Norad

LEARNING AND RESULTS 2020–2021

Tax for development portfolio

REPORT 6/2021

Content

Introduction

This report highlights progress and lessons learnt from the first two years (2020–2021) of Norway's Tax for Development (TFD) strategy 2020–2025. It does not attempt to capture all progress or all activities across the portfolio and it is not an evaluation of results. Rather, a selection of case studies and thematic focus areas are meant to improve learning and to inform future direction and decision making of the TFD portfolio.

Norway takes a comprehensive and ambitious approach to tax related development aid. The approach covers grant agreements with different thematic and geographic focus. The grant agreements include bilateral institutional cooperation, multilateral institutions, research organizations and civil society and is therefore managed as a portfolio. This means that the agreements are managed strategically based on a common theory of change, see chapter 3. The portfolio approach has been adopted to facilitate learning across the different areas of engagement.

Identifying key learning questions is an important part of the portfolio management. The program strategy developed some initial questions for the learning plan.[1] The learning plan has since been further developed, see appendix 1. In addition to identifying the questions, the learning plan will reflect how and when information will be collected. The case studies and thematic focus areas in this report are first steps in adding substance to the learning plan.

The report is organized as following: Chapter 1 summarizes the report's key findings. Chapter 2 gives an overview of TFD activities in 2020 and 2021. Chapter 3 looks at the theory of change, i.e. how the strategy proposes to make an impact. Chapter 4 and chapter 5 are specifically related to the learning plan through a selection of case studies and thematic areas, respectively.

1 See program strategy, page 17, https://www.norad.no/globalassets/publikasjoner/publikasjoner-2020/tax-for-development_strategy.pdf

1. Key findings

The country cases (Somalia, Uganda and Zanzibar) show that the appropriate partnerships depend on contexts. Still, there are some common denominators, such as aligning assistance with national development plans, maintaining close dialogue and being able to adapt to unpredictable environments and making sure partner countries are in the driver's seat of interventions.

Globally, the TFD-financed FACTI[2] panel gave several recommendations to advance financial integrity for sustainable development, including reforms to the international tax system. Change at the global level is a long-term endeavour and requires commitment to keep the dialogue going over time. Since the FACTI panel has ended its mandate, it is important that the work on bringing about change to the identified weaknesses continue in existing structures and bodies.

TFD will continue to follow up both the OECD process, which saw an agreement on a homework for international tax reform in July 2021, and the broader FACTI process that seeks to change the international architecture and improve inclusion of developing countries. The awareness and attention to issues of financial integrity need to be supported both through civil society and media as well as through multilateral organisations.

Media and civil society have important roles in raising awareness and attention to issues related to tax and development. The partnership with the International Consortium of International Journalists (ICIJ) has shown how important it is to safely strengthen the capability of developing country journalists to understand and take forward complex reports about illicit financial flows, tax evasion and criminal activities. Protection of investigative journalists and dissemination of news should be better supported at the country level.

Building a solid knowledge base for decision making is central in the tax for development strategy. It is important to better understand how tax is linked to other parts of the development agenda. This report discusses four thematic areas that were prioritized in 2020/2021: Inequality, health, local government and the environment. The aim is to get a better understanding of how aid and development cooperation best can support partner countries to advance equality through tax systems or introduce new taxes that can improve revenues or contribute to other SDG through behavioural change.

2 High Level Panel on International Financial Accountability, Transparency and Integrity for Achieving the 2030 Agenda (www.factipanel.org)

2. Portfolio overview 2020–2021

Norway is committed to international collaboration that strengthens domestic resource mobilization in development countries and fight illicit financial flows. Norad's Tax for Development (TFD) program is one of the main delivery channels for this commitment. The Tax for Development strategy corresponds with the collective commitment made by 25 partner countries, 20 development partners and 18 supporting organisations under the Addis Tax Initiative Declaration 2025 to maintain funding to development cooperation and to strengthen collaboration for domestic resource mobilization and equitable, efficient tax systems.

During the first two years of the program's implementation, TFD has established a wide range of partnerships through funding agreements and facilitating platforms for learning and exchange. Tax for Development currently has 21 partners supporting tax system changes (administrative and policy) in at least 68 countries.

By supporting the four multilateral organizations on tax (UN, IMF, WB and OECD) directly as well as through the Platform on Collaboration on Tax (PCT), TFD has contributed to more effective development cooperation on tax. Through the same channels, Norway has actively promoted enhanced participation of representatives from developing countries in the setting of tax standards and rules.

TFD has influenced the global debate on the future of global tax and financial integrity mainly by contributing to the launch and implementation of the FACTI panel process. The panel acknowledges the need to better align the global tax system to developing countries' cicumstances. It also identifies a need to strengthen capacity in weak tax administrations to improve implementation.

Tax administrations are key to improving domestic revenue and stopping illicit financial flows. TFD works closely with the Norwegian Tax Administration (NTA) to establish long-term institutional partnerships with sister administrations in partner countries. Cooperation has been established in Zanzibar and Rwanda, while dialogue on partnership has been initiated in several other countries, including Ghana, Lebanon and Uganda. TFD also supports regional organizations for tax administrations in Africa and Latin America, as well as Tax Inspectors Without Borders (TIWB). TIWB currently supports 46 countries and has helped raise USD 537 million extra in tax revenue between 2015 and 2020.

Research institutions and civil society are important to produce and disseminate knowledge about the linkages between tax and development. TFD-partners have advanced public debate and knowledge about tax systems nationally, regionally, and globally. They have produced valuable analysis on the relationship between tax and the pandemic including the COVID bailout tracker and Tax Justice Networks Tax Justice in the time of Covid.

The COVID-19 pandemic and the ensuing social and economic crisis has set the progress in fighting poverty back more than 10 years. It has increased inequalities and devastated economies. Financing the recovery will require increased domestic resource mobilization that stimulates economic growth and service delivery while protecting the most vulnerable. Domestic mobilization of public revenue is going to be even more important in the recovery, both because of the need for increased financing, but also because other sources of financing to developing countries has decreased.

Implementation of activities and programs in the first 18 months of the pandemic have been severely impacted by the pandemic. However, the ability and willingness of partners to adapt and innovate when faced with travel restrictions and other restrictions are commendable. What could be moved to online platforms have been moved, and while most partners indicate that aspects of the communication get lost, it has also enabled more people to participate than in physical meetings.

Multilateral partners have shown more flexibility than bilateral partners. Bilateral partnerships have shown some progress where relationships were established before the pandemic broke out, while bilateral programs that were in the early phases have stalled to a larger degree.

The COVID-19 pandemic and the ensuing social and economic crisis has set the progress in fighting poverty back more than 10 years. It has increased inequalities and devastated economies.

3. Theory of change: Revenues and social contracts

Tax is important to finance the sustainable development goals. The TFD program assumes that the primary changes to improve domestic resource mobilisation must take place at the national level, where revenue and spending take place. However, domestic tax systems are also highly reliant on international agreements and normative frameworks. These are not sufficiently oriented towards the needs and capacities of developing countries.

Taxes are lost through avoidance, evasion, crime, and corruption. In addition to new rules and norms, improved enforcement by revenue administrations is important to combat these leakages. Curbing illicit financial flows will narrow the SDG financing gap.

Tax is more than raising money. It is also a governance issue through the social contract. When collection is transparent, fair, and efficient, taxes can reduce inequality, be growth-friendly and help maintain peace and stability. These outcomes are preconditions for a favourable development in the society at large. Dysfunctional revenue collection undermines trust, reduces tax moral and feeds a vicious cycle toward less public revenue and less services.

Building good tax systems is difficult. Not only because of the technical complexities, but also because of the political aspects. Taxes constitute a core government operation, and most changes and reforms will be controversial. Lasting improvements requires in-depth understanding of the local context and a long-term and holistic approach including all stakeholders in the tax ecosystem. This means government, civil society, academia, private sector, and the media. While approaches will vary from context to context, there is significant learning that can take place between countries and among stakeholders.

TAX AND THE SDGS

Tax for development primary contributions to the SDG are through Goal 16 and Goal 17, but also has clear contribution to a number of other goals, with SDG 10 reducing inequalities being among the more prominent.

Goal 16: Promote just, peaceful and inclusive societies

→ 16.4. By 2030, significantly reduce illicit financial and arms flows, strengthen the recovery and return of stolen assets and combat all forms of organized crime
→ 16.6 Develop effective, accountable and transparent institutions at all levels
→ 16.7 Ensure responsive, inclusive, participatory and representative decision-making at all levels
→ 16.8 Broaden and strengthen the participation of developing countries in the institutions of global governance

Goal 17: Revitalize the global partnership for sustainable development

→ 17.1 Strengthen domestic resource mobilization, including through international support to developing countries, to improve domestic capacity for tax and other revenue collection

Goal 10: Reduce inequality within and among countries

4. Case studies – lessons learnt

This section contains five case studies that provide reflection on lessons learnt from implementation to date and recommendations for the way forward. These narratives include three country cases (Uganda, Somalia and Tanzania/Zanzibar), which by their different contexts and stages of cooperation shed light on some of the different successes and challenges. Following the country narratives, one case illustrates the engagements at the global normative level and one case illustrates the engagement with journalists as part of civil society.

External consultants have supported the TFD team at Norad to conduct interviews with partners, verifying information from periodic results and producing result stories which have been used as a basis for this section of the report.

Somalia: Building tax systems in a fragile state

Beyond raising revenues, effective and fair tax systems are important building blocks to support state capability, legitimacy and accountability. While state building is crucial in fragile states, it is also particularly difficult as negotiations about tax can drive conflict. Tax for Development's partners in Somalia are giving important inputs to the limited knowledge about tax in fragile states.

Advancing tax systems in fragile states is a central part of the TFD strategy. While there is an awareness that implementing tax programs in fragile states requires a different approach than in other countries, there is not sufficient knowledge about which approaches are needed to ensure sustainability and ability so scale up. Building resilient institutions and trust is necessary for stabilisation and state building but comes under constant threat.

Photo: KPMG

LEARNING QUESTION
What lessons can be drawn from programming in fragile states?

Somalia has over the past decades been consistently ranked as one of the most fragile states in the world. Tax collection is rudimentary, fragmented, plagued by corruption, and dampened by the lack of public trust. There are three levels of government that levy taxes and often in an uncoordinated manner: the federal government, federal member states and local governments. In addition, both government armed forces and Al-Shabaab rebels levy fees illegally, which are interpreted as tax by the population.

TFD supports two programs through multilateral partners in Somalia: UN-Habitat with a focus on local tax and the World Bank's Global Tax Program with a focus on customs. The selection of interventions is based on work by CMI and Norad, which identifies local tax and customs as two thematic areas with potential for development in fragile states.

TFD's partners in Somalia both have explicit objectives of enhancing knowledge and continually improving their approach. UN-Habitat seeks to systematically build on knowledge gained about land and property taxation in fragile states and learn from its successive interventions by developing knowledge products (research papers, implementation guidelines) and facilitating experience sharing (through networking activities). The World Bank project team also facilitates learning across countries under the umbrella of the Global Tax Program.

The UN-Habitat project builds on the UN project "Joint Program for Local Governance" (JPLG) which has worked on decentralization and local governance since 2008. This program has since the beginning received support from the Norwegian Embassy alongside other donors. Evaluations have shown the JPLG program to have had a transformational impact on local government governance and finance; dramatically increasing property registration, improving property tax compliance and collection, generalising community engagement in the planning of local budgets, and strengthening the provision of public services, particularly in the infrastructure sector. The TFD support to UN-Habitat aims to scale up the good practices and facilitate learning with other countries with similar fragilities. It also aims to develop tools for land based financing in fragile states through the Global Land Tool Network.

The World Bank's Global Tax Program in Somalia focuses on improving customs administration across federal member states and the federal government. Customs represent a key step in state building, as it has a divided functional responsibility across the different levels of government. In addition, it is an important source of tax revenue with significant potential for growth. The World Bank project has made substantial progress in strengthening the dialogue between relevant authorities at federal and federal member state level. Most significantly, the federal government and the states of Somaliland and Jubaland reached an agreement – under the auspices of the project – which determines the tariff rates that will eventually be applied at all major ports of the country. This is critical to avoid conflict and stalemate in developing the federal tax system across all levels of government.

LESSONS LEARNT

Both programs are essentially governance and state building programs, building the capacity of governments to collect taxes while the functional responsibilities often come up for negotiations. The approaches applied ensure that dialogue between different levels of government is constructive. The World Bank project has identified that tensions in the country directly affect the willingness of the federal member states and the federal government to maintain a dialogue on customs harmonisation. Without this dialogue any technical solutions and capacity development is not sustainable. The revenue results are not yet seen or expected, but the approach gives confidence that a solid foundation is built for better and more predictable tax and customs collection.

Implementing projects in Somalia is reliant on constant dialogue and adapting the pace and sequencing of interventions. The UN-Habitat project has faced significant delays because of lack of access to stakeholders due to travel restrictions stemming from the pandemic. Without the verification of data of the project by local government, next phases of the implementation have been postponed. Physical presence and face to face meetings are critical to maintain the necessary trust as a foundation for implementation, both for UN-Habitat and the World Bank.

WAY FORWARD

The understanding of how taxes work in fragile states is growing but how to link it to development programming is still limited. Sequencing of interventions require considerable local knowledge and coordination to ensure the best results. TFD will facilitate knowledge exchange between UN-Habitat and World bank projects in Somalia and other partners. There is an interest in and need for sharing the lessons learnt from the projects with the larger community of practitioners in Somalia and globally.

The dialogue series on land-based financing organized by Global Land Tool Network (GLTN) identified a need to further understand the interconnection between land management, redistribution, and revenue collection and how to integrate these in programming to reduce risk of conflict. These are sensitive topics and highly context specific. Lessons learnt on this should be linked to the UN SGs guidance note on land and conflict.

The World Bank project will continue to support state building by combining high-level dialogue and trust building with analytical work to make trade-offs explicit. Future lessons from this approach could be applied to tax and customs capacity development in other fragile contexts.

Uganda – Capacity development through multilateral partnerships

Tax for Development supports capacity development at the Ugandan Revenue Authority (URA) through multilateral organizations. The engagements are anchored in Uganda's Domestic Revenue Mobilization Strategy (DRMS), which ensures alignment with government priorities. The different programs have been well coordinated and complimentary, much due to Ugandan authorities being in the driver's seat.

An integral part of managing the Tax for Development portfolio at Norad is identifying synergies and learning across the different interventions and agreement partners. The case of Uganda focuses on what we can learn and improve in a country where several agreement partners are working on similar interventions and activities.

Tax for Development is supporting Uganda's Domestic Revenue Mobilization Strategy (DRMS) through implementing partners World Bank Group (WBG), IMF and OECD. Both IMF and WBG have conducted tax administration diagnostics studies, which collectively identified major gaps to fill. Along with WBG's tax and excise duty gap studies, as well as IMF's advice by missions and headquarters, these engagements informed Ugandan authorities in the drafting and ratification of the DRMS.

Various capacity development initiatives have led to tangible results, including the collection of additional revenues and ability of the URA to conduct and formulate its own costed implementation plan for the DRMS, following direct support from the IMF. IMF support to improve filing and payment processes has enabled the URA to have 100 percent electronic filing and payments rates for each tax type. These developments have contributed to improved tax revenue performance in recent years.

Capacity development support from the OECD has also delivered tangible results. Joining the Convention on Mutual Administrative Assistance in Tax Matters, developed jointly by the OECD and the Council of

Photo: KPMG

LEARNING QUESTION
How do multilateral partners work together at country level?

Europe, has enabled all forms of administrative cooperation between Uganda and other signatories in the assessment and collection of taxes. This cooperation ranges from exchange of information to the recovery of foreign tax claims. The exchange of information has with technical assistance by the OECD led to identifying and collecting EUR 34 million between 2014 and 2019. The activities of the OECD are coordinated and complimentary to the WBG's capacity development support administered under its international tax transparency workstream to ensure there is no duplication of work.

LESSONS LEARNT

A driving factor to the results to date have been the extent of alignment of donor programmes – all of which are complementary – as well as the leadership by the URA. When channelling support through large, complex multilateral programs, often operating and interacting with the same group of beneficiaries, coordination can prove challenging. In the case of Uganda, there is evidence that complementary approaches between the various implementing partners has been impactful, and relatively well-coordinated.

Coordination is helped by anchoring the work of the IMF and WBG, including all capacity development support, directly to the DRMS. This also helps mitigating the problem of recipient absorption that often can be a problem when multilateral programs result in governments pursuing competing priorities. It is also important to acknowledge multilateral constraints. Cooperation partners have their own capacity limitations. The IMF has annual support ceilings for its workstreams, for instance. The URA has requested more support on transfer pricing, but the IMF may not be able to assist. Whilst there is always an opportunity to do more, bilateral support could be beneficial if it is targeted and tied to a "vacant space."

WAY FORWARD

There is a need to strengthen country-level coordination of technical assistance efforts in all countries where the TFD program and its partners operate. Lessons from Uganda can be applied on the ground in other countries where several multilateral TFD partners operate and inform discussions at a systemic level in coordination initiatives such as the Platform for Collaboration on Tax and the Addis Tax Initiative.

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Zanzibar: Building trust and access

The development of a cooperation between tax authorities in Norway and on Zanzibar has been severely impacted by Covid-19. Still, strong demand and commitment from the Zanzibarian side has kept the prospect of a program afloat during a period where social restrictions have made the establishment of new partnerships difficult.

Following a scoping mission in 2019, the Norwegian Tax Authority (NTA) has been providing ongoing technical assistance to the Zanzibar Revenue Board (ZRB) in the form of a pilot program, as it continues to agree the final scope of work in dialogue with counterparts in ZRB. The approach has been to establish mutual understanding of ZRB needs at a more detailed level, as well as building trust between the two organizations. Currently, long-term cooperation will focus on institutional strengthening of ZRB and support to improve VAT collection in the hospitality sector.

Photo: Helena Lovincic

LEARNING QUESTION
What learning can be relevant for other portfolio agreements (results, approach, risks, etc.)?

Covid-19 has impacted the ability of NTA and ZRB to fully formulate the final scope of the project and building mutual trust. Some of the acute challenges for the pilot program following Covid-19 were eased by purchasing ICT equipment to better enable digital dialogue. This has made possible frequent meetings during the prolonged period of travel ban to develop an audit manual. A workshop was organized in June 2021 and another is planned in September to anchor the manual and its implementation at management level.

NTA appears uniquely positioned in Zanzibar, with only a few other partners giving limited support to the ZRB. Many projects managed through international consultancies have left technical capacity gaps upon their conclusion. In contrast, NTA's approach is to work alongside ZRB to build the requisite capacities of a well-established revenue administration, through a combination of direct assistance, mentorship, and delivery of discreet pieces of work through a "shoulder-to-shoulder" approach.

This model is underpinned by the relationships built between the two organizations. Throughout the pilot phase, NTA has invested in building trust, access, and ownership (at the right levels) within ZRB to establish longer-term relationships with counterparts. A strong relationship and ownership were built with the previous Commissioner of ZRB, and NTA is working to develop their requisite trust and access with the new incumbent. Ownership at management is critical, but most of day-to-day implementation can be exercised through a very competent and efficient coordinator.

The Project Coordinator holds the authority to delegate tasks for implementation and is in routine (weekly) contact with NTA staff regarding implementation. NTA sees tremendous value in this relationship, and the coordinator is a key factor in driving program delivery, particularly considering the inability for NTA staff to travel to Zanzibar due to the ongoing pandemic. NTA has also been able to develop a good relationship with the ICT Director. Several opportunities to leverage NTA's ICT expertise has emerged.

LESSONS LEARNT

While still early days, the experience with NTA and ZRB says something about the importance of a prolonged inception period in developing a trust-based bilateral cooperation. Through NTA's scoping work, missions and delivery of discreet pieces of work, NTA was able to ascertain foundational issues that may not have been present during initial discussions. A longer engagement period also enables relationships to be built, trust to be established and joint formulation of activities that reflect needs and demand. Most importantly, the main reason why the cooperation now is deemed promising despite difficult circumstances is the solid commitment and enthusiasm from ZRB to engage and prioritize this work

WAY FORWARD

The aim is to as soon as possible to establish a program document for a broad long-term relationship between the two sister institutions, including work programs and result frameworks. This may require some extent of physical presence and if so will be dependent on the lifting of travel bans and internal travel policies.

High level panel on financial accountability, transparency and integrity

There are structural challenges in the international financial architecture that impact domestic resource mobilization and financing of the SDGs. While there is a growing consensus on the challenges, there are many different proposals for the solutions. Ensuring that there is an inclusive dialogue around the challenges and solutions is essential. TFD has supported the high-level panel on financial accountability, transparency and integrity (FACTI Panel) tasked to assess the challenges within the current financial governance architecture and propose concrete recommendations to advance financial integrity for sustainable development.

Developing countries lose trillions of dollars every year due to financial manoeuvring and corruption facilitated by weaknesses and inconsistencies in the global financial system. Over the past two decades Norway has had a leading role in the international efforts to stop illicit financial flows and curb corruption and there is a broad recognition that obstacles to financial integrity are found both at national and international level. Support to the FACTI panel secretariat and the process, facilitated increased international debate on how the international financial architecture impacts development and developing countries.

A key objective of the FACTI Panel is to *"review existing international institutional and legal frameworks related to financial accountability, transparency and integrity, with a view to identify any gaps, impediments and vulnerabilities"* and to make recommendations for addressing these. The Panel was mandated to closely engage with UN Member States, relevant international institutions and bodies, civil society and other stakeholders and launched a set of analysis and a final paper of recommendations in 2020. An independent secretariat was also created to support the work of the Panel and hosted by the UN Department for Economic and Social Affairs (UNDESA).

The FACTI Panel can be credited for a direct impact on the inclusion of developing countries in the discussion

Photo: Fuse

LEARNING QUESTION
What results and what factors should be present for support to global normative processes?

of the global financial architecture and global tax cooperation. However, the depth of the reforms suggested by the panel is at present not supported by a consensus among countries. Implementation requires further negotiations and follow-up through existing forums and mechanisms.

The work of the Panel has the potential to contribute to a more inclusive global tax cooperation architecture, either by gradually garnering broader political support for its recommendations, or by acting as an impetus for the better inclusion of developing countries within the existing norm-setting mechanisms. In both cases, a positive outcome seems to critically depend on initiatives taken soon by national governments willing to assume leadership in the follow-up to the FACTI Panel report, particularly among high-income countries.

LESSONS LEARNT

Changes at the global level requires time and it requires investment in keeping the dialogue going over time. The broad dialogue and consultation as well as the broad media coverage have contributed to put the issue of the global financial system on the agenda and facilitated increased debate on unfair tax systems. A key assumption of the TFDs theory of change is that the international tax system enables illicit financial flows and that there is a need to find new solutions at the global level. This assumption is supported by the findings and conclusions of the report.

This year's FACTI panel process as well as the ongoing OECD negotiations on international tax has put these issues higher on the agenda. Support to normative and standard setting processes that advance meaningful participation of developing countries and civil society should be continued. The awareness and attention to issues around financial integrity needs to be supported both through civil society, media as well as through multilateral organisations. Supporting these stakeholders improves the legitimacy of the outcomes.

FACTI recommendations point to a need for continued broad stakeholder engagement at country and at international level. Civil society has played an important role in raising issues of fairness, accountability, and transparency of the international financial system over a long period of time and multilateral organisations such as the UN and the OECD has continued to bring country actors to the table.

WAY FORWARD

Many of the recommendations of the report are aligned with established policy in Norway while other recommendations require further inter-ministerial deliberation to determine Norway's political positions. This process is ongoing. TFD should continue to support to agreement partners and partner countries to hold similar discussion within government and with civil society to advance public debate.

Recommendations point to overarching challenges in the global financial architecture that are relevant for Norad's development cooperation. Most notably Tax for development and the anti-corruption programs. They identify overarching obstacles at the national and international level that facilitate illicit flows, corruption, tax avoidance and evasion under the label "financial integrity". Improving coordination and joint programming between tax and anti-corruption should be explored to improve results and enhance messaging.

Building capacity of Investigative Journalists

Skilled and independent journalists are central for ensuring accountability and allowing media to play its role in democracy. With support from Tax for Development, the International Consortium of International Journalists (ICIJ) has been able to train and work with journalists in developing countries to enable them to access information, investigate locally relevant angles and produce stories of tax and financial crimes. Better-quality reporting is one ingredient to ensure public debates that fosters improvements for societies at large.

ICIJ – a Washington-based news organization – spearheads a collaborative of news outlets that is dedicated to protecting public interest and exposing systemic failures around the world. Its aim is to curb corruption, injustice and inequality. ICIJ brings hundreds of investigative journalists across the world together to work as a single team on some of the biggest and most important investigations such as the Panama Papers, Luanda Leaks and the FinCEN files.

Photo: KPMG

LEARNING QUESTION
Does support to journalist organizations strengthen the ecosystem for tax reform?

The participation of investigative journalists from developing countries has been limited due to the lack of resources and networks and adverse working conditions such as freedom limited of the press. This has hampered journalists from for instance Africa to participate in international investigations and networks, to write their own stories and push back on local corruption and financial crime despite the data being available.

With Norad funding, ICIJ has been able to expand its network in developing countries as well as strengthening local investigative networks and communities. Through face-to-face and online training, participants in Africa have been able to participate at a more equal footing with its colleagues in Europa and North America in investigations. As a result, they have been able to uncover local stories and crimes and produce more and better-quality reporting.

Moving forward, Tax for Development can help in socializing released investigation reports by for example giving support to ICIJ or others to organize presentations and public discussions. This would be similar to discussions that take place in Europe when investigations break news. Tax for Development could also reflect report findings in programmatic activities in areas such as anti-corruption and tax collection.

LESSONS LEARNT

The theory of change for TFD assumes that the social contract is enhanced by access to information coupled with accountability systems. Information is not enough to support changes towards a fairer tax system that contributes to improved equality. This is particularly challenging with shrinking civic space in many developing countries, press freedom is restricted, journalists are under threat and civil society organizations lack capacities to protect and defend their civic space and rights. Having international networks with experience in protecting the rights and safety of journalists is an advantage. ICIJ has demonstrated that they take protection of journalists in their network seriously and have developed sound processes and methodologies for this. This is a precondition for supporting journalist organisations.

Illicit financial flows are global in nature, but the leaks and sources require local knowledge to become relevant. Uptake by media, civil society and law enforcement authorities is crucial for deterring tax evasion and criminal activities. This is more difficult in developing countries as the press freedoms are often restricted, the press and civil society organizations lack capacities to challenge cases in the media and in the justice system.

WAY FORWARD

Moving forward TFD should aim at supporting partners at country level to coordinate and making information made available through journalists work to wider civil society community and programmes for tax reform. Tax for Development can help in socializing released investigation reports by for example giving support to ICIJ or others to organize presentations and public discussions.

More should be done to facilitate uptake, awareness and follow up of published reports and analysis. Looking at supporting better integration, information sharing and collaboration between agreement partners operating in the same country or region could be a solution. The work of investigative journalists on IFF has close connection to the work on anti-corruption. TFD should explore how to better integrate these two workstreams especially on protection of journalists.

Investigative journalists are often under threat and might find it difficult to participate in public debates directly. TFD needs to be cognisant of this risk when planning for country level activities. When appropriate, reports should be shared with embassies and other stakeholders.

5. Thematic focus areas 2020/2021

Building a solid knowledge base for decision making is central in the tax for development strategy. It is important to better understand how tax is linked to other parts of the development agenda. Four thematic areas were prioritized in 2020/2021: *Inequality, health, local government and the environment.* The aim is to get a better understanding of how aid and development cooperation best can support partner countries to advance equality through tax systems or introduce new taxes that can improve revenues or contribute to other SDG through behavioural change.

Inequality is one of the biggest threats to development. Taxes can reduce economic inequality when they are based on ability to pay and when the revenues raised are spent socially. This rationale is valid both domestically and globally. As regards the latter, big companies and high net worth individuals are responsible for substantial illicit financial flows out of developing countries. These financial flows could provide much needed resources to fund critical investments in social development. Development cooperation should therefore approach the challenge of inequality on different levels in terms of policy reforms. In addition, improving enforcement could raise more revenues to be redistributed.

Pro-health tax programs are too often product driven (e.g. Tobacco programs) and built on the experiences of Western countries. For development cooperation to contribute to the best outcomes for partner countries it should emphasise comprehensive analysis of a range of products and be based on domestic consumption patterns and projections. The models should weigh progressiveness of the tax with other pro-poor benefits such as better health. These are complex processes, and in the end political decisions should be informed by political economy analysis and transparency in public debates. Although there are potentially significant revenues to be made, and they are often relatively technically easy to enforce, the health of the population should be the primary objective.

Subnational taxation has unexploited potential both for increasing public revenue for service delivery and strengthening the social contract. Fiscal transfers from central government to local government rarely corresponds to the decentralized responsibilities they are given. Therefore the ability for local governments to introduce local taxes and fees is important. Supporting dialogue between different levels of government on fiscal responsibilities is important to ensure stability and state building. The Addis Ababa Action agenda recognizes the need for national revenue strategies to look at multi-level government responses to financing for development. This has not been sufficiently supported by donors.

Green taxes can be in the best interest of developing countries, even though poor countries' carbon emissions pale in comparison to rich countries' and rich countries to a large extent do not tax their carbon emissions. Green taxes can help tackle local pollution and they can raise much needed revenues to finance vital public services. Green taxes can also encourage long-term economic growth as they channel investments to cleaner alternatives. The barriers to carbon pricing lie in making sure that change is equitable and aligned with the country's development objectives.

Tax and economic inequality

The topic of inequality as it relates to development in general and to tax specifically has in 2020 and 2021 gained increased attention. Inequality is accepted as one of the main barriers to development. Tax policies should, if possible, aim to reduce inequality. From the literature study TFD conducted in 2020, some findings impact both the general knowledge base and strategic decision making for the TFD portfolio.

Fiscal policy has a more significant impact on inequality in developed countries than in low-income countries. The redistribution effects depend on the size of the welfare state, especially the tax system and social benefit transfers, but also the provision of public services such as education and health care. These schemes are relatively generous in developed countries compared to less developed countries. In some lower middle- and low-income countries that include Indonesia, Tajikistan and Tanzania, policies increase inequality – tax and benefit policies have on aggregate had a sustained regressive effect.

Many economists have traditionally been sceptical towards the effectiveness of redistribution: Efficiency dictates that taxes should be kept low and structured in the least harmful way possible, i.e. with broad bases and limited progressivity. Inequality should preferably be reduced through well-targeted expenditure. Still, economists have increasingly concluded that the benefits of inequality-reducing taxation can outweigh its costs. There is empirical support to claim that at a given level of redistribution, lower inequality is strongly associated with faster and more durable growth.

HOW TO CONSIDER EQUALITY IN TAX AND DEVELOPMENT PROGRAMS?

Different approaches to inequality lead to different corrective strategies; these, in turn, assign different roles to taxation. Schematically, equality of opportunity leads to the use of tax revenues to finance interventions that seek to address inequalities upstream, while equality of outcomes places the focus on redistributing income downstream.

For the proponents of equality of opportunities principle, taxation is essentially an indirect instrument for providing incentives and financing interventions in favour of those who are deprived of opportunities. Their emphasis, therefore, is on (a) encouraging effort through tax, particularly when it helps to expand opportunities; (b) funding programmes that compensate for penalising circumstances. The “welfare to work” and “active labour market” policies implemented by many high-income countries since the 1990s are an illustration of this two-pronged approach.

Advocates of greater equality of economic outcomes, by contrast, see taxation as the key instrument of redistribution, i.e. of income transfers. Their focus is therefore on the direct use of tax to modify levels of income and wealth and its indirect use to finance inequality-reducing benefits (such as means-tested welfare payments). Naturally, the existence of linkages between the two types of inequality strengthens the case for a combined use of these two approaches to taxation – e.g. to reduce inequalities of income among parents while also providing better schooling opportunities to children.

To these considerations about the role of taxation in reducing inequality, one should add the concern that taxation itself should be fair to embody the notion that all citizens be treated as equals. There are different approaches to the equity of taxation. The most common approach to tax equity is based on the premise that taxes should impose an equal burden on all citizens and should therefore depend on their ability to pay. This principle underpins the notions of horizontal equity (that individuals with similar income or wealth should pay similar amounts of tax) and vertical equity (that taxes should increase with income and wealth).

Horizontal equity appears as a minimum condition of equity. Vertical equity requires the additional task of evaluating what constitutes an equal burden for different levels of income and wealth. A broadly accepted idea is that the sacrifice of paying an extra dollar in taxes decreases with the level of income; it follows that to impose an equal burden on all citizens, taxes should not only increase with, but also in proportion to the level of income (and wealth). In reference to vertical equity, taxes are considered progressive (resp. regressive) when they rise at a steeper (slower) rate than income.

Three important remarks can be made about progressivity as a measure of tax equity, and its relation to inequality reduction.

First, narrow assessments of the progressivity of tax are misleading. In particular, progressivity often refers to the structure of nominal rates applied by the personal income tax. Analysis shows, however, that progressive nominal rates can coexist with effective rates of taxation that are proportional or even regressive for parts of the income distribution once the incidence of all forms of direct taxation and tax exemptions are taken into account. The focus on only income tax might give a skewed reflection of the distribution of the tax burden if wealth is more concentrated than income, which is generally the case.

Second, tax evasion induces a major bias in the assessment of progressivity. Recent empirical investigations have found that the richest 0.01% of Scandinavian households evade up to 25% of their tax obligations by hiding assets in offshore financial centres. Considering the geographic distribution of the wealth held in tax havens, similar levels of tax evasion are likely to affect numerous developed and developing

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countries. In other words, tax equity is substantially lower than what incidence estimates based on tax collection figures suggest in many parts of the world.

It should be noted, finally, that the impact of progressive taxes on pre-tax income inequalities should not be assessed in isolation. It is the overall fiscal incidence that matters. The caveat is important: if progressive taxes finance public expenditures that aggravate inequalities of outcome or opportunity, then their overall effect is ambiguous and can be opposite to the intuition. In the same spirit, a standard advice to developing countries is to adopt a broad-based Value-Added Tax (VAT) irrespective of its regressive nature and use part of its revenues to finance means-tested benefits in order to address equity concerns.

Ideally, the effect of taxes on inequalities should therefore be evaluated comprehensively as the full fiscal-incidence result, embracing to the extent possible the range of tax instruments and the expenditures financed through taxation. While it is seldom possible to assess the level of inequality that would prevail in the absence of any tax, a more attainable objective is to analyse the effect of a particular tax (or tax reform) on inequality within the broader context of taxation and public expenditure.

WHAT'S NEXT?

At the decision-making point it is important that TFD considers how support to an initiative and agreement partner will impact inequality/equality. Requesting partners to include this aspect in their proposal should be considered when appropriate. It should also be considered as an important aspect of evaluations.

TFD has supported analytical work to advance the understanding globally on tax and inequality and will continue to support dialogue and development of methodologies. This will be supported through partnership and coordination as well as support to the multilateral and normative processes including ATI, the WB IDA, PCT, IMF and UNU-WIDER. Developing frameworks that can allow countries to better model or measure inequality should be an objective for the analytical work. There is room to continue to influence decision makers in multilateral organizations to strengthen the analysis of equality contributions.

The country specific dimensions must be considered for all country programming including the political economy dimensions. Currently Norad does not support tax policy through bilateral programs and will not propose to do so going forward. Hence country level support to tax policy and broader tax system reform for improved equality through tax programming will mostly be supported through multilateral programs.

Continued support to civil society is critical both to facilitate national debate, and to challenge the analysis. The alternative analysis that has come from civil society and academia has contributed to shift the debate and influenced policy. It is important that this support continues.

Pro-health taxes

Norway launched a new strategy for non-communicable diseases (NCD) in 2019. In this strategy tax was listed as one of the tools for combatting NCDs and where Norway has experience in using taxes on harmful products to reduce consumption and improve health outcomes.

The launch of the strategy also brough about a need harmonize the response to pro-health taxes between tax sector- and health sectors practitioners. When scanning the development landscape, it was clear that there was a lack of common analysis from health and tax economist that could potentially lead to contradictory policy advice. Collaboration between Norad's health section and the TFD team has contributed to increased debate on the issue and has led to identifying some core issues that should be addressed through pro-health tax programming nationally and internationally.

The interest in this topic and the need to draw on the expertise from different sectors is anchored in the need to mobilize resources to finance the SDGs in a manner that does not adversely impact vulnerable populations. Domestic public resource mobilization is the largest funding source for national health budgets in developing countries and the reduction of the tax base because of COVID-19 has had a dramatic effect on public revenue in developing countries. Lower income countries and fragile states generally have a narrower tax base with fewer tax types and therefore extra vulnerable to external shock and changes. This has a direct impact on financing public health services.

By using taxes as a way of changing consumption and behaviour patterns, "pro-health taxes" are presented to improve health, and thereby reducing expenditure on preventable deceases on the public budget, and to improve domestic revenue generation. For the most part these taxes are levied on tobacco, alcohol, and sugar beverages, but can also be used on products that cause air pollution which has a direct effect on NCD prevalence. The consequences of NCDs are costly in terms of medical treatment and the loss of productivity in the society. Studies show that both mortality and morbidity can significantly be reduced through behaviour change.

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Norad commissioned in 2020 a study on current research and policy trends and facilitated subsequent discussions between tax and development actors and health sector actors. Some of the findings are highlighted below and will guide future funding and engagement on pro-health taxes for TFD:

Using country data and analysis: It is assumed, largely based on positive experiences in Western countries, that pro-health taxes impact behaviour and reduce exposure to harmful products thus improving peoples' health outcomes and avail health budget to treat other ailments than NCDs. Consumption patterns for tobacco, alcohol and sugar sweetened beverages vary significantly between higher income countries and lower income countries, the trend does show an increase in NCDs in developing countries as well.

Comprehensive analysis: A comprehensive approach to pro-health taxes can play an important role in advancing this agenda. Support to analysis that look at the combined development effects, and not just one aspect, should be the priority for development cooperation. Analysis and models that include both economy, equality, health, social cohesion would give a better view of what tax programming should be proposed. A comprehensive analysis can justify introduction of regressive taxes in the short term if it has a pro-poor effect in the medium term and if it will help the holistic planning for national budgets.

Using a broad country analysis to determine "if, and what kind of" pro-health taxes would have the best impact on people's health and the economy. It is particularly important to avoid a pre-determined "product focused process" with global targets and promote country focused process, data and analysis. Country specific consumption patterns and projections would be an integral part of the analysis. There should also be openness to considering pro-health taxes that have not been tested in Western countries to the same extent, e.g. processed food and air pollution from various sources that are known to be important drivers of NCDs. Support long term impact models to determine the regressive impact vs. the pro-poor impact with a longer, but realistic, timeline.

Balancing short- and medium-term objectives: It is important to note that consumption patterns and drivers for consumption and behaviour vary a great deal between Western countries and developing countries, thus it is important to avoid shaping policies on the experiences of Western countries.

Be careful with earmarking: Increased revenues for pro-health taxes will together with the governments' other revenue sources better enable the implementation of national strategies. Earmarking exempts certain areas from the priorities all governments need to do. The weighing of all sustainable development goals and other national priorities should be done in a comprehensive process. Linking pro-health taxes to health expenditures could also backfire, because, inherently, successful pro-health taxes will change people's behaviour and then decline. When it comes to health taxes the division of labour between Ministry of Health and Ministry of Finance should be clarified and joint working arrangements proposed.

Bringing tax actors and health sector actors both at the donor side and at the country level is an important contribution for better results.

Ensuring transparency and participation in the process: Participation and transparency are important while introducing pro-health taxes as it enhances the social contract and reduces the risk of conflict and divisive policies. There is also broad agreement that for maximum impact, health taxes should be implemented alongside complementary measures such as public information campaigns to educate citizens on the harms and costs of consumption and measures to reduce the attractiveness and availability of the products. Transparency and participation also mitigate risk of unwanted interference and threats from private interests and pressure from commercial interests.

Subnational taxes

Research has identified subnational taxes, especially property taxes, as a low hanging fruit with potential to impact both local revenue and social contracts. The donor support has however been fragmented across different communities of practice; tax and development on one side and local governance programming on the other. This has led to low levels of learning from good practices and coordination. The same lack of coordination is often found within government structures, between Ministries and between the various levels of government. Most governance systems involve at least two levels of government and ensuring that state building has a coordinated approach to multi-level governance system promotes stability and legitimacy.

Subnational governments in low-income countries often lack the necessary resources to deliver basic services. Funding gaps tend to be filled by regressive and often informal levies. The responsibilities for service delivery decentralized to local governments far outweigh the resources transferred from central government. The right and need to introduce local taxes and fees are therefore critical for service delivery and for the social contract. Local taxes contribute to unlocking the benefits of decentralization including a government that is closer and more accountable to its citizens.

Of all local taxes, property taxes are among those with the highest potential to contribute to local development. Around the world property taxes provide the backbone of subnational revenues. In many OECD countries property taxes account for 2–3 pct. of GDP, but in most low-income countries it accounts for less than 0.2 pct. of GDP. Property taxes are administratively easier to introduce and manage as they are levied on observable assets in fixed locations. They are also more economically efficient as they do not distort work and investment decisions and recaptures gains from public investments. They are generally more progressive than other local taxes and fees since property owners usually represent wealthier segments of the population.

There is growing demand for subnational financing, especially in Africa. Revenue generation is not keeping pace with the rapid urbanisation and need for services. The need for domestic revenue mobilization at the subnational level has also increased during the pandemic. A case study in Kampala showed an 83 pct decline in own source revenue. In comparison with data from other parts in the world where local government finances incurred reduced revenues, there is evidence that those local governments that rely more on property tax revenues have had a more resilient revenue base during the COVID-19 period.

Understanding the local context and political economy of reform process is important, and some programs point to the benefits of having a local reform champion and sufficient flexibility to seize opportunities when they occur. Reform outcomes are higher when key variables align, these include political, technical, and personal alignment to create an optimal window of opportunity. Local Governments are the frontline representatives of governments and essential for the provision of public goods and services required to advance progress on the Sustainable Development Goals.

Reforms tend to look at the different elements of the tax system in isolation. Commonly, efforts to enhance tax revenues have focused on one tax base at the time, ignoring fiscal externalities, i.e., plausible effects on revenues from other taxes. For instance, can revenue gains from the introduction of a municipal property tax be offset by reduction of revenues from other taxes at national or sub-national levels?

Being aware of the potential conflict of interest between the national government and local government and how this can impact tax reforms is central to "do no harm" and to achieve results. Donors and development partners often operate at a national level for practical or political reasons but can play a more important role in supporting dialogues between national and local government. Better coordination and exchange of information between central and sub-national tax administrations reduce risks.

WHAT'S NEXT?

In 2021 Norad collaborated with the donor network on Local Governance and Decentralization (DeLoG) and Addis Tax Initiative to facilitate a number of dialogues on subnational taxes. The dialogue and webinar series invited experts, development partners and key stakeholders to a series of events to exchange information and learn about how the development community collectively can improve multilevel government strategies for subnational taxation. A particular focus has been to involve experts on local governance and tax experts as well as representatives from local and central governments. These dialogues have forged new partnerships and TFD will continue to follow up these processes. The new Addis Tax Initiative Declaration 2025 has included a stronger focus on subnational DRM, and this should be followed up in the dialogue around the Financing for Development process at the UN.

The ongoing program on subnational land-based taxes in fragile states implemented by UN-Habitat and the Global Land Tool Network will continue to be supported. Important lessons are being captured in both Somalia and Afghanistan and an expansion to DRC and a possible forth country is planned for 2021/22.

There is a need to expend this work, in line with recommendations from recent research. And although it has been highlighted as an important channel in fragile states, it should be elevated as a strategy for a wider range of developing countries. TFD will explore the possibility of including work on subnational DRM in existing agreements and have also made the decision to become a contributing partner of the Local government Revenue Initiative (LoGRI) as part of an agreement with the International Centre for Tax and Development (ICTD). ICTD has a long history of working on local tax, especially in Africa.

Green taxes

Increasing the price on greenhouse gas emissions is considered one of the most cost-efficient measures to mitigate climate change, and a crucial part of the efforts of the global community – and individual countries – to fulfill the Paris agreement. Green taxes can also be an efficient revenue source, since the tax is applied on a “bad” – a product or service that has negative effects that are not reflected in the price.

Norad’s Tax for Development portfolio strategy 2020–25 identified green taxes as an area to be explored. First, the TFD team commissioned a background report on carbon taxation from KPMG, to better understand the issue. In 2021, the TFD team has contributed to a broader report on solutions Norway can pursue in its development assistance to mitigate climate change, under the auspices of Norad’s Rethinking Development project, and developed a stand-alone discussion note on what role Norad can take in mitigating climate change through environmental taxes.

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The analysis shows that for many developing countries, climate taxation can be a more appropriate carbon pricing mechanism than other alternatives. Compared to an emissions trading scheme, climate taxation taxes require less administrative capacity and investment and can have an effect even for small economies independent of other countries and global processes.

Climate taxation can, under the right circumstances, have a triple dividend – reducing GHG emissions, increasing government revenue and improving public health through reduced air pollution. However, climate taxation can also have negative effects on poverty and inequality, depending on the design, consumption patterns and how the extra revenue is used. The developmental impact of a carbon tax in developing countries is further bludgeoned by the fact that the expert consensus leans towards setting a very low rate with limited scope at first, and then increasing the rate and broadening the scope gradually. A low rate and limited scope mean that revenue gains and emissions reductions will be limited in the short term.

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Green taxes are not easy to implement. The technical design can be relatively straightforward, especially if the tax builds on existing fossil fuel excises which are already in place in a fashion in many countries. But the key obstacle is often political and social opposition – because of legitimate concerns with the poverty and distributional effects of the tax, a weak social contract leading to low trust in the government, or opposition from elite groups who benefit from the status quo.

There is often a disconnect between climate and finance on all levels of government, in multilateral organizations and development agencies. Norad has started to bridge that gap through the Rethinking Development report and the TFD analysis, supported by Norad's new strategy where climate and environment will be even more integral to Norad's operations. Several of the TFD program's partners already work on green taxes, such as the UN Tax Committee / UN-DESA, the OECD Centre for Tax Policy and Administration, the World Bank Group, the regional tax organizations in Africa (ATAF) and Latin America (CIAT), and The International Centre for Tax and Development. But there is ample scope for the TFD program to expand its work on green taxes, in collaboration with other Norad teams, other donors and existing and new partners.

Based on the analysis, a set of insights emerge that could guide Norad's approach to green taxes:

1. Climate taxes are a necessary part of the policy package to reach the 1.5-degree target, also for developing countries, but the expected impact in the short run must be realistic.

2. The emphasis should be on what is politically feasible for a government in a developing country, and all other considerations around design and implementation must build on that – even if that means opting for second-best solutions in a climate and/or revenue perspective.

3. Successful implementation requires a complex set of skills, tailoring and patience – which is why we should start today but have a long-term view.

4. The complexity of the issue requires us to pursue several tracks at the same time – e.g. through global normative arenas, awareness raising among decision-makers, knowledge production and contributing to successful implementation.

WHAT'S NEXT?

Going forward, TFD will explore ways of bridging the gap between climate and finance in Norway's development assistance and in global normative arenas. TFD will look for opportunities to support country-level implementation of climate taxation and seek to understand how developing countries can overcome the political and social barriers to implementation, including how civil society organizations and other accountability stakeholders can contribute to increasing the acceptability of such taxes. Finally, TFD will explore connections with Norway's large climate-related development assistance portfolios, particularly within the climate and forest initiative and the renewable energy program.

Appendix 1: Learning plan

Subject	Learning Question	2020/2021
1. Agreement level learning (progress and results)	1.1 What are the contributions to overall portfolio results?	Annual reports from partners
	1.2 What learning can be relevant for other portfolio agreements (results, approach, risks, etc.)?	2020/2021 we identified **five case studies**
	1.3 Are there opportunities for strengthening alignment with portfolio goals?	
2. Portfolio synergies and gaps	2.1 How are the different portfolio partners working together?	**Case study Uganda:** How do multilateral partners work together at country level? **Case study Somalia:** What lessons can be drawn from programming in fragile states?
	2.2 How are the combined agreements contributing to the overall objective and ToC for TFD?	
	2.3 Have we got the right balance of interventions given new information and contextual factors (outcome 1 and outcome 2)?	

Subject	Learning Question	2020/2021
3. Future portfolio direction	3.1 Have the foundational assumptions been strengthened or weakened?	
	3.2 How is the portfolio aligned to Norway's development policy?	
	3.3 Under which circumstances is the ecosystem approach effective?	**Case study ICIJ:** Does support to journalist organizations strengthen the ecosystem for tax reform?
	3.4 What factors should determine a broad or narrow geographic orientation for the program (regional, country/global)?	**Case study FACTI panel:** What results and what factors should be present for support to global normative processes?
4. Hypothesis testing	4.1 What are the most cost-effective ways for aid to support increased tax revenue?	Partner roundtable on subnational tax Literature study on tax and environment
	4.2 What are the necessary conditions for effective capacity support to national tax authorities?	Literature study on tax and health
	4.3 What are the most effective approaches to strength the social contract through tax cooperation?	Literature study on tax and inequality

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