

STRUCTURAL TRANSFORMATION  
AND THE CHALLENGE OF  
**FINANCING**  
**AFRICA'S**  
**POST-2015**  
DEVELOPMENT  
AGENDA

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Empowered lives.  
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THIS PAPER IS A SYNTHESIS OF DELIBERATIONS BY A GATHERING OF AFRICAN THINKERS, PARLIAMENTARIANS AND CIVIL SOCIETY ORGANISATIONS, HOSTED BY THE PAN-AFRICAN PARLIAMENT BASED IN MIDRAND, SOUTH AFRICA.

THE PURPOSE WAS TO DEVELOP A SHARED NARRATIVE OF WHAT THE POST-2015 DEVELOPMENT AGENDA SHOULD ADDRESS IN THE AFRICAN CONTEXT.

THE MEETING ARTICULATED WHAT IS EMERGING AS A GROWING CONSENSUS ON THE CONTINENT WHICH IS THAT, TO END POVERTY AND SUSTAIN IT IN THE POST -2015 ERA, 'THE BUILDING BLOCKS OF DEVELOPMENT' HAVE TO BE FRONT AND CENTRE.

IN THE AFRICAN CONTEXT THIS HAS TO BE UNDERPINNED BY DEVELOPMENTAL/STRUCTURAL TRANSFORMATION AND THIS PROCESS SHOULD IN TURN INFORM THE APPROACH TAKEN TO ISSUES OF GOVERNANCE (DEVELOPMENTAL GOVERNANCE), FINANCING, GLOBAL DEVELOPMENTAL PARTNERSHIPS, AND ANY SOCIO-ECONOMIC DEVELOPMENT GOALS AND TARGETS THAT ARE INTERNATIONALLY AGREED.

# O

## INTRODUCTION

The Millennium Development Goals (MDG) agenda helped to focus the world's attention on the importance of explicitly concentrating on and channelling resources to poverty reduction and various dimensions of social development. In Africa, this was against the backdrop of structural adjustment and 'development as usual' policies which had not only failed to deliver human development outcomes, but also resulted in reversals in a number of countries. The failure of development on the continent meant that the financing of the poverty reduction effort became increasingly dependent on international resources, in particular: development assistance, international debt and skewed forms of private capital inflows. These, by themselves, were not only inadequate, but proved to be unsustainable and in some cases damaging to the long-term development effort.

Therefore, whilst the MDGs undoubtedly helped to save lives and brought other gains, in the context of the post-2015 development framework, it is clear that there needs to be a focus on developmental transformation. This encompasses the structural transformation of Africa's political economy, including developmental governance, environmental sustainability and equitable development- as the building blocks for sustainable human development. Structural transformation is particularly crucial if Africa were to adequately manage the impacts of its vulnerabilities and those imposed by the international political economy. Structural transformation is both a goal and a necessity to adequately finance, achieve and sustain developmental goals in the African context.

There needs to be a focus on developmental transformation that encompasses the structural transformation of Africa's political economy, including developmental governance, environmental sustainability and equitable development- as the building blocks for sustainable human development

<sup>1</sup> This meeting took place in Midrand, South Africa on 24th- 27th February, 2013 and was jointly organised by the Pan African Parliament, the United Nations Millennium Campaign, UNDP, ACORD, Tax Justice Network-Africa, Third World Network-Africa and Christian Aid. There was expert participation from UNECA, the African Union and African Futures.

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# 1

## STRUCTURAL TRANSFORMATION IN THE AFRICAN CONTEXT

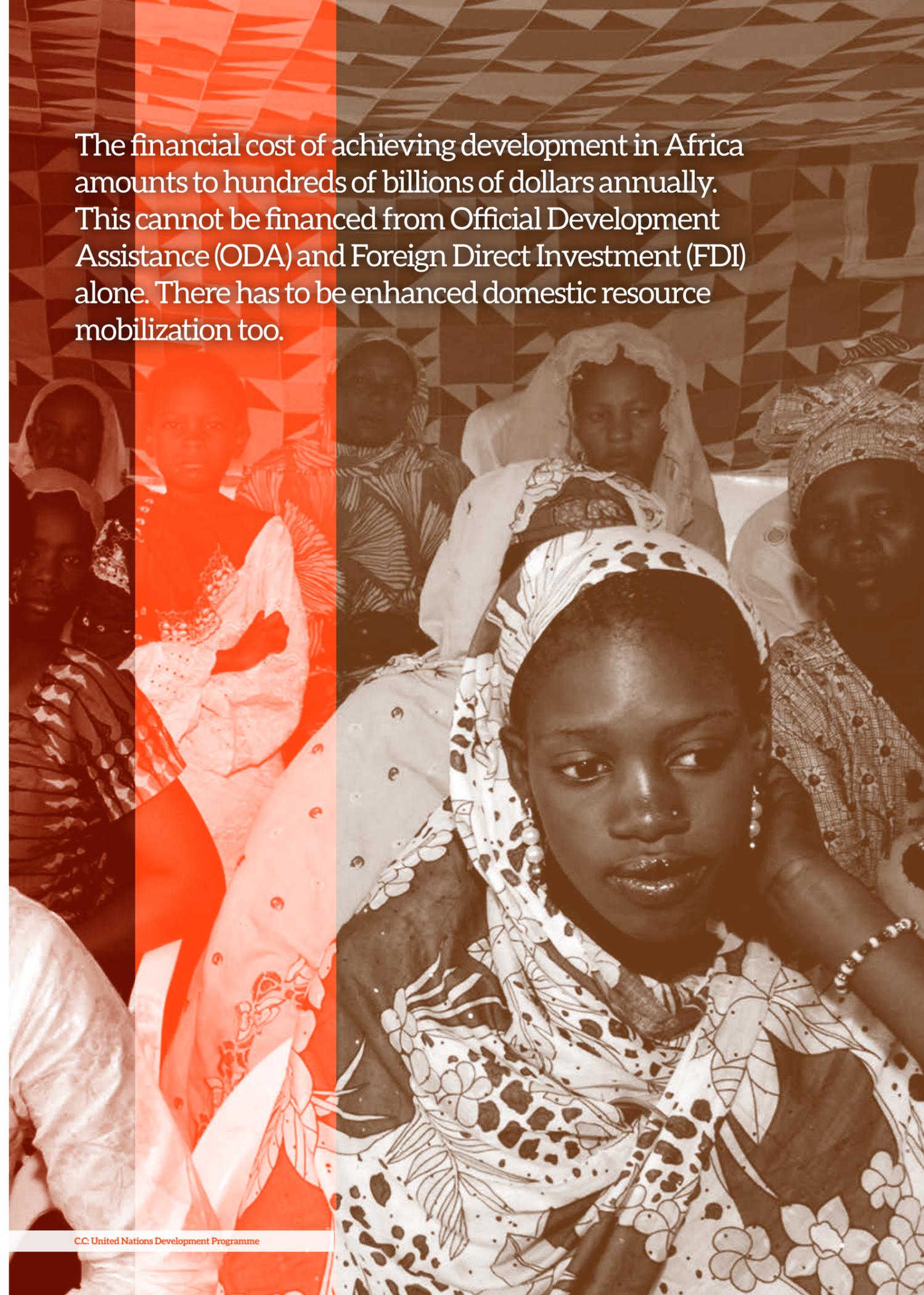
The priority that is being assigned to structural transformation has to be understood within the context of Africa's historical position in the global division of labour, largely as an exporter of raw materials and natural resources. Its economy and social structures are rooted in the production and exports of low value, diminishing returns goods. This role ties Africa's fortunes to the volatility of the primary commodities' market and the political whims of aid providers. The low value addition explains the paradox of: high Gross Domestic Product (GDP) growth, alongside poor human development; expanding volumes of natural resource exports that goes side by side with Africa's diminishing value share in global trade; and explains the inability to finance social development and the lack of diversity and capacity in its economic and social institutions.

Africa's desire for an agenda which addresses transformation is also derived from its recent experience with Structural Adjustment Programmes and the MDGs. Although the latter helped to bring needed attention to absolute poverty, it did little to address Africa's dependence. Indeed, implemented within the framework of the Poverty Reduction Strategies of the International Financial Institutions, the MDGs may have inadvertently contributed to entrenching Africa's dependence on primary commodity exports and low-value added and low productivity agriculture, resulting in the expansion of Africa's dependency on aid, food and even external policy advice over this period. Africa's inability to finance its development from its own resources also contributed to weakening its voice in the international political arena.

The call for economic transformation in Africa derives from the need to put an end to the perverse process which transfers Africa's wealth elsewhere, thereby perpetuating misery and endangering the very survival of the continent's population. Only an Africa with transformative socio-economic development will avoid the unattainable imitative development path and promote sustainable development in a resource constrained world.

*The MDGs could not have made progress without significant financing. The financing needs for post-2015 should be adequate, predictable, sustainable and integrated. These characteristics are intricately linked with successful structural transformation.*

The financial cost of achieving development in Africa amounts to hundreds of billions of dollars annually. This cannot be financed from Official Development Assistance (ODA) and Foreign Direct Investment (FDI) alone. There has to be enhanced domestic resource mobilization too.



## WHAT DO WE MEAN BY STRUCTURAL TRANSFORMATION?

### 1.1\_

The first task of structural transformation in the African context is the transformation of the system of “production” from one dominated by primary extraction and low value-added agriculture and services, to one in which high value is added through the application of technology, innovation, beneficiation, better linkages between sectors in the wider economy and a fairer share of natural resource rents. Africa’s transformation fortunes rest heavily on how natural resources – the extractive sectors in particular – and agriculture are managed and transformed. The Africa Mining Vision and the Comprehensive Common Agricultural Programme adopted by the African Union (AU) provide road maps in this direction. But transforming these sectors requires technology, innovation and a healthy and educated workforce living in freedom. Economic transformation is therefore inextricably linked to the social conditions of society.

Structural Transformation should be a Post-2015 goal. This means economic, political and social change to support sustainable, long-term development.

Successful transformation will over time result in the reduction of the share of relatively dominant sectors of today (agriculture and raw minerals/fossil fuels) in the economy, relative to manufacturing and value added services. The ultimate measure of successful economic transformation is a mixed (small, medium and large enterprises) and balanced, economy. Such an economy will put money, wealth and capability in many hands, thus contributing to further progress and the financing of public goods through enhanced taxation and consumption of goods and services.

The ultimate success of social transformation is that a transformed economy is creating and financing a better life for all people (men and women, children and elderly, physically abled or disabled), ensuring universal access to essential services, providing additional social protection for the poorest and weakest in society and ensuring an equitable, peaceful and harmonious society.

In technical terms, four essential and interrelated processes define structural transformation in the economy: a declining share of agriculture in GDP and employment; a rural-to-urban migration underpinned by rural and urban development; the rise of a modern industrial and service economy; and a demographic transition from high rates of births and deaths (common in underdeveloped and rural areas) to low rates of births and deaths (associated with better health standards in developed and urban areas). Economic and structural transformation is also associated with rising agricultural productivity, an integrated economy and rising per capita growth rates. It will require, among others, the full and effective implementation of the African Common Market, the African infrastructure strategy and other regional integration agreements, to achieve transformation as described above. Therefore, in relation to the post-2015 development agenda, it will be important for Africa that a Goal on “structural transformation” be established which can be measured and tracked by the indicators outlined above. Issues such as the intra-regional portion of Africa’s trade and progress in infrastructure development are important measures of development “enablers”.

*Economic growth should be inclusive and equitable, with regard to narrowing the disparities between rich and poor and those that relate to access to basic services, spatial as well as social dimensions of differentiation such as gender, age, disabilities, ethnicity, religion or race. Narrowing economic inequalities at the global level is crucial to create the conditions for narrowing inequalities at the national level, given that global inequalities are larger than intra-country inequalities.*

Economic and structural transformation is also associated with economic growth which is both inclusive and sustainable. Economic growth is inclusive if its benefits are fairly distributed in vertical terms (between the poorest and richest households, wages and profits); in spatial terms (between geographic regions) and in terms of demography (age composition of society and other societal identities such as gender, religion, and other socially excluded groups). Economic growth is sustainable if it is equitable in terms of impacts as described above, and if it uses natural resources, including energy, fisheries, water, forests, soils and biodiversity resources sensitively, and if growth does not suggest insatiable and wasteful consumption. *To this effect, a goal related to economic growth must be qualified, and tracked, by its distributive impacts as outlined above.*

## THE ROLE OF THE AFRICAN STATE IN THE TRANSFORMATION EFFORT

### 1.2\_

Structural transformation also pre-supposes a transformed relationship between state and citizens. Except for the brief period in many African countries following de-colonisation, the experience of political governance has been largely negative, fraught with corruption and nepotism, human rights violations, military or one-party dictatorships and poor stewardship of the economy. The African political elite have largely been more accountable to external powers – political and big business – through aid dependency, commodity export dependency, and outright political and military interventions by external powers. The period of structural adjustment programmes, spanning two-three decades – exacerbated this growing distance between people and governments, by diminishing the role of the state in the direct provisioning of essential public services to the poor, by trimming the state down and weakening its capability to serve the people including peace, security and democratic accountability and by deepening inequalities that contribute to tearing the society apart.

A post-2015 agenda must be based on new relationships of accountability between people and state, rooted in a focus on participatory democracy, service delivery, human rights, the accountable use of public resources, social protection of the weak and poor, gender equality and better economic governance.

*The Post-2015 agenda for Africa should primarily be drawn up in Africa, by Africans, for Africans.*

The pathways for these challenges have already been defined in Charters, resolutions and programmes agreed to by African Heads of State and Government, in the context of the African Union. These include: the African Charter on Human and People's Rights; the Protocol to the African Charter on Human and People's Rights on the Rights of Women in Africa; the African Charter on Elections and Democracy; the New Partnership for Africa's Development (NEPAD); and, the African Peer Review Mechanism (APRM), among others. A successful post-2015 agenda must be consistent with the principles and programmes contained in them, and require their full implementation. In this context, Africa must include in its monitoring framework for a post-2015 development agenda, indicators of implementation of common programmes, agreements and Charters that African governments have voluntarily agreed to. This is an important accountability framework for regional integration and political accountability at the cross-boundary level.

There must be a paradigm shift in the relationship between the African state and the international community. The international community must trust and respect Africa's ability to put its own house in order.

## 1.3\_ THE NEED FOR A PARADIGM SHIFT

The relationship between the African state and the international community must equally undergo transformed change, one that is rooted in the principles of equality of nations and peoples; mutual collaboration for mutual interest and respect for the ability and right of Africans to lead their own change. But for this to happen, Africans must understand that they need to put their own house in order: rely less on aid, use their own resources properly, ensure a fairer share of natural resource rents, and rely more on mobilising, retaining domestic resources, including through effective taxation and the plugging of illicit financial outflows and take steps to manage FDI for development.

To this effect, Africa must include, in its post-2015 monitoring framework, indicators to track progress towards natural resource beneficiation; natural resource rent sharing; tax systems, structures and share of tax revenues to GDP, indicators of capital flight and other such measures. These are important building blocks for Africa's voice in global partnerships.

These realities suggest that a post-2015 agenda must represent a paradigm shift: a shift from a culture of dependence on external resources and leadership, to one of greater reliance on domestic resources and capable institutions; a shift on the understanding of governance from one dominated by narrow ideas of "good governance" emphasising electoral politics and a lean and non activist state making room for the market, to one that understands the intricate links between governing the economy (for structural transformation), governing the social and political system (for human development and individual freedoms) and governing the natural environment (for sustainability). The task, as defined by the African Union, is to build "democratic developmental states". Transparency and accountability are key for development and vibrant states.

Partnerships between Africa and the rest of the world for post-2015 must be based on this paradigm – the fashioning of capable states built on, and building, capable economies, upon which sustainable development is financed and achieved. International partners can help by reshaping the unfair rules that govern the flow of global trade, finance and technology so as to make it more conducive for Africa to achieve the transformative shifts described above. The elements of these reforms are described in the last section of this narrative.

# 2\_

## FINANCING TRANSFORMATIVE CHANGE IN AFRICA POST-2015

The scale of resources needed to finance an ambitious post-2015 sustainable development agenda will no doubt pose a daunting challenge to align expectations with implementation. The financing issue could also make or break any agreement on a new agenda, especially in view of the disappointing outcomes of MDG 8 which speaks to international partnerships, including financing and technology transfer. Given that Africa has been the most dependent on foreign sources to finance its development over the past three decades or so, it is crucial that Africa, takes the lead in putting forward its ideas about how the financing issue should be addressed. It was in this context that the Midrand gathering devoted two days of discussion to the issue.

The meeting reflected an emerging consensus on the continent, which is that the financing question and that of the organization of the economy and the state are interlinked. Consequently, there is an imperative to strengthen and realign the focus of state activities towards an orientation of a **developmental and capable state** in regard to the mobilization and expenditure of resources; that the different sources of finance while additive at one level, also impact one another at others. Further, the issues of financing and development partnerships cannot and should not be divorced from policies aimed at system-wide sustainability, resilience and a pro-active focus on developmental priorities to mitigate the growing financialization of our economies.

Proposals for financing and development partnerships should be assessed from three perspectives: first, from the point of view of evidence discernible from recent trends for the different financing modalities; second, from a political economy perspective as regards state-citizen relations and accountability; and, third, from the point of view of their contribution to economic, social and sustainable development-related transformational agendas for the continent. There is a well-documented push for greater reliance on domestic resource mobilization, principally through identifying how the tax base can be expanded further as well as staunching underpayment, illicit transfers, licit transfers through transfer pricing negotiated subsidies etc. There is also a real need for more creative models of financing in which public finance (domestic and foreign) leverages private finance for productive, value-adding, investments.

## 2.1\_ THE SCALE OF THE RESOURCE NEEDS

The resources needed to finance a post-2015 sustainable development agenda of zero extreme poverty, where no one is left behind, under conditions of minimal social disparities and environmental damage will be immense. There needs to be adequate investment in estimating the resource needs in a transparent and inclusive way. By transparent is meant that all the assumptions underpinning estimates and projections are known and subject to debate. We need to learn the lessons of the Monterrey financing agenda and start the process of generating these figures sooner rather than later to feed into informal and expert dialogues.

Whilst we do not know in certainty what the resource needs will be to achieve an ambitious development agenda that leaves no one behind, the estimates for climate financing give a clue. The World Bank estimates the global mitigation and adaptation costs to be in the region of between \$520bn-840bn annually. In relation to Africa, the estimates for adaptation costs alone range from \$30bn-\$50bn annually. Add to this figure, the cost of arresting desertification, species depletion, water resource depletion and pollution as well as the cost of providing universal access to basic services, social protection, fulfilling human rights and peace and security and infrastructure for regional integration (energy, railways, roads, water resources etc.), among others. The additional annual cost for filling Africa's infrastructure financing gap alone is estimated as \$31bn, at the minimum. If we factor in current spending in these areas, we are talking about hundreds of billions of dollars annually for Africa alone.

It is not realistic to expect such a scale of financing to be met by international development assistance, philanthropy or even private commercial capital by itself. This calls first and foremost for enhanced domestic resource mobilisation based on growing and diversified economies delivering decent incomes, higher aggregate savings and larger tax revenues. Functioning economies and larger domestic savings will also create the space to leverage foreign capital on terms that are development and environment friendly. This underscores the point that effective financing ultimately rests on transformed economies on the back of, and re-enforcing, democratic developmental states.

Whilst external resources remain essential for Africa's development, if care is not taken in its pursuit, the African state can be undermined. This can happen if the conditions attached to attracting them lead governments to prioritize accountability to external providers over their citizens and when they undermine the tax system that underpin mutual accountability between state and citizen. The 'race to the bottom' is one example where countries compete for foreign capital by offering low taxes and tax concessions thereby undermining their tax systems.

## 2.2\_ THE ROLE OF THE STATE

A capable state is, among others, one that has strong and well-resourced institutions, including those that design and implement effective regulatory systems that guide trade and finance (private and public) into development impacts. A capable state is also one that has strong legitimacy among its people through the services it provides, including the rule of law, peace and security. A capable state regulates the economy so as to re-direct incentives in favour of value-added activities as opposed to un-productive rent-seeking ones and in this process the economy becomes more balanced, more resilient and more competitive. A capable state in the African context is a **democratic developmental state**. A capable state is essential for the mobilisation of tax revenues, for counter-cyclical macroeconomic policies to protect growth and wellbeing in times of economic downturns and for the proper regulation of capital flows for development. These are all central to a sustainable financing agenda.

*Government accountability should be a Post-2015 goal: the goal should honor the work done by the AU and African heads of State and Government, requiring that their principles and programs be implemented.*

A capable state is also dependent on a capable economy. By a capable economy is meant one that is growing, diversified (through value addition) and balanced, in the sense of: (i) a better mix of different sizes of enterprises (small, medium, large) feeding into each other and, (ii) largely owned by the local private sector or the state or the mix of both, and (iii) distributes the benefits of growth fairly. Such an economy is more likely to be jobs-intensive and able to spread opportunities, incomes and wealth more broadly. Such an economic structure is best suited for growing and sustaining the tax base and revenue pot without undermining the incentives for investment, re-investment or even necessary consumption. With an Africa-wide nominal Gross Domestic Product (GDP) approaching US\$ two trillion per annum, a two per cent growth rate puts in an extra US \$40 billion into the economy. Similarly, significant resources can be mobilised for investment by increasing the value of exports.

A capable state is also a legitimate one. How legitimate the African state is in the eyes of its people cannot be divorced from its historical relationship of dependency on foreign finance. This relationship has created a number of challenges. The first is the so-called dual constituency problem. By this is meant, the tensions between satisfying donors and global corporations on the one hand, and accounting to and satisfying the electorates on the other. Over the past three-decades or so, accountability to the external, has trumped accountability to the electorate.

The second is the tension between a focus on the mobilisation of domestic resources and the attraction of foreign capital, including Foreign Direct Investment (FDI) and Official Development Assistance (ODA). The evidence suggests that over the past three decades or so, policies and actions have prioritised the foreign over the domestic, and that foreign capital inflows may have been attracted at the expense of the mobilisation of domestic resources in Africa. Cases in point are: the so-called "race to the bottom" policies in which extensive tax and other concessions are provided to attract foreign capital, with dire impact on the tax burden; and, the illicit financial outflows phenomenon - in which more resources are lost than attracted, through tax avoidance and evasion strategies, using profit shifting in international pricing and tax havens and secrecy jurisdictions to hide wealth from taxation and re-investment.

The third challenge is the tension between a short-term and narrow approach to domestic financial sector development (the focus on commercial banks), and the attraction of short-term external capital (focus on loans, aid and portfolio flows) at the expense of building institutions for long-term capital formation (e.g. pension funds and life insurance or even development banks which were set up in the past to absorb that which private banks cannot) and productive FDI.

The fourth challenge is the dichotomous approach to the relationship between public and private finance. This challenge is at three levels. First, is the virtual demise (except in some countries of Southern Africa and recently Ethiopia) of development banking essential for medium-term credit to the productive sectors in the false belief that banks are the preserve of the private sector alone. Development banks are better placed to fill the credit gap especially where risks in the productive sectors may be too high for commercial banks. Boosting production is Africa's core need. The second is the missed opportunity for private and public sources of capital to leverage each other and in that process not only expand volumes of capital but transform its nature to suit the needs of production-based economies. The third, which follows from the second, is the missed opportunity to channel international public finance such as those from international financial institutions in a manner so as to complement national development finance for development.

Given the above, Africa's key challenges going forward in the post-2015 era should include: (i) maximising the mobilisation of domestic resources especially through taxation (ii) tackling illicit outflows of capital (iii) taking steps not only to harness foreign resources to complement domestic resources, but also to manage foreign inflows in order to maximise their positive impacts and minimise their negatives (iv) taking steps to ensure that a domestic capital market thrives in support of the transformation agenda (v) ensuring a fairer share of natural resource rents and maximisation of the benefits of natural resources (vi) harnessing the complementarities between private financial flows and development banking (vii) advocating for the reform of the global systemic issues that constrain Africa from harnessing adequate resources for its development.

African leaders must take full responsibility for their development, rely less on aid and use their resources properly, ensure a fairer share of natural resource, retain more of their domestic resources for development - including plugging illicit financial outflows.



UN Photo/Eskinder Debebe  
Secretary-General Addresses African Union Summit

## 2.3 MOBILIZING DOMESTIC RESOURCES FOR DEVELOPMENT - THE ROLE OF TAXATION:

### A\_ POTENTIAL

Tax is already the biggest source of public finance in developing countries. African governments, for example, raise over ten times more revenue through taxation than through aid.<sup>2</sup> Even if only the "low hanging fruits" in terms of simple steps to improve revenue collection are taken, the result is likely to be significantly increased public resources.

This is borne out by a brief study of recent trends in tax revenue in low and lower-middle income countries. A simple average across those countries for which sufficient data is available during the years 2002-9 shows an average annual increase in the tax to GDP ratio during this time of 0.23 percentage points. In a few countries the ratio fell; if we exclude these, the annual increase rises to 0.44 percentage points. If this latter figure is a reasonable estimate for the potential increase that could be achieved through a concerted effort across all low and lower-middle income countries, the result would be a year-on-year increase in public revenues of US\$22.5 billion.<sup>3</sup>

As ODA declines and FDI becomes increasingly volatile and concentrated, taxation will become even more important for the provision of services and public investments generally. If all African countries raised just 15 per cent of GDP in revenue, the continent's governments would have an additional US\$200 billion at their disposal annually. The potential of taxation as part of the post-2015 settlement is therefore evident. The key challenge is to take steps to increase the tax to GDP ratio.

*The potential for raising resources through domestic taxation is huge.*

A recent study showed that a 0.44% increase per annum in the Tax/GDP ratio could raise additional public revenues of US\$22.5 bn on a year by year basis. Therefore the key challenge is to increase this ratio.

<sup>1</sup> African Development Bank, OECD & UNECA, 2010: *African Economic Outlook 2010*

<sup>2</sup> Data from <http://worldbank.org/>; latter figure is based on 2011 GDP.

### TAXATION IS AT THE CORE B\_ OF DEVELOPMENT

Taxation is central to transforming the relationship between state and citizen

It would be a mistake to view the tax agenda as solely about raising money – it is in the process of raising money that accountability is strengthened and the state apparatus is built. The true priorities of policies are often revealed more clearly by budgets and tax legislation than they are by declarations and action programmes. And governments ultimately become responsive to their biggest funders. Here, increasing tax revenue and its responsible management is crucially linked to transparency of revenues and budgets – disclosed in a format that citizens can understand.

Taxation is a potent tool for addressing inequalities

We live in a world where the top 20 per cent of the global population enjoys more than 70 per cent of total income. Inequality of outcome becomes inequality of opportunity for children. A child in the richest 10 per cent of households has on average 35 times more effective income available to meet their needs than the income of a child in the poorest 10 per cent of households. Taxation enables the state to:

- Ensure universal access to good quality basic goods and services- food, housing, water, health services, education and social protection;
- Improve revenue collection from sectors and agents that have benefited disproportionately from aggregate income growth.

Taxation is a policy tool for promoting "green growth"

Sustainable economic transformation will require shifting economies towards valuing environmental resources. Taxes can dis-incentivize the use of goods and services, with social and environmental costs – this revenue can be used to invest in green growth.

In summary, the role of taxation in development can be summarised as in 4 'R's.

- **Revenue** – to provide funding for basic services;
- **Representation** – strengthening the relationship between state and citizen;
- **Redistribution** – challenging inequality through progressive taxation and provision of social safety nets; and,
- **Re-pricing** – increasing the cost of goods and services which do not reflect social and environmental externalities.

### THE ROLE OF TAXATION IN DEVELOPMENT CAN BE SUMMARIZED AS THE 4 'R'S.



## THE CHALLENGES AND OPPORTUNITIES FOR TAXATION IN THE C\_ POST-2015 AGENDA:

### CHALLENGE 1:

#### Maximising the benefits of natural resources

As mentioned earlier, the key to Africa's failure or success in transforming its economies and societies lies in how natural resources, are managed. Natural resources, especially minerals and petroleum have been the main source of economic growth over the last decade. Export of commodities have been the main source of foreign exchange, and in the petroleum and agricultural sector, the main source of revenues. Commodities, if properly managed, could lead Africa's industrialisation effort, thereby further expanding the tax base in several respects. However, Africa is yet to maximise its share of natural resource rents, by securing a fair share of tax revenue from profits made in the sector by largely foreign - owned companies, or add significant value to its raw materials. The African Mining Vision developed through the leadership of the African Union with the support of UNECA, the African Development Bank and African civil society actors is a step in the right direction. The African Minerals Development Centre being established to promote the goals of the Vision will require political and technical support to succeed.

### CHALLENGE 2:

#### Matching tax potential to revenue need

There is certainly potential to raise more tax revenue in every country, subject to the various trade-offs. But that potential varies from country to country. Potential corporation tax revenue from policy reforms depends on the size of a country's private sector, the diversity of that sector and its actual and potential levels of inward investment or re-investment of profits. These depend in part

on factor endowments, the degree of economic diversification and the policy environment.

A paper from the OECD Development Centre in 2011 compared the public resources needed to meet the Millennium Development Goals (MDGs), against a simple measure of each developing country's 'tax potential'. "Although at the global level the magnitude of potential additional resources available from improved tax collection is similar to that of the additional resources needed to achieve the goals," it concluded, "on a country by country basis substantial external resources will still be needed."<sup>4</sup> Such countries are likely to be low income countries, countries emerging from, or embroiled in, conflicts and countries with less diversified economies.

### CHALLENGE 3:

#### Raising revenue in a progressive way

In an ideal scenario, African countries would increase their domestic revenue through progressive taxes that have little or no incidence on the poorest and significant incidence on the richest. Special attention would be paid to the gendered impact of tax reforms: the fiscal system wouldn't be gender neutral, it would redistribute income from men to women to compensate for the opposite effect in the economy and society at large. There are of course complex conceptual and practical questions behind these assumptions.

One of these is the concept of progressivity of taxation. We use this term in its simplest form to apply to the principle that "the more a person earns, the more tax they should pay". This principle should be applied broadly enough to ensure that those with immense wealth (e.g. idle non-taxed landed property which has not been transformed into income), are not let off. There is also the issue of where progressivity matters most? According to the IMF's Mick Keen, "[w]hat ultimately matters...is the distributional impact of the full tax-spending system," not that of individual taxes or even of the tax system as a whole.<sup>5</sup> According to this logic, it's OK to tax regressively if you spend progressively; but not everyone would agree. Given the degree of income and wealth inequalities in many African countries, the least we can apply the principle

is that, the poorest people should, by necessity, not contribute more than the rich, relative to their incomes, even if they receive more in expenditure incidence, especially if reducing inequalities sharply is a policy objective. These complexities notwithstanding, it is sufficient progress in an increasingly unequal world where wealth is shielded from tax, that the principle of progressivity be put front and centre of the tax-expenditure system.

Tax revenue as a source of finance brings with it many benefits, but it is important to be aware of the trade-offs, too. It's unlikely that an ambitious approach to increasing tax revenues can be realised solely through taxes levelled directly on wealthy individuals and companies. One core gap in most countries' tax policy toolboxes is the capacity to conduct the distributional analyses of tax reforms (by income group or gender) needed for stakeholders to fully understand this trade-off. This may be important to invest in, in the post-2015 world, if equality and equity are to be effectively monitored.

### CHALLENGE 4:

#### Re-examining the global distribution of taxing rights

Owing to the fact that their tax bases are less diverse than those of developed countries, developing countries are more dependent on taxes levied on companies rather than those derived from personal incomes (except pay roll taxes). Tax avoidance, illicit capital flight and tax incentives are all factors that constrain developing countries' current revenues, and because of their greater reliance on business taxes, these ills exert a greater proportional impact than in developed countries. Another aspect also merits consideration.

Across the globe, the majority of corporation tax revenues come from multinational companies. The division of these companies' tax bases is determined by national policy and administration, and by tax treaties, all influenced by international tax rules, in particular the UN and OECD model tax treaties and the OECD transfer pricing guidelines.

Yet international rules are not politically neutral - they have implications for the distribution of taxing rights between different groups of countries. China and India, for example, have already implemented measures to increase their share of the tax base beyond what is allocated to them by international rules.

A global development finance settlement, especially one that considers aid and tax in the same breath, ought to include an explicit discussion of this point from a development perspective, before reaching a settlement on how these revenues are to be (re) distributed. A commitment to shift the distribution of taxing rights over multinationals towards developing countries would provide them with a sustainable increase in revenues, while increasing the benefits from inward investment. If combined with effective measures to address 'base erosion and profit shifting', this could even be a revenue-neutral intervention for developed countries.



C.C: World Economic Forum

The Panel captured during the Manufacturing Session at the World Economic Forum on Africa 2011 held in Cape Town, South Africa.

<sup>4</sup> Vararat Atisophon et al, 2011, *Revisiting MDG Cost Estimates from a Domestic Resource Mobilisation Perspective*. OECD Development Centre Working Paper No 306.

<sup>5</sup> Mick Keen, 2012. *Tax and Development - Again*. IMF Working Paper WP/12/220

## CHALLENGE 5:

### **'What gets measured gets managed': Three types of targets**

Clarity about what needs to be measured and monitored in relation to revenue mobilisation is crucial to harnessing maximum resources for the post-2015 agenda. Three targets are worth considering:

**Tax to GDP ratio:** This is an attractive starting point to measure progress in domestic resource mobilisation, but it must recognise the different starting points and potentials across different countries. Asking each country to increase its tax to GDP ratio by, say, three percentage points over 10 years might therefore be better than a notional target that may be too easy for some and too hard for others to attain. Alternatively, an aggregate target tax to GDP ratio across all developing countries, with differential contributions by different countries to achieving it, might make sense.

**Progressive taxation:** Hand-in-hand with any target incentivising, increased tax revenue must be one that measures and directs the share of taxation paid by the poor, and particularly by women. It must do so in a way that stimulates, rather than constrains, public debate on a topic that runs to the heart of political discourse. That most developing countries lack the analytical capability to measure this at present is precisely a reason to create such a target, which might conclude, for example, that women should be net beneficiaries of the fiscal system, or that the bottom third of the population by income should always pay a smaller share of their income in tax than the top third.

**Corporation tax:** There could be a global financing target focused on the corporate tax base. This could be, for example, an absolute increase of 20 per cent in tax revenue from multinational companies in developing countries. At one end of the spectrum, this target could be achieved at a (relatively small) cost to developed countries through a shift in the allocation of the corporate tax base to developing countries; in which case, it may be revenue neutral for multinational companies themselves. At the other end, it could be obtained through reforms that increase companies' overall tax payments by reducing 'base erosion and profit shifting' and eliminate tax incentives, thereby increasing revenues in both developed and developing countries. An intermediate option would combine the two, keeping revenues constant in developed countries.

## CHALLENGE 6:

### **Transforming Foreign Direct Investment into increased revenues**

South-South financial co-operation, where southern countries negotiate financing deals for mutual benefit, is increasing rapidly. In 2010, FDI overtook overseas development assistance as the primary source of international capital into Africa.

It is a mistake to assume that mobilising revenue involves a direct trade-off with attracting FDI. The upstream and downstream linkages of FDI can be improved through increasing investment in manufacturing infrastructure, funded in part through taxation. For instance, it should be possible to increase transparency with regards to the impacts of firms by taking measures to ensure that all firms apply a 'do-no-harm' principle to their core business through evaluating and disclosing social impacts of their activities. The Global Reporting Initiative guidelines provide a helpful framework.

### *Both the challenges and the opportunities for taxation in the Post-2015 Agenda are huge.*

That said, there is evidence that when FDI is channelled into consumption rather than investment expenditure, the impact on economic growth and development generally is diminished and FDI may in fact negatively affect domestic resources mobilisation. This is also the case when policies to attract FDI promote tax concessions and do not pay attention to incentives to encourage re-investment of profits.

But states must also be equipped to glean revenues from FDI flows. This is particularly the case with natural resources intensive countries.

These include maximizing the benefits of natural resources, matching tax potential to revenue need, raising revenue in a progressive way, re-examining the global distribution of taxing rights, putting measuring and monitoring systems in place and transforming foreign direct investment into increased revenues.



## 2.4 CURBING ILLICIT FINANCIAL FLOWS

*“The costs of this financial haemorrhage have been significant for African countries...[Capital flight has had adverse welfare and distributional consequences on the overwhelming majority of poor in numerous countries in that it heightened income inequality and jeopardized employment prospects.]”*

*Governor Ndung'u of the Central Bank of Kenya*

In addition to mobilising other external resources outside of ODA, tackling illicit flows from Africa should be at the centre of resource mobilisation to finance the Post 2015 framework. The establishment of the African Union's High Level Panel on illicit financial flows led by former President Thabo Mbeki, testifies to how seriously Africa takes this issue.

The Panel's approach to illicit money is broader, referring to monies that are both illegally and illegitimately earned, transferred or used. It is illicit if it breaks laws or ethical boundaries in its origin, movement or use. Some of these flows are obvious – money earned from illegal and criminal activities and laundered across borders. Examples include: drugs trafficking; illegal weapon sales; the trafficking of women and children; and, monies and assets earned through bribes and kick-backs.

According to the Global Financial Integrity (GFI), the composition of illicit flows is roughly as follows:

The share of public sector bribery in global illicit flows

**3%**

Criminal activities 30-35%

**30-35%**

Commercial activities

**-60%**

*Africa must take the lead and put its own financial house in order but the developed world must ultimately take the lead in addressing the issue of illicit financial flows as part of the Post 2015 commitments.*

The bulk of the losses from commercial activities emanate from trade-mispricing i.e. the illegal use of transfer pricing by TNCs through mis-invoicing of imports and exports and the deliberate mis-recording of trade pricing in order to hide and transfer profits abroad. Other methods include aggressive tax planning that exploit loopholes and encourage secrecy.

These practices are motivated by the desire to minimize, evade or avoid taxes; to channel capital secretly abroad, to conceal certain activities from public view and to conceal identities behind the ownership of wealth using secrecy jurisdictions.

Estimates on the magnitude of illicit financial flows from developing countries vary enormously, but even the most conservative suggest that the total outflow significantly exceeds the amount of ODA receipts from the OECD countries. Conservative estimates suggest that illicit outflows from Africa totalled about US\$854 billion between 1970 and 2008.<sup>7</sup> Less conservative estimates put the cumulative amount closer to US\$1.8 trillion.<sup>8</sup>

*Curbing illicit Financial Flows should be central to plans for resource mobilization to finance the Post-2015 agenda.*

If this staggering loss of capital would have been retained in the continent, most African countries could have paid off their outstanding external debt and still held surpluses for economic development and service provision. Notably, these estimates do not take into consideration very important forgone public revenue as a result of tax incentives, which cost African countries millions of dollars annually and contribute to a race to the bottom of tax competition between African countries, to the detriment of cooperation within and between regions.

Illicit flows not only minimise the revenues needed for improving governance institutions, the provision of public services and for growth-enhancing investment such as infrastructure development, they also erode legitimacy of economic activities and thus thwart vital economic development.

*Conservative estimates put IFFs from 1970 - 2008 between US\$854bn and US1.8 trillion. If that money had stayed in Africa, most countries would have paid off their outstanding external debts and still held surpluses for economic development.*

<sup>6</sup>The estimations are based comparison of bilateral trade data held at IMF Direction of Trade Statistics. But this database cannot pick up illicit flows resulting from same-invoice faking; and yet "several studies have plausibly indicated that illicit flows through same-invoice faking are at least as large if not larger (and almost impossible to detect) than those involving mispricing between invoices".

<sup>7</sup>Global Financial Integrity: Illicit Financial Flows from Africa: Hidden Resource for Development, 2010

WHAT DRIVES THESE FLOWS? RECENT RESEARCH SUGGEST THE FOLLOWING, AMONG OTHERS:

- **Structural factors such as the existence of tax havens and secrecy jurisdictions which “lease sovereignty” to offer sanctuary to hide ill-gotten assets from legitimate governments and conceal information from tax and anti-money laundering authorities;**
- **Business policies and practices to evade and avoid taxes as well as to escape regulation;**
- **Corruption and kick-backs in investment and procurement agreements;**
- **The capacity of institutions to collect taxes and counter illicit activities;**
- **The inclusion of the ‘shadow economy’ in the tax base.**

ACCORDING TO UNDP, OTHER FACTORS CONDUCIVE TO ILLICIT FINANCIAL OUTFLOWS INCLUDE: INEQUALITIES AND INEQUITABLE GROWTH, AND THE SIZE OF THE UNDERGROUND ECONOMY;

- **The degree of liberalization of trade, finance, foreign exchange and the capital account; the degree of foreign indebtedness; natural resource dependency; Weak regulatory capacity of government especially of companies and banks and large loopholes in laws easily exploited by lawyers and accountants;**
- **Lack of focus of governments on the provisioning of basic services to citizens, thereby encouraging aggressive tax avoidance;**
- **Inequitable taxation and tax burdens;**
- **Lax corporate regulatory regimes that tolerate the concealment of natural persons behind the ownership of companies and bank accounts.**

# — WHAT NEEDS TO BE DONE?

1

## ADDRESS THE STRUCTURAL FACTORS THAT CREATE THE DOMESTIC ENVIRONMENT CONDUCTIVE TO ILLICIT FLOWS.

As indicated above these factors include especially, wide, and in some cases, growing disparities between rich and poor; extreme liberalization of finance and the capital account, loopholes in legal and regulatory regimes and capacity of tax authorities, including customs authorities to monitor these flows. Addressing these issues is important in any case in the fight against poverty and under-development.

2

## BENEFICIAL OWNERSHIP (BO)

Knowledge of Beneficial Ownership is important to trace hidden assets and income streams, to fight tax evasion, corrupt payments, theft of state assets, money-laundering, terrorism financing etc. This requires maintaining public registers of beneficial owners of companies nationally but also as an international agreement. To curb the practice requires knowledge of who the warm-blooded owners of these companies, trusts and foundations are. Instead, rich countries (the G8 and the OECD) seem to be heading towards agreeing that though the registration of the beneficial owners of their companies is necessary, the registers should be kept private.

The question is whether, and if so how, they will ensure access to 'competent authorities' (e.g. tax authorities) in developing countries. It is essential, for the financing of the post-2015 agenda that African governments have access to this information.

3

## AUTOMATIC EXCHANGE OF INFORMATION (AEI)

This is important for much the same things as BO. Automatic Information Exchange is now recognised as the gold standard for information exchange. The OECD will lead a process to create and agree a multilateral system for automatic exchange of information. It is very important that there is strong African involvement in that process; that full reciprocal information provision is not required from African and developing countries at the outset (i.e. so that they can start to receive information before having the systems to provide information in exchange); and that support is available to ensure these countries make use of this short window of opportunity ; and that poor countries are not excluded on such grounds as 'poor governance or the lack of capacity'.

We know that the OECD is pushing against developing countries participating fully from day one on the grounds that they will slow down the process, ostensibly citing governance and capacity limitations. Without a major push by Africans, African countries are likely to be the most marginalized.

## INTERNATIONAL CORPORATE TAX SYSTEM

### A. Transparency

Transparency is essential to allow tax authorities to do 'rule of thumb' assessments of whether particular multinational companies are a tax risk; and to set a baseline for use in the increasingly important 'profit apportionment' options in the OECD's Transfer Pricing Guidelines. All UK Crown Dependencies and Overseas Territories have agreed to sign the Multilateral Convention on Mutual Administrative Assistance in Tax Matters.

The OECD's 'Base Erosion and Profit Shifting' (BEPS) initiative that will lead to a requirement for multinational companies to report on a country-by-country basis is a good beginning and has been endorsed by the G20. The European Commission (and the French) have in effect said that they will pursue this already (and in a limited way, it already exists in US and EU for extractive companies). The US and EU have passed legislation requiring all companies in the Oil, Gas and Mining sector to disclose their payments to governments on a country by country and project by project basis. The EU capital requirements directive has extended this to the banking sector. There are now discussions at the EU about extending this to all sectors. African governments need to inform themselves about this process and engage with it.

The review of the EU Anti Money Laundering directive also has the potential to win transparency on company ownership in all EU countries – and subsequently related tax havens. But the proposals currently on the table suggest that EU countries would keep this information private within law enforcement authorities in EU countries. African countries need to push this issue and make the case for public disclosure of this information. They perhaps stand to gain the most from greater transparency.

### B. Choice of rules – the issue of transfer pricing

The BEPS initiative reflects a growing recognition that the current system of transfer pricing is not fit for purpose. Most importantly, it treats individual subsidiaries as if they were [profit-maximizing] separate entities. It is clear that this is not the case; and that the relevant level for profit maximization is the level of the whole group. For this reason, there is growing pressure to move further in the direction of profit apportionment (that is, using the relative scale of economic activity in different subsidiaries to apportion the global profit), rather than continuing with the fool's errand of trying to guess the 'correct' price for trade within a multinational group, when no such thing exists. The pressure will continue to grow for unitary taxation: taxing the multinational group as a single unit, rather than each legal entity separately. African governments should use the opportunity of post-2015 discussions to address the issue.

### C. Obstacles and areas to push further at global level

Even if, Automatic Exchange of Information and Beneficial Ownership were to be fully implemented, a lot still remains to be done. We need to call for full public transparency of beneficial ownership of companies, trusts and foundations; multilateral automatic information exchange; public 'combined and country-by-country reporting from multinationals; and a more coherent approach to profit apportionment in international corporate taxation. Africa of course has its own special problems of dealing with natural resource contracts and detecting mis-pricing in trade generally and in natural resources in particular.

### D. Taking the lead and putting own houses in order:

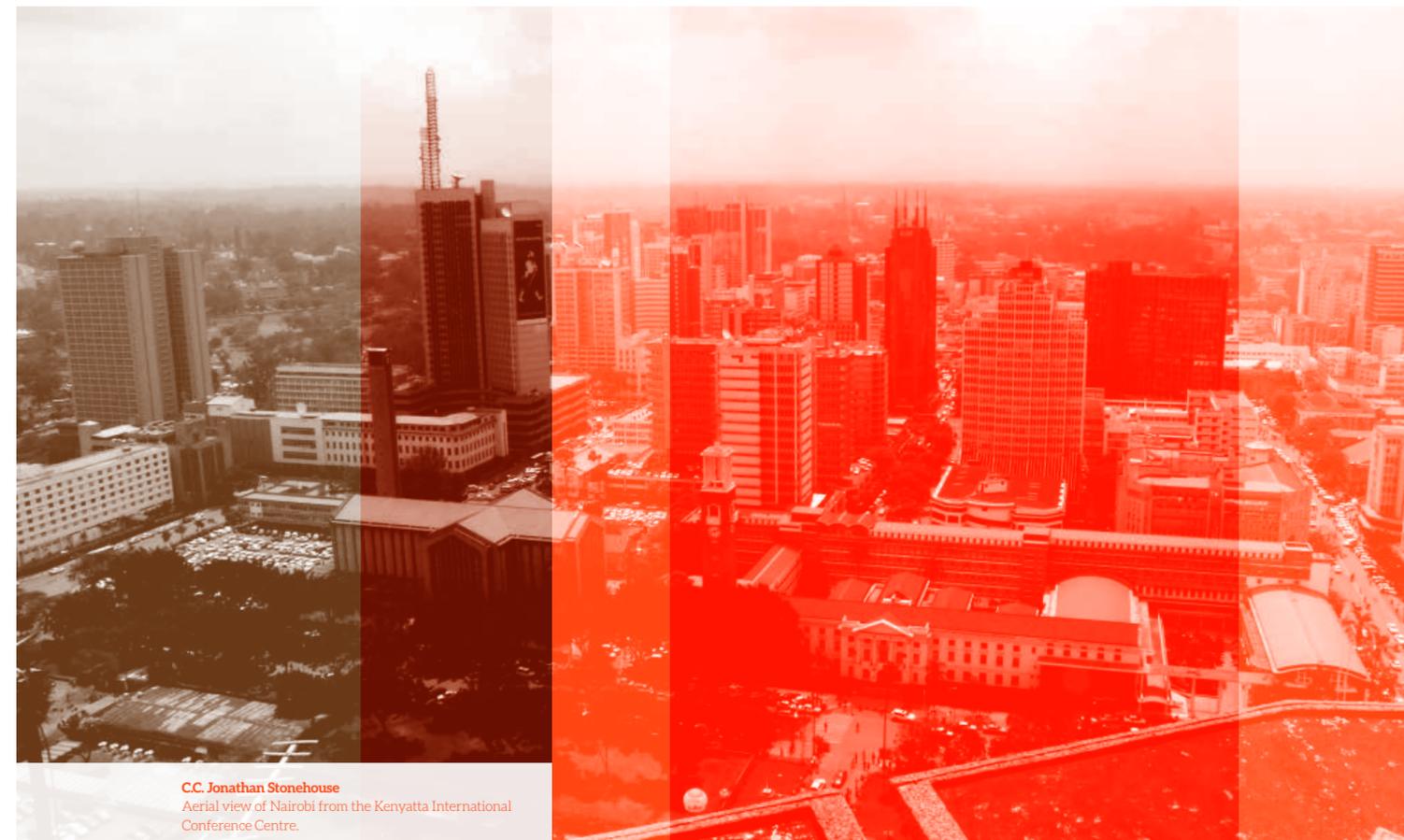
The President Mbeki panel is an opportunity for African states to address these issues collectively whilst developing joint strategies to engage the rest of the world, using the post-2015 process as an opportunity to put their case.

#### An agenda for action could include:

- (A) Establishing or improving registers of company ownership. This may require review of existing company registration and banking laws;
- (B) Preparing systems to be able to use, and to provide reciprocally, tax information;
- (C) Sign up to the multilateral convention on mutual administrative assistance in tax matters – providing access to banking and tax information on request for all UK linked tax havens;
- (D) Consider an African Convention on AIE and Country-by-Country reporting for countries listed on African stock exchanges;

- (E) Resist moves from banks and others in the finance sector to set up Offshore Centres in Africa (Examples of Accra and Nairobi);
- (F) Address the domestic structural factors accentuating illicit financial flows (IFFs);
- (G) Make the tax system accountable to people e.g. the Rwanda Meet the People road-shows of tax authorities; and
- (H) Providing collective solidarity to governments taking bold steps to address natural resource rent sharing imbalances (e.g. Ghana's on-going renegotiation of mining contracts) and to stem illicit financial flows (e.g. Zambia's move to track and repatriate foreign exchange).

Ultimately, Africa cannot address the issue of illicit flows on its own. The biggest drivers and levers lie outside its control and is largely the responsibility of developed countries. Developed country partners should undertake binding obligations to take measures to address their role in illicit financial flows in the context of the post-2015 sustainable development framework



CC. Jonathan Stonehouse  
Aerial view of Nairobi from the Kenyatta International Conference Centre.

# 5

## MANAGING REMITTANCES

The value of financial remittances from African migrants abroad has grown significantly and now exceeds official development assistance. The recorded flows may well be far less than real inflows if one factors in cash carried in pockets across borders or transfers made in the form of goods rather than cash. Although most of these transfers are directed to fulfilling household consumption and housing needs, there is some evidence of increased investments financed by remittance. What is clear is that the potential to manage remittances for structural transformation is immense. Ethiopia's diaspora bond has succeeded in attracting hundreds of millions of dollars for the construction of the millennium dam project, signalling an untapped potential.

AFRICA SHOULD MANAGE ITS REMITTANCE INDUSTRY BETTER TO TAKE ADVANTAGE OF THE WEALTH, KNOWLEDGE, IDEAS, ENERGY AND VALUES OF ITS HUGE DIASPORA

This informs the decision by the heads of State and Governments in the African Union to establish an African Institute for Remittance to study, monitor and develop incentives and investment products to harness the development impacts of remittances. The cost of remittances to Africa is however quite high, reflecting various charges and taxes as well as limitations in the banking infrastructure and capital management policies and infrastructure.

There is a role for partnerships – across transnational banking institutions, money transfer companies, financial regulatory institutions and government – to shape the remittance industry to support Africa's transformation agenda.

A post-2015 financing framework should encourage and incentivise the creative harnessing of remittances. Critically, there is an imperative to recognise that the actual and potential resources that African migrants transmit back home transcend finances to include knowledge, ideas, energy and values.

# 6

## OFFICIAL DEVELOPMENT ASSISTANCE

Aid in context:

- Developing and emerging economies have been driving global growth since mid-2000s, and this trend is set to continue;
- Most developing countries expanded their fiscal revenues by almost four times over the years 2000 to 2010, with revenues expected to total **US\$10 trillion** in 2015;
- By 2030, OECD (2010) estimates that emerging and developing countries will generate two-thirds of global GDP; this was diametrically opposite in 1990;
- FDI stands at **US\$506bn** in 2010, up from **US\$158bn** in 2001;
- Workers' remittances are now at **US\$319.6 billion**, from just **US\$90bn** in 2001;
- ODA is about **US\$130bn**, compared with under **US\$100bn** in 2001;
- And philanthropy funding to developing countries is estimated at **US\$53 billion**, compared with about **US\$12bn** in 2003.

But it is not all about numbers: African economic growth has resulted in improvements in livelihoods for some, and is placing the continent on a positive trajectory. However, this should not give rise to complacency or reductions in aid commitments. Africa's economic growth is still characterised by inadequate job creation and low value-addition, and, remains in large part, driven by export of primary products and natural resource extraction.

OFFICIAL DEVELOPMENT ASSISTANCE, WHILE STILL ESSENTIAL, SHOULD BE MADE MORE PREDICTABLE, HONOURING THE RECIPIENT'S NATIONAL DEVELOPMENT PRIORITY AND LOOKING TO ADDRESS LONG-TERM SYSTEMATIC CHANGES RATHER THAN SHORT-TERM QUICK FIXES

According to UNDP analysis, even if high-income countries were to stop growing today and Sub-Saharan Africa were to continue on its current growth patterns, it would take Sub-Saharan Africa until 2236 to catch up.<sup>8</sup> Therefore it is clear that we cannot afford to neglect the important role an adapted ODA can play in placing Africa's growth on a sustainable path.

In the consensual agreement on Financing for Development reached in Monterrey, Mexico in 2002, leaders committed to a "substantial increase in official development assistance [to help] developing countries achieve internationally agreed development goals and objectives".<sup>9</sup> However, although ODA increased steadily since the introduction of the MDGs, rising from US\$58 billion in 2000 to a projected US\$125 billion in 2010, it still falls far short of the estimations of the financing gap for achievement of the MDGs, as well as in comparison to the collective pledges made by donor countries.

ODA will therefore remain crucial – particularly in low income countries and fragile states where revenue mobilisation is challenging. In 2009, for example, countries such as Burundi, DRC, Ethiopia and Guinea Bissau collected as little as US\$35 per person – hardly enough to provide the services needed to improve maternal mortality or provide universal education. Here the need for aid is crucial.

To ensure a long term positive impact for ODA, the Paris Principles on Aid Effectiveness should be observed:

- Pledges and commitments are honoured to make ODA predictable and reliable;
- ODA is aligned with recipients' national development priorities and not the other way around;
- It is ensured that donor aid delivery modalities are better coordinated.

This will be increasingly important as sources of development finance become more diversified – from innovative finance mechanisms, the growth of non-traditional donors and grants from philanthropic organisations and South-South transfers and aid programmes. There is increasing evidence that the less dependent a country is on aid, the more effective aid is likely to be. These likely results from the fact that less aid dependent countries are better positioned to resist policy imposition and therefore more likely to use aid to supplement domestic resources to finance nationally owned development strategies.

But for aid to be an effective instrument for development in poorer countries there remains the need to address the donor political economy conundrum: the tension between 'instant Results' and building resilient Systems.

**Two approaches are possible:**

**Approach A:** Try to engage further and support long term systemic change, which means:

- Working to understand the complexities of national political systems better;
- Managing home political constraints.

**Approach B:** Accept that systemic changes are too complex for donors, and so focus aid on simple shorter-term results such as providing vaccines, building roads, schools, hospitals and infrastructure etc.

<sup>8</sup>UNDP, Human Development Report 2005: International cooperation at a crossroads – aid, trade and security in an unequal world (2005), p. 37).

<sup>9</sup> United Nations 2003, 14

# 7

## INNOVATIVE SOURCES OF FINANCE

Innovative financing mechanisms have been at the forefront of discussions on financing poverty reduction, the management of disease pandemics and climate change mitigation and adaptation.

In order to raise adequate resources to finance the ODA commitments arising from the G8 Gleneagles Summit in 2005, former Prime Minister Gordon Brown, proposed the International Financing Facility (IFF), a government bond aimed at raising resources from the capital markets in order to front-load expenditures on international development.

The IFF did not fly because rich countries would not take the risk. Other proposed mechanisms for raising funds for international and climate change financing have spawned a wide variety – international airline taxes, taxes on fertilizers, lotteries, taxes on oil and fats, advanced market mechanisms for financing risks related to market failures, carbon trading, the financial transaction tax (the so-called Robin hood tax) and many more. None of these mechanisms have as yet proven to be a source of significant resources.

What is striking is that most of these mechanisms are tax-based. To the extent that industrial economies are suffering recessions and the tax system is undermined by tax evasion and aggressive avoidance practises by companies and wealthy individuals, it is unlikely that these international innovations will be a reliable source of resources for Africa to finance its development.

But innovations need not be only of international origin. The relative success of Ethiopia's diaspora bond which has raised capital from Ethiopians home and broad is instructive; as is Rwanda's recent successful appeal to its population for voluntary contributions to plug its budget hole when donors suspended budget support. Also, Ghana has been relatively successful in harnessing and channelling its pension funds (the Social Security and National Trust, SSNIT) into long-term investments and creating taxed-based specialised funds to finance its critical infrastructure such as roads, health and education. These initiatives indicate that the scope for creative resource mobilisation remains to be fully harnessed. The post-2015 process should serve as an opportunity for African governments and people to carefully assess and establish mechanisms for monitoring and sharing lessons on innovative financing initiatives.

# 8

## FACTORING RESOURCE MOBILISATION INTO THE POST 2015 AGENDA

The Post -2015 framework can incentivise the increase and improvement of domestic resources at the national level and better management of foreign sources of finance. This will involve monitoring of key metrics on revenue mobilisation as a proportion of GDP. Given the dependence of many African countries on commodity exports and the need to increase value addition, a sector-by sector disaggregation of revenues could be valuable. To increase accountability and tax morale, budget transparency indicators are also crucial.

THE POST-2015 AGENDA SHOULD INCENTIVISE THE INCREASE AND IMPROVEMENT OF DOMESTIC RESOURCES AT A NATIONAL LEVEL AND HELP BETTER MANAGE FOREIGN SOURCES OF FINANCE.

### Financing principles:

For financing to address Africa's long term needs, it should be guided by the following principles:

#### A. Robust analysis of financing needs

The Post-2015 framework must be built on a robust analysis of the financing required to achieve the goals established. This should include international aid commitments and ensuring they are aligned with country priorities. At the national level, goals and targets should seek to incentivise adequate revenue mobilisation (such as a national target on Tax to GDP ratio).

#### B. Externalities

Consideration should be given to the impact of countries' own economic policies on the development efforts of other countries. If countries tackle their own economic and financial problems without taking into consideration the congruent impact on other countries, this can negatively impact on interests of African countries and more importantly, could jeopardize domestic resource mobilization efforts for sustained and adequate economic growth. This includes the provision of tax incentives and financial secrecy.

#### C. Policy space

The issue of "policy space" is fundamental to policy sovereignty as it concerns countries' independence and flexibility in designing their economic and financial policies and institutions in light of their circumstances and devising ways and means of aligning domestic policy to international opportunities and constraints. However, this needs to be cognisant of the impact of these policies on other countries' development efforts. The principle of proportionality needs to be applied here.

#### D. Long-term, stable financing and designed to expand productive capacity:

Ideally, resources flowing into Africa from external sources should help to ease the constraints for value addition in the productive sector, preserving natural capital or in the expansion of human capital and social institutions.

#### E. Developmental and justice principles

Financing should be aligned with human rights principles and priorities as well as climate justice goals. The poor should not be forced to bear the price when systemic failure is caused by excessive risk taking and poor regulation.

#### F. Domestic resource mobilization and ease of mobilization principles

These include: a focus on expanding the share of taxation in GDP without punishing the poor and small entrepreneurs; the need to link taxation with the provision of public services; principles encouraging progressive taxation; principles related to a fairer sharing of natural resource wealth; and, the encouragement of innovative modalities for mobilising resources.

#### G. Governance principles - financial system resilience and coherence principles

These relate to such issues as the criteria and extent of public bail-outs and irresponsible lending.

#### H. Accountability principles:

This relates to freedom of information, transparency, transparency related to taxation, tax dodging, payment of fair taxes, transparency on information on taxes paid.



CC: Africa Renewal / UNMIL / Christopher Herwig  
Does financing benefit African women?



UN Photo/Rick Bajornas  
Press Conference on African Union Programme NEPAD

### Indicators

The post-2015 framework should promote disaggregated indicators that assist with identifying developmental impact and also help with identifying transition from reliance on one type of finance to another. Examples of indicators that align financing in line with the changing structure of the economy and size of potential resource mobilization base include:

- Revenue mobilization based on measures of local content in trade and value chains;
- Capital inflow indicators – that encompass the types of capital inflows as a way of tracking hot money as well as financial volatility;
- FDI – sectoral decomposition and what percentage goes to middle tier of firms and not just apex firms;
- ODA – as a proportion of GDP, budget, social sector spending with the objective of transitioning.

Table 1. Below offers examples of indicators related to the mobilisation of international resources:

INTERNATIONAL FRAMEWORKS TO SUPPORT DEVELOPMENT FINANCING	
TARGET	INDICATORS
Increased and more effective use of resources for development	<ul style="list-style-type: none"> <li>• OECD DAC donors will uphold their commitment to allocate 0.7% of GNI to ODA;</li> <li>• Bilateral and multilateral development actors progress on the principles established through the Global Partnership for Effective Development cooperation (using their monitoring indicators)</li> </ul>
International transparency to support domestic resource mobilisation	<ul style="list-style-type: none"> <li>• Increased transparency of financial flows through south-south cooperation;</li> <li>• Progress on countries committing to and delivering automatic exchange of beneficial ownership information.</li> </ul>

## 9

### ADDRESSING GLOBAL SYSTEMIC CONSTRAINTS TO AFRICA'S ABILITY TO FINANCE ITS OWN DEVELOPMENT.

As noted earlier, Africa is highly integrated into the global economy but as a primary commodities exporter. It's social and economic conditions are highly sensitive to external macroeconomic conditions that affect the flow of capital, commodity prices and policy space for economic transformation. Its ability to finance its development therefore rests heavily on the global financial and trading systems as well as the external macroeconomic environment which lie outside its control. Therefore the issue of how the international community can best support the financing of Africa's development requires not only an increase in direct transfers but systemic reforms to create the necessary conducive environment. The South Centre lists these succinctly as follows:

- 1 Review multilateral rules and agreements, especially trading agreements as well loan agreements with the international institutions in the case of Africa, with a view to improving the policy space to pursue industrial development necessary for economic growth and social development. Industrial, macroeconomic and financial policies of developing countries are severely constrained by bilateral investment treaties (BITs) and free trade agreements (FTAs) signed with advanced economies. These agreements are designed
- 2 Attention should be paid to the international intellectual property rights (IPR) regime with a view to facilitating technological catch-up and improving health and education standards and food security in developing countries.
- 3 Review minerals contracts with transnational companies (TNCs) in order to remove unfavorable terms that undermine revenues and the ability to add more value to commodities.
- 4 Introduce multilateral mechanisms to bring discipline to policies in advanced economies to prevent adverse consequences for and spillovers to poor countries, including agricultural subsidies, restrictions over labor movements and transfer of technology and beggar-my-neighbor monetary and exchange rates policies.
- 5 Establish mechanisms to bring greater stability to exchange rates of reserve currencies and prevent competitive devaluations and currency wars, such as those seen during the current crisis.
- 6 Reduce global trade imbalances through faster growth of domestic demand, income and imports in countries with slow growth and large current account surpluses in order to allow greater space for expansionary policies in deficit developing countries.

AS A PRIMARY COMMODITIES EXPORTER, AFRICA'S SOCIAL AND ECONOMIC CONDITIONS REST HEAVILY ON GLOBAL FINANCIAL TRADING SYSTEMS. THESE NEED TO BE REFORMED, REVIEWING MULTILATERAL RULES AND AGREEMENTS AND INTERNATIONAL INTELLECTUAL PROPERTY RIGHTS. MINERAL CONTRACTS WITH TRANSNATIONAL COMPANIES SHOULD BE REVIEWED AND MULTILATERAL MECHANISMS PUT IN PLACE TO STOP ONE COUNTRY'S GAINS SETTING BACK ITS NEIGHBOURS. THERE NEEDS TO BE GREATER STABILITY TO EXCHANGE RATES OF RESERVE CURRENCIES AND BETTER PROCEDURES FOR INTERNATIONAL SOVEREIGN DEBT REPAYMENT.

**7** Make full employment a global objective, to be pursued by all countries without resort to beggar-my-neighbour exchange rate, trade and labor-market policies.

**8** Reversal of the universal trend of growing income inequality should also be a global goal. This calls for reversing the secular decline in the share of labor in income in most countries. This goal could be pursued through various means to establish a level playing field between labor and capital, including greater international mobility of labor, regulation of international financial markets and capital movements, more equitable taxation of wage income and incomes from capital and financial assets, prevention of tax competition and a code of conduct for TNCs. Pursuit of such a goal calls for breaking the dominance of finance and corporate interests in the formulation of policies and operation of the global markets. No single country alone can do this – it should be pursued collectively at the global level.

THE GLOBAL COMMUNITY NEEDS TO UNDERTAKE FINANCIAL AND TRADING SYSTEM REFORMS TO GIVE AFRICA A FAIR CHANCE.

**9** Regulate systemically important financial institutions and markets, including international banks and rating agencies and markets for commodity derivatives with a view to reducing international financial instability and instability of commodity prices.

**10** Establish impartial and orderly workout procedures for international sovereign debt to prevent meltdown in developing countries facing balance-of-payments and debt crises.

**11** Compensate costs inflicted on developing countries by global environmental deterioration and climate change.

**12** Secure a fair and equitable allocation of usable carbon space between advanced economies and developing countries, taking into account cumulative contributions of advanced economies to atmospheric pollution. Even then, developing countries should not incur additional costs to accommodate the tightened carbon space constraints such as those involved in developing and using cleaner technology or energy sources. Transfer of technology for these purposes should be greatly facilitated and provisions in the international Intellectual Property Rights regime impeding such transfers should be revised.

**13** Introduce international taxes in areas such as financial transactions or energy to generate funds for development assistance as well as for financing the costs of climate change mitigation and adaptation in developing countries.

**14** Reform international economic governance in ways commensurate with the increased participation and role of developing countries in the global economy. Re-examine the role, accountability and governance of specialized institutions such as the IMF, the World Bank and the WTO, and the role that the UN can play in global economic governance.

These recommendations are highly relevant to the conditions necessary for Africa to achieve structural transformation and finance transformative change sustainably.

# CONCLUSION

THESE RECOMMENDATIONS ARE HIGHLY RELEVANT TO AFRICA'S DESIRE FOR STRUCTURAL TRANSFORMATION AND TO FINANCE TRANSFORMATIVE CHANGE LARGELY FROM A CAPABLE ECONOMY AND EMPOWERED PEOPLES.



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