization?**

Domestic Revenue Mobilization (DRM) is the process through which countries raise and spend their own funds to provide for their people. DRM not only provides governments with the funds needed to alleviate poverty and deliver public services (a critical step in the transition out of aid dependence and reaching the SDGs), but it can also strengthen the social contract between citizens and the state – which is essential for accountable, equitable and sustainable societies.

DRM has become a major discourse both at national and global level. Many countries, particularly African countries, are shifting their efforts towards enhancing both traditional and innovative mobilization efforts in the face of dwindling aid and unsustainable debt levels. The DRM Agenda was first mutated during Monterrey Consensus on Financing for Development in 2002, which emphasized the critical role of DRM for financing development complimented by foreign direct investment, international trade, ODA and Remittances. In 2014, at the First High Level meeting of the Global Partnership for Effective Development Cooperation (GPEDC), developing countries clearly endorsed the need for greater focus on DRM and called on donors to increase the amount of aid directed towards DRM from 1% to 2% per year[[1]](#footnote-1). In 2015, the Addis Ababa Action Agenda further reaffirmed the mobilization and effective use of domestic resources and underscored the principle of national ownership as being central to achieving the sustainable development goals. The Addis Tax Initiative (ATI) emerged as the international community’s shared responsibility and commitment to this end – with twenty of the world’s largest donors committing to double their annual aid to DRM, from $223.7m in 2015 to $447.5m by 2020 (ATI Commitment 1). In addition, 25 partner countries have joined the ATI committing to step up their own DRM efforts (Commitment 2), and agreed to DRM indicators to track progress in July 2019. Both donors and partner countries committed to policy coherence for DRM (ATI Commitment 3). The ATI Secretariat monitors and reports on all 3 ATI Commitments annually.

Bilateral donors have embraced DRM as an essential ingredient in their foreign assistance strategies going forward. Mark Green, USAID’s administrator, has emphasized DRM as the agency embarks on a new strategic vision to help recipient countries transition to greater self-reliance. However, DAC donors were still only allocating a total of $273m in support of DRM in 2017 (0.19% of total ODA). This marks an increase from 2015, but donors are still not on track to meet the ATI “doubling” commitment by 2020. Top bilateral DAC donors of aid to DRM were: 1. European Union ($ 69.46m); 2. USA ($42.38m); 3. UK ($37.85m); 4. Germany ($36.25m); 5. Australia ($15.46m), which accounted for 74% of total aid for DRM in 2017.

International financial institutions (IFIs) are also increasingly contributing towards DRM. The World Bank is the largest provider of development finance for DRM ($352m in 2016)**.**As of 2018, the World Bank was actively supporting 106 countries across the world to improve their DRM through numerous [operations](http://projects.worldbank.org/search?lang=en&searchTerm=tax). In 2016, the IMF committed to spend at least $105 million on DRM-related capacity development by 2018.

China, through south-south Cooperation, is also intensifying its efforts by providing large DRM projects for example $30m grant to Uganda[[2]](#footnote-2). Private foundations are also playing a complementary role, particularly in their support for civil society, journalists and other accountability stakeholders, which are key to accountable DRM systems.

**Why is aid to DRM important to Africa?**

African Governments reaffirmed their commitment through the African Union Agenda 2063 to consider DRM as a key development indicator and placed taxation at the center of financing continental development priorities. They committed to ‘putting mobilization of the people and their ownership of continental programmes at the core; the principle of self-reliance and Africa financing its own development; the importance of capable, inclusive and accountable states and institutions at all levels and in all spheres…’, and established ‘Strengthen domestic resource mobilization and build effective institutions’ as their first priority. Domestic Resource Mobilization is expected to contribute at least between 75% - 90% of financing of the Agenda 2063 on average per country[[3]](#footnote-3). Continental initiatives including the High-Level Panel on Illicit Financial Flows and the Planning and Coordination Agency of the NEPAD confirm African governments’ commitments to enhance DRM. Of the 24 partner countries which have joined the ATI, 16 are African.

Yet, most African countries’ capacity to raise such revenues through their collection of taxes is still low and stagnating. A study[[4]](#footnote-4) covering 26 African countries shows that in 2017, these countries unweighted average tax-to-GDP ratio was 17.2% (compared with an average of 22.8% in LAC and 34.2% in OECD countries). On average, the tax-to-GDP ratio in SSA is at ts lowest level in a decade, while debt levels have increased by 100% over the same period. In addition, the gross domestic saving in sub-Saharan Africa amounted to 17.6% of GDP in 2006 compared to 26% in South Asia and about 43% in East Asia and Pacific countries (World Bank, 2007). The low saving rate in sub-Saharan Africa explains the low level of economic activity in the region and the slow pace of growth. Other factors include the very low levels of financial intermediation and credit on the continent and the fact that over 40% of African savings are invested outside Africa. The challenge of mobilizing domestic taxes should be considered against the funds required to achieve the SDGs. [According to the IMF](https://www.imf.org/en/Publications/Staff-Discussion-Notes/Issues/2019/01/18/Fiscal-Policy-and-Development-Human-Social-and-Physical-Investments-for-the-SDGs-46444),  the funds required in five SDG areas (education, health, roads, electricity, water and sanitation) will grow to 15 percent of gross domestic product (GDP) by 2030, on average across low-income countries. But given the current development level, most of SSA will require more than an average of 15 percent of GDP.

Sub-Saharan Africa was the biggest recipient of aid to DRM in 2017 (46% of total ODA to DRM, an amount of $125m), receiving nearly 3 times as much as the second largest recipient, Asia (14%). Among the top aid for DRM recipients are Ghana ($11.74m), Kenya ($8.19m), Uganda ($6.93m), Tanzania ($5.18m), Zambia ($5.05m) and Tunisia ($4.26m).

Strengthening of DRM through aid in Africa is critical as it offers many potential benefits that will help towards financing the continent’s transformation agenda including infrastructure, agriculture, industrialization, and energy development geared towards lifting majority out of poverty. The following are some of the benefits for increased support to DRM generation:

* **Firstly,** it can help strengthen fiscal institutions because stable and predictable revenue facilitates long term fiscal planning which can help ensure that resources are allocated to priority sectors and are translated into outcomes.;
* **Secondly,** it is potentially the biggest source of long-term financing for sustainable development and it is the life blood of all state governance such as the provision of public goods and services. DRM will give African countries policy space which is often constrained under the terms and conditions of external resources providers and thus reinforces country ownership of their development processes;
* **Thirdly**, mobilization of domestic revenues for the provision of public goods can help to strengthen not only the legitimacy of the state but also deepen the social contract between governments and their citizenry;
* **Fourthly**, DRM will reduce the dependency on external flows and reduce vulnerability to external shocks and
* **Finally,** DRM can provide a holistic approach encompassing mobilization and prudent management of domestic public and private resources that includes participation of the wider society including Parliament, CSOs and communities among others and contribute to reducing the widening gap between the rich and poor.

**What are some key issues with aid to DRM?**

**An ambitious reform of global tax rules is essential to achieve full potential of DRM.** International tax rules and loopholes allow the richest companies and individuals to avoid tax, depriving governments from domestic revenue. Developing countries lose at least $170bn each year in foregone tax revenues from corporations and the superrich. Africa is currently losing more than $50 billion through illicit financial outflows[[5]](#footnote-5) per year (twice as much as the ODA it received last year). Over the last 50 years, Africa is estimated to have lost $1 trillion in IFFs, a total which is the equivalent of “all of the ODA received by Africa over the same time frame and is enough to wipe out the region’s total external debt of around $250 billion and still leave $600 billion for poverty alleviation and economic growth”. In addition, excessive exemptions and other tax incentive for foreign companies and donors are further depriving African government from revenue. The West Africa region alone is losing an estimated $9.6bn annually as a result of corporate tax incentives offered by governments to attract investors. Evidence, however, shows that such incentives significantly reduce domestic revenue collection and are not necessary to attract foreign direct investment, especially in a region like West Africa, as the dominant sector is the lucrative extractives industry. Most ATI donors have policies in place that enable such harmful tax practices, thereby giving aid for DRM while at the same time contributing to the capital flights from developing countries. It is irresponsible for donors to ‘offer’ developing countries aid to DRM to support the SDGs on the one hand, if they are not taking serious steps in parallel to mitigate this outflow of money and to change the global rules towards a fairer system where corporate taxing rights are set to make companies pay their fair share of taxes where they create real value and where they really operate. This is a matter of policy coherence. It is also crucial that African governments engage actively in negotiations on the reform of international tax rules which are taking place within the OECD-hosted ‘Inclusive Framework on Base Erosion and Profit Shifting (BEPS)’. Donors should also be supporting their capacity in creating the political conditions to play such a role, on real and effective equal footing.

**Levels of aid to DRM are still woefully low (0.19% of total ODA in 2017).** Donors are increasing their support to DRM, but they are not on track to meet their commitment to double support for DRM. Perhaps more important is how aid for DRM is increasing: the majority of increased aid has gone to DRM related trust funds at the IMF, World Bank and OECD – less so directly to partner governments.

**Donors are mainly focusing their attention on using aid to leverage ‘more’ DRM, rather than ‘more equitable’ DRM.** Donors are primarily focused on implementing technical and administrative reforms with the aim to increase the capacity of tax administrations and overall revenue collection (e.g. training and use of new ICT systems), instead of focusing on support to build fair revenue systems. In particular, an Oxfam study[[6]](#footnote-6) shows that:

* A commitment to equity is absent or unclear in most DRM projects. In 2016, just 2.8 percent of total projects (18 of 634) contained clear goals on equity or fairness.
* Gender equity is largely neglected. In 2016, only 0.5% (less than 1 percent) of DRM project descriptions actually indicate any gender related objectives.
* Country ownership is far too weak, with only 16 percent of aid for DRM is channeled to domestic stakeholders.

Aid to DRM needs to shift away from supporting narrow technocratic reforms, and instead focus on addressing the underlying challenges countries face in building fair revenue systems. These include excessive tax incentives for corporations and investors, a lack of taxes on wealth and assets (such as property and capital gains taxes), and failures of transparency, accountability and citizen trust in public institutions. Donor support should help ensure that the pressure to increase domestic revenue in the short-term doesn’t trigger poor policy decisions — e.g. squeezing the poorest through quick rate hikes or creation of new taxes. Instead, donors should support country-led efforts to achieve a more equitable composition of revenue, where reforms lead to more revenues, with a greater percentage of that revenue being derived from progressive taxes (e.g. direct taxation) and sustainable revenue sources, and less from regressive taxes (e.g. consumption based taxes such as value-add tax (VAT), which hit poor households and women the hardest). This is particularly important in sub-Saharan Africa, where higher tax collections in SSA have been driven primarily by rising revenues from VAT (which constitutes on average around one-third of total tax collections in SSA), despite lower revenues from taxes on international business operations. In the 26 African countries covered in the study mentioned above[[7]](#footnote-7), the greatest source of tax revenues were taxes on goods and services, which accounted for 53.7% of total tax revenues on average in 2017, with VAT alone contributing 29.4%. Taxes on income and profits accounted for 36.2% of tax revenues.

**Shrinking space for Civil Society.** Tax reform is not simply a technical matter, it is political – which means strong civic space is an essential ingredient for pro-poor and sustainable tax reform. The OECD acknowledges that ‘much of the focus on DRM has been on international tax policy and building the capacity of tax administration’, while ‘in contrast, understanding and improving tax morale has been relatively neglected’[[8]](#footnote-8). Tax morale, defined as the intrinsic motivation to pay taxes, relies on the fiscal contract and trust in government on taxation, which in turn requires government to be held accountable through ‘transparent budgeting, courts, civil society and media’. Without accountability for how revenue is raised and spent, increasing domestic revenues can actually exacerbate inequality and poverty. Civil society can play a critical role in helping to strengthen the effectiveness of fiscal policy for its expenditure and how this will impact on different groups in society. It is therefore of huge a concern that the space for citizens and CSOs to play this role is shrinking rapidly across the world (see backgrounder on CSO enabling environment).

**What could the main priorities for the DAC-CSO Reference Group on aid to DRM?**

Work led by the OECD, under G20 mandate, on the reform of the international tax system (the Base Erosion and Profit Shifting (BEPS) reform) is conducted by the OECD Committee on Fiscal Affairs (CFA), not by the Development Assistance Committee (DAC). CSOs have been engaging with the OECD on tax issues in recent years, including with other regional CSO platforms and together with ICRIT (a commission of independent and well recognized experts to reform the corporate income tax system, and including names like Joseph Stiglitz or Irene Ovonji) and through the [BEPS monitoring group](https://www.bepsmonitoringgroup.org/), a group of independent researchers and policy advisors in CSOs focusing mainly on BEPS at a technical policy level – not focused on aid to DRM.

In parallel, the OECD has a work stream on ‘tax and development’ (which includes aid to DRM, Tax Inspectors Without Borders, etc.) and is meant to report to and inform the work of both committees, the Committee on Fiscal Affairs and the Development Assistance Committee. A [Tax and Development Task Force](https://www.oecd.org/tax/tax-global/tax-and-development.htm) brings together OECD member countries, emerging and developing countries, international and regional organisations, civil society and business to discuss current tax and development issues facing developing countries. The stated goal of this Task Force is ‘to take action to improve the enabling environment for developing countries to collect appropriate and adequate tax revenues and to build effective states’.However, since the emergence of the Platform for Collaboration on Tax (UN, OECD, WB and IMF), the role of the task force has been less regular. To date, the DAC-CSO Reference Group does not have a specific working group to influence the DAC’s work on ODA to DRM.

In a nutshell, CSOs engaged in these spaces have been focusing mainly on the OECD CFA as a target, rather than on the DAC itself. Yet the DAC has a specific role to play here, including through the production of annual ODA to DRM statistics (which some argue could be improved[[9]](#footnote-9)), and through recommendations and guidelines on how DAC donors should be spending their ODA. In particular, CSOs could advocate for the DAC to pursue the following areas:

* As donor increase DRM, the DAC should encourage donors to end reliance on IMF, WB and OECD trust funds – and to start investing more in Regional Tax Organizations (like ATAF or CIAT), but also UN tax trust fund (which gets support from only India and Norway as of now).
* DAC guidelines for supporting civil society, specifically how donors can strengthen support (financial and non-financial) for civil society working on tax/DRM at national level (as of 2017, very few resources channeled to CSOs for DRM work)
* DAC guidelines for how to improve support for subnational/local governments that have revenue mobilization authority in national decentralization laws.
1. See *http://www.oecd.org/development/effectiveness/globalpartnership.htm* [↑](#footnote-ref-1)
2. On November 6, 2017, the Government of the People's Republic of China agreed to support Uganda's customs modernization project with a grant worth $30 million. AllAfrica. Accessed at: http://allafrica.com/stories/201711070105.html [↑](#footnote-ref-2)
3. AUC Agenda 2063, <https://www.un.org/en/africa/osaa/pdf/au/agenda2063-first10yearimplementation.pdf>. Note that in this context, DRM refers to “resources” that can finance the Agenda 2063, which includes more than 20 different types of resources, of which tax/non-tax revenues are one. [↑](#footnote-ref-3)
4. ATAF, AUC, OECD, Revenue Statistics in Africa 2019, <https://www.oecd.org/tax/tax-policy/brochure-revenue-statistics-africa.pdf> [↑](#footnote-ref-4)
5. Report of the High Level Panel on Illicit Financial Flows from Africa, <https://www.uneca.org/publications/illicit-financial-flows> [↑](#footnote-ref-5)
6. Oxfam, 2018, Doubling Down on DRM, <https://www.oxfamamerica.org/static/media/files/DOUBLING_DOWN_ON_DRM_-_2018_LVC7aXc.pdf> [↑](#footnote-ref-6)
7. ATAF, AUC, OECD, Revenue Statistics in Africa 2019, <https://www.oecd.org/tax/tax-policy/brochure-revenue-statistics-africa.pdf> [↑](#footnote-ref-7)
8. OECD, 2019, Tax Morale, What Drives People and Businesses to Pay Tax? <https://www.oecd.org/tax/tax-morale-f3d8ea10-en.htm> [↑](#footnote-ref-8)
9. Development Initiatives, 2018, ODA for DRM, <http://devinit.org/post/oda-for-domestic-revenue-mobilisation/> [↑](#footnote-ref-9)