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Building Capacity for Domestic Resource Mobilization: The Role of the Government

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The Issue

Africa adopted an industrialization strategy, and committed to implement Agenda 2063 and Sustainable Development Goals (SDGs), all of which require adequate funding. Given that no African country fully achieved all the Millennium Development Goals (MDGs) largely due to funding constraints, domestic resource mobilization is therefore a very critical issue. Domestic resource mobilization is defined as the generation of savings from domestic resources and their allocation to economically and socially productive investments as well as accounting for such allocation. Africa has the capacity to adequately fund its development programmes from its own pool of resources (*The Africa Capacity Report, 2015*). Thus African governments are responsible for ensuring that national and continental development programmes are fully implemented, hence should mobilize sufficient resources to fund them. The public sector achieves this mandate through taxation and other forms of public revenue generation. In ensuring sustainable mobilization of domestic resources including curbing of illicit financial flows[1], accountable governments are necessary.

The 2015 Africa Capacity Report highlighted one major challenge that militates against effective and efficient domestic resource mobilization, that is, the capacity to do so. The report shows that governments play a central role in partnership with other key stakeholders in developing and implementing strategies to scale up domestic resource mobilization and curbing illicit financial flows. The government is defined as the three arms that constitute constitutional and parliamentary democracies in Africa, thus the executive (the presidency for policy making), legislature (law making) and the judiciary (the executors of the legal processes).

This policy brief highlights the key capacity messages and policy recommendations pertinent to domestic resource mobilization which African Governments need to pay attention to.

The Study

The 2015 Africa Capacity Report is based on a survey that was undertaken in 45 countries. The research unearthed capacity dimensions that affect domestic resources mobilization and illicit financial flows in Africa. The study provides the opportunity for understanding the potential of and limitations to African governments in enhancing resource mobilization. It documents examples of good practices that certain countries have put in place in successfully scaling-up broad-based domestic resource mobilization.

Key Emerging Issues

State of Domestic Resource Mobilization in Africa. Africa has the lowest savings rate, investment and per capita growth rates when compared to other regions like East Asia and Pacific, Latin America and the Caribbean, and South Asia. However, these low savings form part of domestic resources apart from taxes. Although Africa realized an increase in tax revenues over a decade from \$123.1 billion in 2002 to \$503 billion in 2013, this increase in tax revenue has been driven by resource rents which are unstable due to the volatility of international commodity prices. Africa's revenue base is shallow, and the tax collection system is very expensive and inefficient. On one hand, remittance inflows to Africa are lower than in other regions partly due to high transaction cost. On the other hand, the official development assistance and other externally-generated flows to Africa are shrinking (see Box 1).

Box 1: Tax revenues, aid and other external flows in Africa.

The African tax revenues have generally been rising topping approximately \$500 billion in 2012, but this amount is below its potential level. Remittances to Africa amounted to \$64 billion in 2014 but is still low when compared to other regions. There is potential to increase the tax revenues collected if Africa manages to curb illicit financial flows since there was \$60.3 billion lost on average over 2003–2012, whereas the average official development assistance for the same period was \$56 billion (OECD–DAC International Development Statistics online database). On the other hand, aid to and donor spending in Africa is projected to decline until 2017 and has not previously yielded intended results. This clearly shows the need for African governments to improve the effectiveness and efficiency of domestic resource mobilization initiatives so that development programmes can sustainably be financed. This calls for African governments to implement robust policies which encompass capacity development to increase tax revenues collected and minimize revenue loss through illicit financial flows.

Very few African governments are paying attention to the expenditure side, and tax-payers argue that public funds are either lost or misused through high levels of corruption in government, poor prioritization and lack of accountability. Therefore, the responsibility of governments to scale up domestic resource mobilization and fully account for it is inevitable.

Impacts of Illicit Financial Flows. Illicit financial flows are counter-developmental to any government. First, they drain the much needed capital and revenue that could be used to finance development programs such as building infrastructure, training, research and development, and providing social services. Illicit financial flows have both short term and long term effects which all undermine the growth and development of African countries. This is mainly through capital flight which slows capital accumulation, investment, output growth and job creation. Countries may remain aid-dependent on donor funding which is conditional and continue to accumulate high external debt to finance its spending which incites further capital outflows. IFFs both weaken and undermine governance and widen social inequalities, especially when corruption is done by senior government officials and the elite hence undermine accountability. Ultimately, political instability may result when governments fail to be accountable, and are unable to provide social services to the public. These effects are all counter-developmental since they work against the effective implementation of domestic resource mobilization strategies. Governments should therefore find options to curb IFFs and effective mobilize domestic resources.

Capacity Challenges Affecting African Governments in DRM. African governments are faced with capacity challenges in their quest to improve domestic resource mobilization. The chief challenge is how to build capacity to scale up domestic resource mobilization, fight illicit financial flows, improve tax revenue collection and financial sustainability, and fight corruption. Most African countries have inadequate qualified

1 Illicit financial flow is defined as the resource flows that are illegally earned, transferred or used (AU and ECA 2015:9).

staff manning the revenue collection institutions. Moreover, the current tax systems are inefficient and costly and are characterized by too many exemptions that promote tax evasion. The 2015 Africa Capacity Report on Domestic Resource Mobilization pointed out that besides the limited capacity, the inability to mobilize resources is compounded by the low national income and output, low levels of financial development, narrow tax bases, and limited stakeholder consultations. This implies that strong and efficient institutions are necessary to scale-up domestic resource mobilization, and that building capacity in this area is critical.

Thus, governments become key economic agents who should lead in developing structures, systems and initiatives that promote revenue collection and close domestic resource leakages. In this regard, partnerships between governments and other economic agents such as the private sector, civil societies, the donor community and the general public are very important in the whole process. Moreover, the economic structure of African countries is such that the informal sector is growing, making it difficult for governments to tax them. In addition, the business climate in Africa hinders investment which is very crucial and affects taxing of business profits. These capacity constraints can be eliminated provided there is strong political will by African leaders and support from other partners. Here, capacity building institutions such as The African Capacity Building Foundation (ACBF) become strategic partners who can assist the governments to coordinate development of the required capacities to foster domestic resource mobilization.

Best Case Practices by Governments. The good country case practices illustrate the various measures being taken by some African governments to enhance domestic resource mobilization, (ACBF unpublished country profiles 2015). The initiatives are outlined in Box 2 below:

Recommended Options for Governments

African governments play a leading role in domestic resource mobilization, and should provide the necessary internal conditions for mobilizing domestic resources as well as mobilizing public and private savings. The *2015 Africa Capacity Report* recommends several options which African governments should consider in order to build capacity for effective domestic resource mobilization. These include:

- Increasing engagements with civil societies, the private sector, state institutions and the public to create ownership and understanding of the resource mobilization process.
- Collaborating with other stakeholders such as regional economic communities (RECs), forming regional watchdogs and get assistance from regional and continental capacity building institutions like The African Capacity Building Foundation (ACBF), African Tax Administration Forum (ATAF), and Collaborative Africa Budget Reform Initiative (CABRI) to share intelligence to effectively mobilize domestic resources and curb IFFs.
- Intensifying education and awareness campaigns on the importance of tax compliance (and accumulating savings). This also requires partnership with civil societies and the revenue authorities through trainings and workshops.
- Demonstrating the political will to curb corruption, plug resource leakages and capital flight through establishing stronger legal frameworks that allow tracking, stopping and recovering of illicit financial resource flows.
- Designing fair and easily implementable tax systems. This may involve removing unnecessary tax preferences, dealing with transfer pricing abuses and taxing attractive industries fairly and transparently.
- Capacitating revenue collection agents and financial institutions by acquiring and deploying ICT (information, communication and technology) that enables the integration of financial markets,
- Investing in financial data collection and helping to set up tax registries.
- Expanding the taxable base by reaching out to the informal sectors and all other economic groups which might be omitted from the tax-payers' bracket.
- Developing sound macroeconomic policies that promote private sector investment, and a savings culture.
- Legitimizing the tax collection process to increase transparency and accountability through publishing government expenditure, the stock of mineral resources and the proceeds realized from minerals and demonstrating the productive use of tax proceeds. Such information must always be compiled, updated and disseminated to the public.
- Expanding the human resources' skills base of staff (including government executives, the tax authorities' staff, legislature and the judiciary) in the domestic resource mobilsation policies, laws and processes.

Box 2: Country Cases of Good Practices for Improving Domestic Resource Mobilization

Some African countries such as Ghana, Kenya, South Africa, Zambia and Zimbabwe undertook robust measures to improve domestic resource mobilization through building or strengthening revenue collection capacity. For instance, the Ghana Revenue authority developed and implemented a revenue modernization plan. The plan includes measures such as deploying geographic information systems to locate tax payers. And just like Zimbabwe, Ghana introduced presumptive taxes on informal activities which form about 60% of African economic activities. Moreover, the government of Ghana created a Port Clearance Unit in the Custom Division to promote compliance in customs and tariff assessments and payments, and an integrated cargo clearance system for easy tracking of goods at the ports. Ghana is also in the process of creating an online tax application and registration platform. These online tax platforms, including e-filing were also set up in South African Revenue Service to improve ease of collecting taxes and enhance efficiency in tax administration.

Engagements with tax payers and tax education helped Zambia to increase voluntary compliance. Other automated administration systems that were developed to improve domestic resource mobilization include, modifying the clearance on permit system to allow consignments to move expeditiously. In Zambia, the government created one treasury bank account where all state institutions deposit all collections and fines directly to minimize theft and misappropriations of funds.

In Uganda, the government established institutions/agencies to enhance revenue collection and passed laws to curb illicit financial flows. These include Financial Intelligence Authority, Capital Markets Authority, Inspector General of the Government, Insurance Regulatory Authority, Uganda and Anti-Terrorist Act. Although weak regulatory and law enforcement capacity remains problematic, these are steps in the right direction.

In Ethiopia, a customs proclamation 622/2009 was enacted and led to institutional improvements of the Ethiopian Revenue and Customs Authority. In the rural areas of Ethiopia, people use traditional and informal ways of mobilizing resources and other African governments should learn and adapt from such initiatives.

Implications

It is clear that Africa fully understands and appreciates the need to finance its development programs from domestic resources. Several initiatives have been put in place by African governments to improve their revenue administration systems. What remains at stake is how best the economic, political and social governance structures can be reformed to ensure optimal revenue collection and accountability by the government so as to reinforce public trust in governments. This calls for the development of clear country strategies and initiatives that enable transparent, effective and efficient tax collection systems. Thus governments' willingness to effectively implement revenue reforms and the capacity to do so are the most important factors that determine the success of such resource mobilization initiatives. It implies that partnerships between governments and key stakeholders should be created and maintained.

Effective and sustainable mobilization of domestic resources requires strong, flexible and adaptive political and government technical leadership that uses a participatory approach in decision making. Similarly, democratizing the process of resource use becomes very crucial.

References

Africa Capacity Building Foundation (2015), *Africa Capacity Report: Capacity Imperatives for Domestic Resource Mobilization in Africa.*