



Policy Paper 2024/01

Domestic Revenue Mobilisation for Sustainable Development in Sub-Saharan Africa and the Contribution of IDA-20

REPOA

Published by:

REPOA
157 Migombani/REPOA Streets, Regent Estate,
P.O. Box 33223
Dar es Salaam.

Suggested citation:

REPOA. (2024). Domestic Revenue Mobilisation for Sustainable Development in Sub-Saharan Africa and the Contribution of IDA-20. REPOA, Dar es Salaam.

Policy Paper 2024/01

Suggested Keywords:

Domestic Revenue Mobilisation, Sustainable Development, Sub-Saharan Africa, IDA.

@REPOA, 2024

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▼ TABLE OF CONTENTS

1.0	INTRODUCTION.....	1
1.1	<i>Key DRM Enhancing Baselines.....</i>	1
1.2	<i>Background Notes.....</i>	5
2.0	BUILDING TAX CAPACITY AND CREATING FISCAL SPACE FOR DEVELOPMENT EXPENDITURE.....	9
2.1	<i>MDBs' Support for Enhancing Domestic Resource Mobilisation (DRM).....</i>	13
2.2	<i>Concerted IDA Action on DRM.....</i>	17
3.0	DOMESTIC RESOURCE MOBILISATION (DRM) IN IDA RECIPIENT COUNTRIES.....	20
3.1	<i>Introduction and Overview of DRM Reforms in IDA Countries.....</i>	20
3.2	<i>Case Study 1—Tanzania (At 11.8% Tax/GDP).....</i>	25
3.3	<i>Case Study 2—IDA SSA Countries with Tax Yields Below 15% of GDP....</i>	32
3.4	<i>Case Study 3—IDA SSA Countries with Tax Yields Above 15% OF GDP..</i>	37
3.5	<i>Comparative Assessment of Case Studies Featured.....</i>	43
4.0	IDA-20 INITIATIVES AND COMMITMENTS MADE FOR DRM.....	53
4.1	<i>Introduction.....</i>	53
4.2	<i>DRM and IDA Initiatives and Commitments.....</i>	54
4.3	<i>Attainment of IDA-20 Commitments in Sub-Saharan Africa.....</i>	63
5.0	CONCLUSIONS AND RECOMMENDATIONS.....	66
5.1	<i>Conclusions.....</i>	66
5.2	<i>Recommendations.....</i>	69
	REFERENCES:.....	75

LIST OF FIGURES

Figure 1: GNI Per Capita, 2022 in Current US\$-Selected 19 SSA Countries.....	6
Figure 2: Population for Selected 22 Countries—in Millions, 2023	7
Figure 3: Stakeholders Shaping Tax System Performance	9
Figure 4: Determinants of Tax Revenue Collection	11
Figure 5: Tax performance % GDP in Sub-Saharan Africa (LICs, LMICs, MICs).....	22
Figure 6: Tanzania’s Domestic Revenue Performance in Billion TSHS.....	24
Figure 7: Tanzania’s Domestic Revenue Performance in Billion TSHS.....	3
Figure 8: Tax/GDP Ratio.....	4
Figure 9: Tax / GDP Ratio	5
Figure 10: SSA LICs and LMICs with Tax/GDP Yields Below 15%, 2020.....	8
Figure 11: SSA LICs and LMICs with Tax/GDP Yields Above 15%.....	5
Figure 12: FY15-FY23 IDA Disbursements to Commitments Ratio	22
Figure 13: Taxation in IDA Countries, Source: IMF World Economic Outlook, April 2016	23
Figure 14: Direct and Indirect Tax Revenue	27
Figure 15: IDA 20 commitments and disbursements	28

LIST OF TABLES

Table 1: Tax Yields and Buoyancy Levels for Countries with less than 15% of Tax/GDP 9

Table 2: Resource-Intensive Countries —Oil Exporters 10

Table 3: Other Resource Intensive Countries 2

Table 4: Tax Yields and Buoyancy Levels for Countries with more than 15% of Tax/GNI 6

Table 5: Resource-Intensive Countries—OIL Exporters 7

Table 6: Other Resource-Intensive Countries 7

Table 7: Resource-Intensive Countries in SSA / IDA Recipients 11

Table 8: Constraints to formalise the informal sector in SSA 18

Table 9: Source and Volume of World Bank Support to Domestic Revenue Mobilisation 20

Table 10: Disbursement – Commitment Ratio in SSA, IDA17 - 20 29

1.0 INTRODUCTION

1.1 Key DRM Enhancing Baselines

Domestic Resource Mobilisation (DRM)—the process through which countries raise and spend their own funds to provide for their people—is the long-term path to sustainable development finance.

Through DRM, countries accelerate their economic growth by raising and spending their own funds for public goods and services, like schools, hospitals, clean water, electricity, and infrastructure—all critical to helping people rise out of poverty and make sustained progress toward the SDGs.

DRM not only provides governments with the funds needed to alleviate poverty and deliver public services but is also a critical step on the path out of aid dependence.

Countries' investment in their own public goods and services, particularly infrastructure, is also essential to attracting private investment and laying the foundation for long-term economic growth.

Specifically, *DRM*, i.e. *increasing government revenues through taxation and other non-debt income sources* is essential in allowing countries to own and flexibly chart policies that address their specific development challenges, while mitigating the risks of debt distress.

DRM does not necessarily mean new taxes or higher tax rates. Governments often see their revenues rise through improved audits or simplified filing and compliance processes. Successful DRM programmes are highly cost-effective; they return many times what is invested in them.¹

Further, DRM reform is not simply about increasing domestic revenue for public goods and services. It also includes activities that help to fight corruption through more transparent and streamlined tax administration but also spending that promotes growth. These not only improve a country's business climate as well as public perception and confidence in government institutions but also promote local production.

To deliver the essential services needed to end poverty and make sustained progress toward the SDGs, developing country governments must spend their resources in a transparent and accountable manner particularly in the context of developing macro-fiscal frameworks, formulating, and executing budgets, and reporting to oversight institutions and the public-at-large.²

The following seven sets of interventions are essential to enhance DRM efforts in the medium-to long-run:

¹ United States Agency for International Development (.gov).

² Michael Ryan Touchton, Brian Wampler, Tiago Carneiro Peixoto, "Of Governance and Revenue: Participatory Institutions and Tax Compliance in Brazil," World Bank Group.

1. Efficient and Equitable Revenue Management

- First, countries need to ensure efficiency in revenue collection;
- Second, Governments also need to make DRM more equitable;
- Third, analysis by the Natural Resource Governance Institute shows that many African countries have already made significant legal reforms in this area; hence taking the next steps to implement these reforms could lead to many benefits, including additional domestic revenue. (*Ibid*)

2. Beneficial Ownership

- Beneficial ownership transparency has emerged as an essential means of combating corruption, stemming illicit financial flows and tax evasion
- 24 African governments have made commitments to beneficial ownership transparency in oil, gas, and mining to comply with the EITI Standards. (*"Countries: Implementation Status," EITI.*)

3. Tax Policy and Administration

- Whether taxation helps or hurts will depend on governments' ability to implement effective and equitable tax policy.
- Improving governance around tax collection can help countries close gaps in domestic resources and recover funds previously lost to tax evasion.
- Improving tax enforcement through transparency regarding beneficial ownership, government budgets, and tax audits, and strengthening judicial and executive oversight can help governments retain these funds. (*"Tax and Governance," International Centre for Tax and Development.*)

4. Efficient and Equitable Spending

- Governments should consider how increased public funding could reduce inequality by improving access to social programmes and essential services, especially for poor and marginalized citizens.
- Participatory budgeting improves public service delivery and increases tax compliance. *(Michael Ryan Touchton, Brian Wampler, Tiago Carneiro Peixoto, "Of Governance and Revenue: Participatory Institutions and Tax Compliance in Brazil," World Bank Group.)*

5. Open Contracting

- Efficient and effective procurement is fundamental to good governance.
- Improving procurement practices can save both governments and taxpayers money, freeing up resources for other development spending.

6. Audits

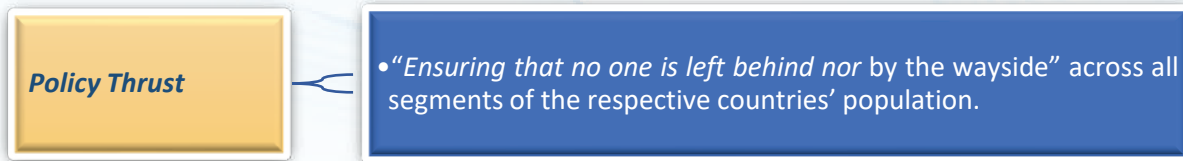
- Publicly available, independent auditing is foundational to good public sector governance.

7. Formalization of the Informal Sector

- An informal sector or grey economy refers to the segment of the economy that is neither taxed nor managed by the government.
- According to the International Labor Organisation (ILO) broader definition, the informal sector refers to "all uncovered economic activities by law or in practice."

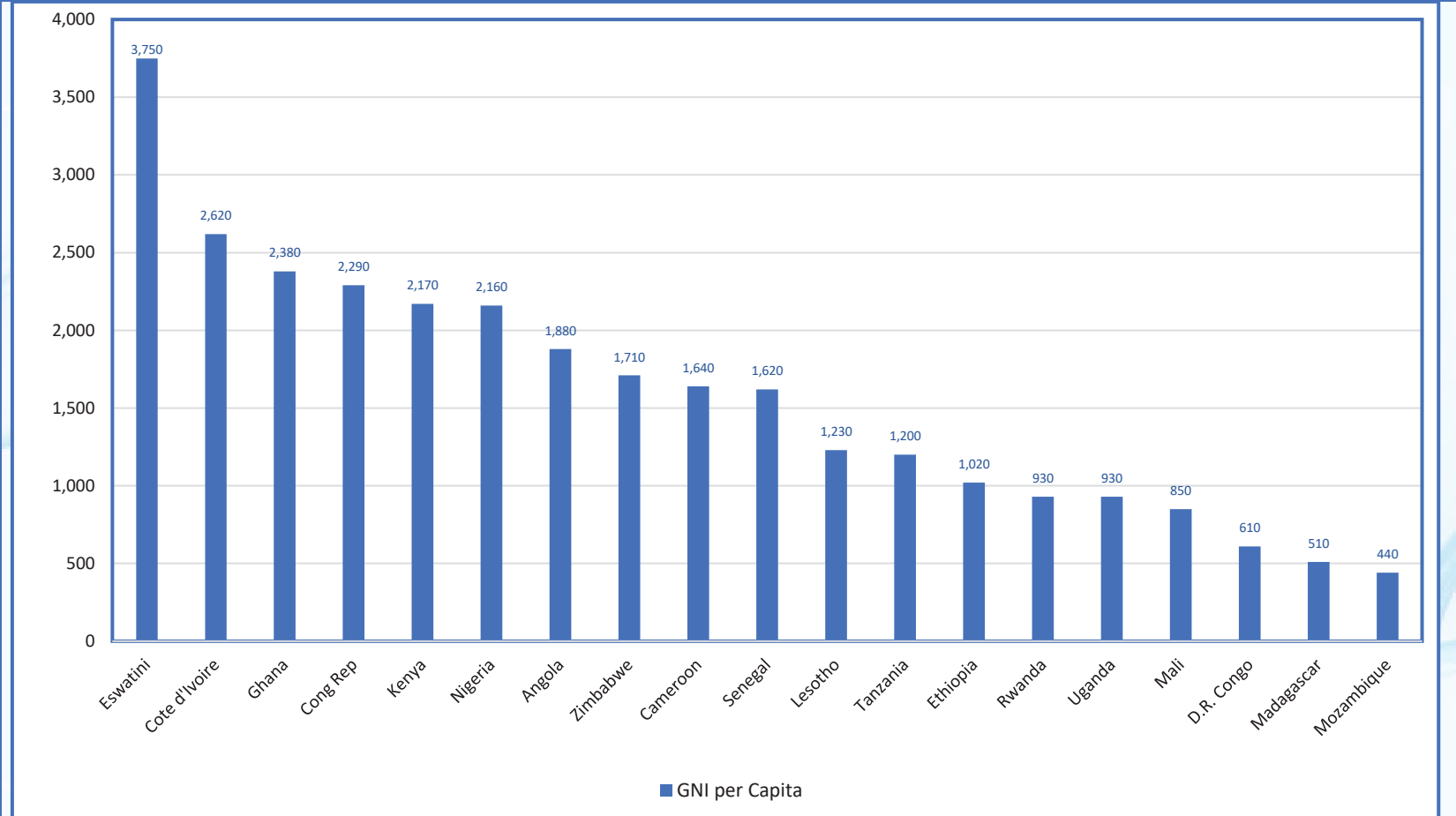
1.2 Background Notes

At the core of Africa's and Tanzania's policy thrust for inclusive growth and sustainable development was the intent of **"Ensuring that no one is left behind nor by the wayside"** across all segments of the respective countries' population. Economic growth is inclusive if there is a simultaneous reduction of POVERTY AND INEQUALITY across all segments of the population.



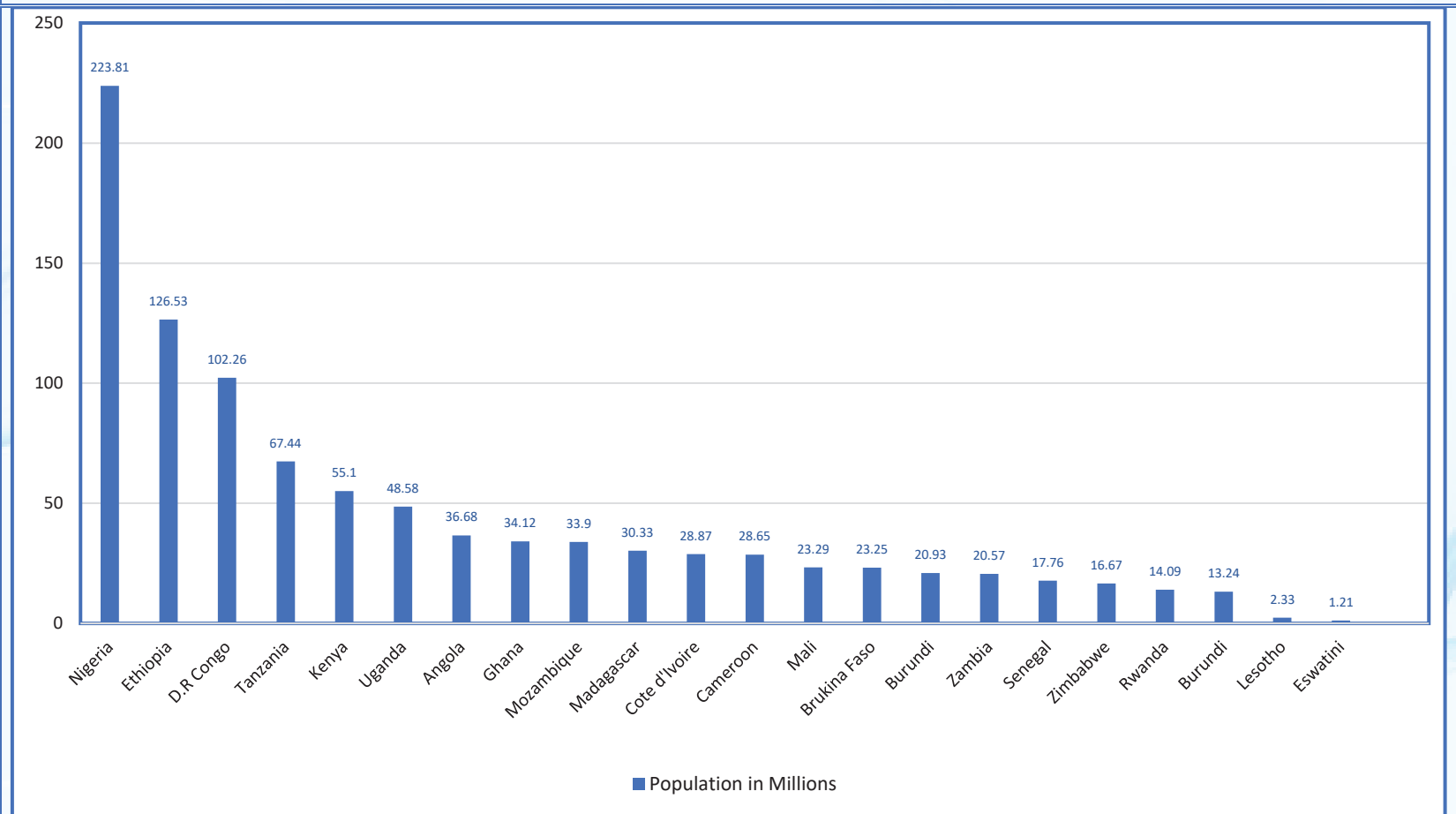
Realizing a demographic dividend requires multiple investments, and the most essential are building the capabilities of people and ensuring their rights and freedoms to achieve their potentials. Young people need the chance to access education and gain experience to succeed in a competitive global workplace, which demands more skills, education, and technical expertise than ever before. While a total of twenty (20) Sub-Saharan Countries have achieved the Lower Middle-Income status, six (6—Botswana, Equatorial Guinea, Gabon, Mauritius, Namibia, and South Africa) have attained the Upper Middle-Income status, and one (1--Seychelles) have attained the High-Income status, they still fall below many other countries in Asia and Latin America and the Caribbean with similar socio-economic conditions (Fig 1). The challenges facing the SSA countries—both Low and Lower-Middle Income (the focus of this Policy Paper)—include economic inequality, joblessness, poverty, and inadequate service provision. The Multilateral Development Bank's support to these countries could help address these challenges head-on.

Figure 1: GNI Per Capita, 2022 in Current US\$-Selected 19 SSA Countries



Source: World Bank—GNI per Capita, Atlas Method—SSA, 2024

Figure 2: Population for Selected 22 Countries—in Millions, 2023



Source: WORLDOMETER, April 2024

Demographic dividends will be constrained without simultaneous investments in decent job creation, good governance, infrastructure, and functioning institutions to foster a conducive investment and business climate for the private sector to thrive. Going forward, the population of Africa will have doubled in size, adding millions young people to the working-age population each year. Creating conditions for decent livelihoods will be an enormous task, especially given that, currently, about 80 per cent of the people who work in these countries are in the informal sector—basically unemployed, underemployed, or irregularly employed. Additionally, the shortage of financial resources will make it difficult to maintain, let alone increase spending on health, education, and nutrition.

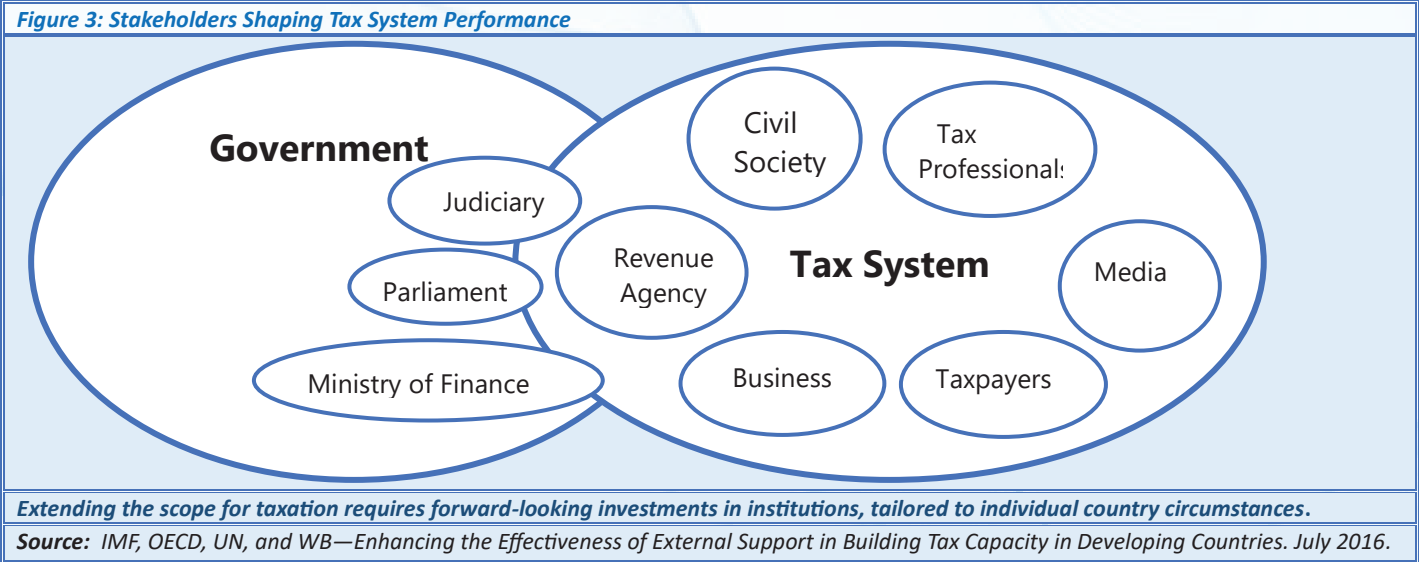
Many African countries including Tanzania need significant financing to close the development and infrastructure gaps, meet the SDGs, and attain the sustained demographic dividends. Historically, many of these countries have relied on fiscal consolidation as a strategy for financing development ostensibly aimed at reducing debt vulnerabilities and boosting resilience. A common dilemma facing governments in these countries is how to meet the sizeable fiscal costs of providing and maintaining infrastructure networks. Over the past decade, developed and developing countries (including Tanzania) have looked to fiscal rules, budgetary reforms, tax policy and administration measures, public-private partnerships, and other innovative financial instruments to raise additional finance for enhancing development expenditure, in particular infrastructure investment.³ Consequently, **revenue mobilisation has remained a key policy priority**. The multilateral development banks (MDBs), development finance institutions, and development partners played and continue to play a key role in providing the needed finance and in helping to attract private investment. But in the context of changing financing trends around the globe, **enhancing domestic resource mobilisation** will remain key for developing countries, and especially those in Sub-Saharan Africa.

³ Teresa Ter-Minassian, Richard Hughes, and Alejandro Hajdenberg; Creating Sustainable Fiscal Space for Infrastructure: The Case of Tanzania; 2008 IMF Working Paper.

2.0 BUILDING TAX CAPACITY AND CREATING FISCAL SPACE FOR DEVELOPMENT EXPENDITURE

Building tax capacity—the policy, institutions, and technical capabilities to collect tax revenue—is central to the role of government in development.⁴ Tax capacity is also integral to achieving the Sustainable Development Goals (SDGs), addressing climate change, and ensuring debt sustainability.

Beyond its fiscal function, tax capacity is associated with accelerated growth and better institutions. Revenue collection enables the state to fund public spending and improve the quality of market-supporting institutions. In this sense, tax capacity is the cornerstone of state capacity



⁴ IMF Staff Discussion Notes; Fiscal Affairs Department. **Building Tax Capacity in Developing Countries.** Prepared by Juan Carlos Benitez, Mario Mansour, Miguel Pecho, and Charles Vellutini September 2023.

According to the IMF assessment, tax revenue has progressed in developing countries, with the average tax-to-GDP ratios increasing by about 3.5 percentage points since the early 1990s to 13.8 percent in 2020.⁵ New empirical evidence suggests that a significant further increase is possible. Achieving this goal will require firm commitment to building better institutions that govern the tax system and manage tax system reforms and improving the design of core taxes.⁶

The domestic revenue increase requires strengthening the design of core taxes—in particular the VAT, excises, personal and corporate income taxes. To that end, the focus should be on tax base broadening by reforming ineffective tax expenditures, ensuring more neutral taxation of capital income, and better use of real property taxes—thus accounting for both efficiency and equity considerations.⁷

Improvement in institutions that govern the tax system and manage tax reform is key to yielding better Domestic Resource Mobilisation (DRM) results.

It calls for, *inter alia*:

- Adequate tax policy units to forecast and analyse the impact of tax policies across all economic dimensions;
- Greater professionalization of public officials working on tax design and implementation;
- Better use of digital technologies to strengthen revenue administrations, and
- Transparency and certainty in how tax policy and administration are translated into legislation.

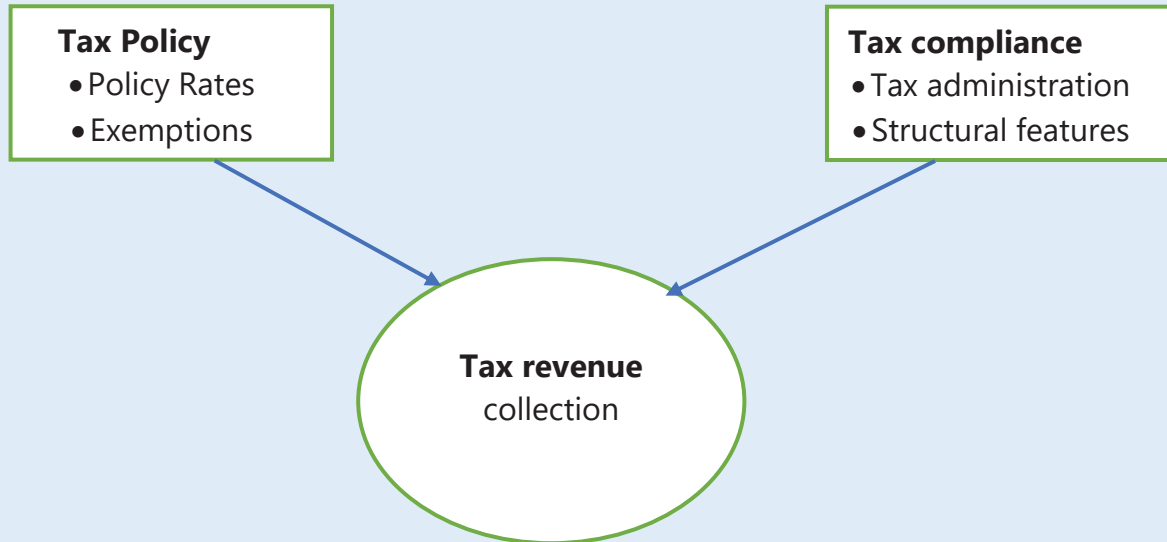
⁵ Ibid.

⁶ Ibid.

⁷ Ibid.

Figure 4: Determinants of Tax Revenue Collection

v



Improving tax policy and tackling tax avoidance require careful preparation and stronger capacity, which take time, resources, and political commitment.

Source: IMF Revenue Mobilisation for a Resilient and Inclusive Recovery in the Middle East and Central Asia; July 2022.

Sub-Saharan African countries' search for creating fiscal space for development expenditures such as additional infrastructure investment within their respective budgets has four broad options at its disposal:

Reprioritization of spending away from less productive forms of expenditure and toward growth-enhancing infrastructure investment and **improvements in expenditure efficiency** within a given overall expenditure envelope;

Identification of **new sources of domestic revenue** which can be used to finance additional infrastructure investments without affecting the overall fiscal balances;

Attracting additional **grants and concessional finance** from bilateral or multilateral sources;

An expansion of **sovereign and concessional borrowing** on domestic or multilateral development banks (MDBs).

Tax policy and administration reforms are usually necessary but not sufficient. To bring sustainable in government revenue, other well-functioning institutions, such as the judicial system, are necessary and other pervasive issues, such as corruption, must be addressed across the public sector. Further, the World Bank may need in-house capacity to conduct analytical and diagnostic work to support tax components in DPOs, especially where the IMF does not have a relevant program.⁸

⁸ Tax Revenue Mobilisation: Lessons from World Bank Group Support for Tax Reform. IEG, 2017. WBG.

2.1 MDBs' Support for Enhancing Domestic Resource Mobilisation (DRM)

In July 2015, the World Bank and the IMF committed to a joint initiative to help countries strengthen their tax systems. Raising additional revenues is crucial to finance development in a sustainable manner. The World Bank-IMF initiative has two pillars: (i) deepening the dialogue with developing countries on international tax issues, aiming to help increase their voice in the international debate on tax rules and cooperation, and (ii) developing improved diagnostic tools to help member countries evaluate and strengthen their tax policies (World Bank 2015b).

One of the pillars of the World Bank-IMF Joint Initiative to Support Developing Countries in Strengthening Tax Systems includes the development of "improved diagnostic tools to help member countries evaluate and strengthen their tax policies". Common diagnostic tools have been developed by the World Bank and the IMF, such as the Tax Administration Diagnostic Assessment Tool, which was launched in 2015 and is now operational in 30 countries. A Tax Policy Assessment Framework is under preparation. Other tools used by the World Bank include the fiscal incidence analysis developed with the Commitment to Equity Assessment, the Custom Assessment Trade Tool kit, an integrated tool for measuring customs performance across countries and over time and the Integrated Assessment Model for Tax Administration.

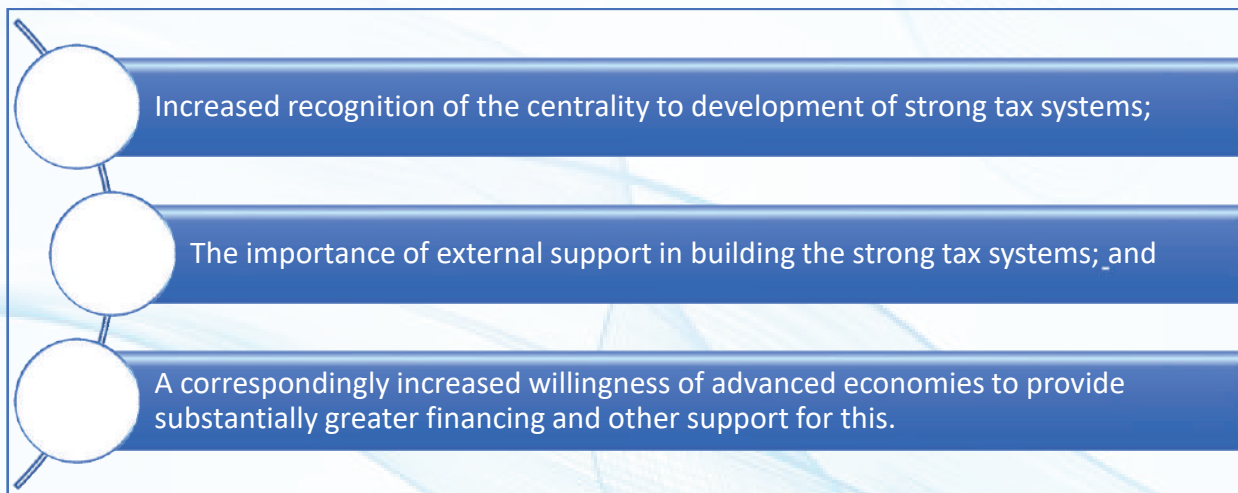
The tax payment aspects of the Doing Business indicators (payments, time, and total tax rate for a firm to comply with all tax regulations) generally guides the business tax work that often includes drafting and enacting tax laws. Harmonization of the legal environment is sometimes addressed through regional projects (as in East Africa).⁹

In April 2016, the IMF, the OECD, the United Nations, and the World Bank Group committed to jointly intensify their cooperation on tax issues and launched the Platform for Collaboration on Tax. The aim of the platform is to support developing countries in strengthening their tax capacity and dealing with key international tax issues.¹⁰

⁹ Ibid.

¹⁰ Ibid.

At the request of the **G20 Finance Ministers**, the International Monetary Fund (IMF), the World Bank Group (WBG), the Organisation for Economic Co-operation and Development (OECD), and the United Nations (UN) in July 2016 jointly submitted a detailed report on modalities for “**Enhancing the Effectiveness of External Support in Building Tax Capacity in Developing Countries**”. The G20 Finance Ministers’ request arose in the context of:



The joint report recognized that, while real progress had been made on increasing domestic resource mobilisation in low-income countries over by then the past two decades, for many countries revenues remained well below levels that were likely needed to achieve the 2030 Sustainable Development Goals and to secure robust and stable growth. The report also took as a fundamental premise that it is not just how much revenue is raised that matters for development and growth, but also how it is raised—and that strong tax systems were key for both equity objectives and enhancing state building.

The IMF and WBG have long cooperated in tax projects. Typically, the IMF focusing on strategic policy advice and support on policy and administration, and the WBG takes the lead on implementation of large and usually loan-based projects and budget support.

The MDBs, OECD, and UN support premised on the fact that strong revenue performance is a core ultimate objective, but a single-minded pursuit of revenue can be deeply counter-productive. The total amount of tax (and non-tax) revenue is the primary concern in meeting development, social, and other spending needs, including those required to achieve the SDGs and infrastructure, while also reducing dependence on volatile and the sometimes-disempowering aid—which may also blunt the incentive to develop own sources of revenue—and securing macroeconomic stability and resilience.¹¹ Strict pursuit of ill-conceived short-term revenue targets, however, is a common source of bad practice—for instance, the denial of VAT refunds, the harassment of taxpayers, or offering tax amnesties that undermine the credibility of the wider tax system. This damages economic activity and feeds a vicious cycle of mistrust between taxpayers and tax authorities.

An additional premise was that an indispensable prerequisite to improving tax capacity is enthusiastic country commitment.

¹¹ IMF, OECD, UN and WB—Enhancing the Effectiveness of External Support in Building Tax Capacity in Developing Countries. Prepared for Submission to G20 Finance Ministers, July 2016.

Given such commitment, the report points to five key enablers to building tax capacity:

- A coherent revenue strategy as part of a development financing plan;
- Strong coordination among well-informed and results-oriented providers;
- A strong knowledge and evidence-base;
- Strong regional cooperation and support; and
- Strengthened participation of developing countries in international rules setting.

The Joint MDBs, OECD and UN report arrived at a number of recommendations for measures to strengthen or achieve those enablers.

The primary recommendations include I:

- Options through which the G20, MDBs, International Organisations and other development partners can encourage political support for tax systems development;
- The development of country-owned medium-term revenue strategies, or tax reform plans depending on country circumstances;
- Support to non-government stakeholders;
- Support by MDBs and development partners to increase managerial, as well as technical skills in taxation agencies.

The primary recommendations include II:

- Various approaches to developing better coordination and collaboration among providers, and avoidance of fragmented support and approaches;
- Intensification of work by the Platform for Collaboration on Tax partners and others to produce comparable and reliable data;
- Increased partnerships and support for regional tax organisations; and
- Support to developing countries to facilitate meaningful participation in international tax policy discussions and institutions.

Against this background, this policy paper analyses SSA's domestic resource mobilisation by focusing on the performance of various taxes overtime, identifying additional sources of revenues including from resource-intensive sectors, compliance, and associated challenges, the use of technology in tax collection; and broadening of the tax base by formalisation of the informal sector. The paper goes further to analysing the role played by IDA 20 in enhancing domestic resource mobilisation and their implications for IDA 21.

2.2 Concerted IDA Action on DRM

DRM has been a focus of IDA action since the adoption of Country Policy and Institutional Assessment (CPIA) ratings in 1980. DRM is one of the 16 CPIA criteria (see Box 1, below), under the public sector management and institutions cluster, that determine the allocation of IDA resources and is used to evaluate the performance of IDA action.

Clusters of the CPIA Criteria:

- Economic Management
- Structural Policies
- Policies for Social Inclusion/Equity
- Public Sector Management and Institutions.

It is estimated that some 32 IDA countries received support for various aspects of DRM between 2005 and 2019 (IDA 17 and 18) through one or in combination of development policy operations (DPO), investment projects, or the IFC's advisory services on business taxation (World Bank, 2023c). IDA reforms of this era have endured small incremental success as opposed to overall commitment targets of lifting tax yields above the 15 percent threshold.

Combined with an average disbursement to commitment ratio of 70 percent (Figure 10, below) during IDA 17 and 18, the actual sums spent on DRM are likely to have been considerably lower. As a result:

- Concerted IDA action and indeed concrete outcomes have at best been mixed and at worst sparsely existent.
- Limited prioritization of DRM funding has partly mirrored the initial coupling of DRM with other broader reform areas that have tended to obscure focus, and specificity of action over the years.

While IDA 17 saw exclusive support for DRM in small island and fragile and conflict-affected states (FCS) as well as the expansion of DRM support to resource-rich countries under the auspices of the Extractive Industries Transparency Initiative (EITI), the continued bundling of ideally concrete and specific DRM reforms with other broader sub-sector initiatives compounded the difficulties of aligning DRM action with operational targets and objectives leading to an array of ill-targeted and under-focused DRM action.

**IDA 18's
targeted
approach
to DRM:**

- Succeeded in demonstrating the utility of a coordinated push for improved policy outcomes;
- This sowed the seeds for more ambitious targeting and strengthened coordination in IDA 19 and 20;
- Both of which have sought to reinforce DRM targets by retaining the same operational target and expanding the breadth of operations and technical assistance to recipient countries.

IDA 19 (2019-2021) extended DRM support to 36 countries beyond its baseline target of 32 (World Bank, 2023). A combination of lessons from reforms discontinuity and optimistic forecasting of the long-term success of IDA 19's DRM reforms saw a consolidation of DRM reforms in IDA 20. The latter initially aimed to achieve a tax-GDP ratio of at least 15 percent in the medium term in some 15 IDA countries through support for equitable (fair and progressive) revenue policies. A midterm appraisal of IDA 20 in November 2023, found

the coverage of DRM support to have extended to 21 countries (World Bank, 2023), with recipients who had been receiving support since IDA 18 finally recording nominal improvements in their DRM. IDA 20 continues the institutionalization of policy commitments aimed at supporting DRM and broader Governance and Institutions.

SSA accounts for:

- 26 of the 36 countries in recipient of DRM support under IDA 20;
- Almost all SSA IDA recipients with the exception of Kenya have tax yields of below the 15 percent threshold.

3.0 DOMESTIC RESOURCE MOBILISATION (DRM) IN IDA RECIPIENT COUNTRIES

3.1 Introduction and Overview of DRM Reforms in IDA Countries

DRM—the process through which countries raise and spend their own funds to provide for their people—is the long-term path to sustainable development finance. DRM not only provides governments with the funds needed to alleviate poverty and deliver public services but is also a critical step on the path out of aid dependence. Through domestic resource mobilisation, countries accelerate their economic growth by raising and spending their own funds for public goods and services, like schools, hospitals, clean water, electricity, and infrastructure – all critical to helping people sustainably rise out of poverty. Countries' investment in their own public goods and services, particularly infrastructure, is also essential to attracting private investment and laying the foundation for long-term economic growth. DRM does not necessarily mean new

taxes or higher tax rates. Governments often see their revenues rise through improved audits or simplified filing processes. Successful DRM programmes are highly cost-effective; they return many times what is invested in them.

Tax components in World Bank operations have been designed to (i) enhance revenue to enable fiscal consolidation or create/maintain fiscal space for priority expenditure (in 60 out of the 80 reviewed Development Policy Operations (DPOs)) and/or (ii) improve investment climate or strengthen export competitiveness and improve trade integration. Together these objectives were expected to contribute to accelerated growth and higher employment while fiscal consolidation was often

considered a prerequisite for securing sustained budget support and laying the foundation for future growth.¹²

While government ownership is a prerequisite for any policy reform, it is particularly important for politically sensitive tax reforms. For many governments and their tax components, success depended on government ownership of the objectives and the program. Tax reforms are not only technical, and institutional but also political and government support for these reforms may fluctuate during project life. Design, monitoring, and supervision should take that into consideration. Commitment can be supported through close alignment with the government's reform program. Tax administration measures that can be introduced under the executive authority can deliver short-term results.¹³

A crisis can be an opportunity to further tax reforms and calls for flexibility. The negative impact of the 2008 global economic crisis on the growth and fiscal position of a number of countries prompted large budget

support from the international financial institutions to maintain fiscal space for priority public expenditure. For several SSA countries, having a comparatively low tax rate for their level of economic development and a long history of failed tax reforms, the dire fiscal situation may provide incentives to make politically sensitive tax reforms to boost revenues.¹⁴

Specifically, *domestic resource mobilisation, i.e., increasing government revenues through taxation and other non-debt income sources* is essential in allowing countries to own and flexibly chart policies that address their specific development challenges while mitigating the risks of debt distress. However, on average SSA collects only 16.3% of GDP as per Figure 5 below (16% for the whole African continent) from taxes compared to Asian and Pacific economies (19.1%), Latin America and the Caribbean (LAC) (21.9%), and the OECD (33.5%). Only 12 African countries have tax-to-GDP ratios of

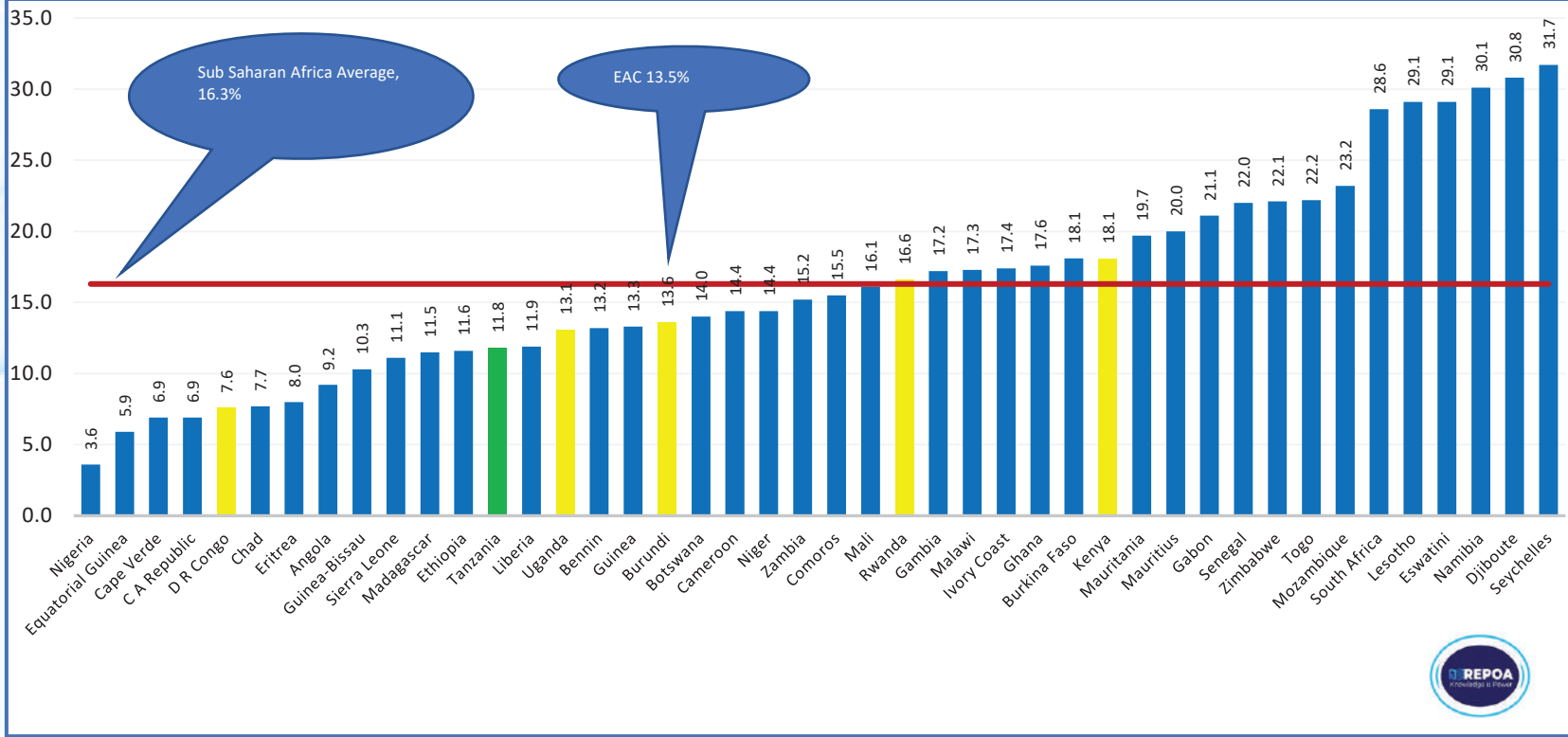
¹² Tax Revenue Mobilisation: Lessons from World Bank Group Support for Tax Reform. IEG, 2017. WBG.

¹³ Ibid.

¹⁴ Ibid

above 20%. Figure 5 provides details of the tax-to-GDP ratios of Sub-Saharan African countries.

Figure 5: Tax performance % GDP in Sub-Saharan Africa (LICs, LMICs, MICs)



Source: OECD/AUC/ATAF, 2020



3.2 Case Study 1—Tanzania (At 11.8% Tax/GDP)

Tanzania has several macroeconomic advantages that could support a successful transition to upper middle-income status. Tanzania is one of the few economies in the region that did not experience a contraction in 2020 due to covid-19 pandemic. The country's macro-economic indicators indicate that its modest risk of debt distress offers some space to prudently utilize debt financing. Further, the government's fiscal position remains relatively strong and stable, and international reserves are at a comfortable level. To capitalize on its sound macroeconomic policy environment and to lay the foundation for robust, inclusive, and sustainable long-term growth, the government should seize the opportunity to implement a more ambitious human capital development agenda. Creating adequate fiscal space to invest in human capital in a context of

persistently high poverty rates, significant downside risks to the economic outlook, and limited budgetary resources will require reforms both to the key elements of its domestic revenue mobilisation and public spending.¹⁵ Investing in human capital is indeed important given its large population relative to its counterparts as depicted in Figure 2 above.

Tanzania has made impressive progress in boosting domestic tax revenues in recent years and levels of domestic revenue mobilisation now compare well with comparable countries in the region. Tanzania's domestic resource mobilisation has grown consistently over the last two decades. Specifically, the country's DRM—Tax and non-tax revenues increased 26-folds from TZS 0.8 to 20.6 trillion between 1999/00 and 2020/21; and is projected to rise to TZS 35.7 trillion in 2025/2026 as per Figure 6 and 7 below.

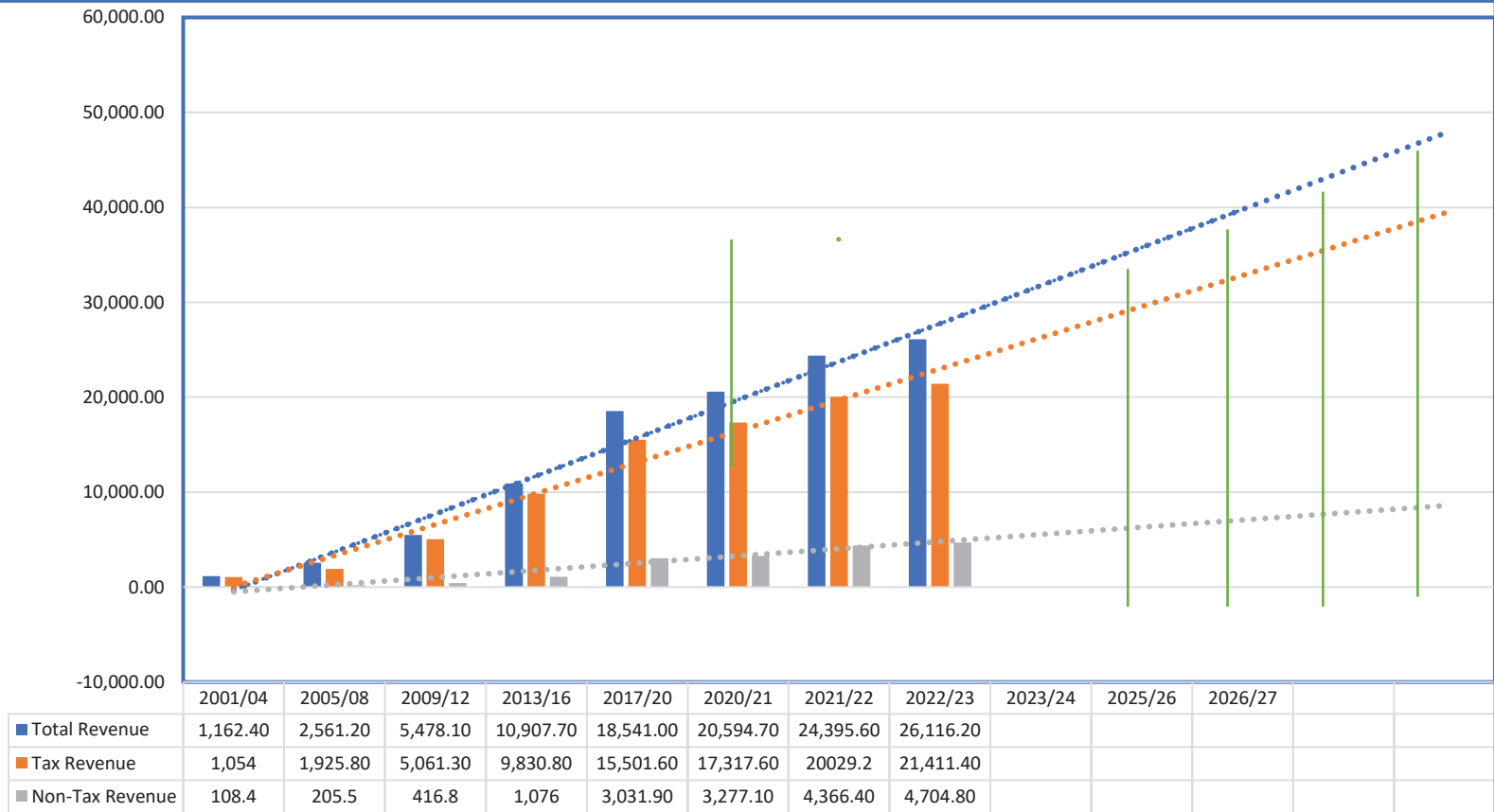
¹⁵ **TANZANIA Economic Update**--The Efficiency and Effectiveness of Fiscal Policy in Tanzania. Issue 19, 2023; World Bank Group

Closing compliance gaps can help bolster revenues while establishing a fairer, more efficient tax system. Tanzania's improved tax collection helped narrow the tax gap from 8 percent of GDP in 2000 to 11.8 percent of GDP in 2023. The government can further increase tax productivity by adjusting rates, rationalizing exemptions, expanding the tax base, leveraging digital technologies to enhance tax administration, and improving compliance management. Introducing a more rigorous system for taxing income from capital and immovable property could bolster the government's revenue position while updating cross-border taxation policies could reduce the risks associated with base erosion and profit-shifting by multinational corporations.

Strengthening tax administration at the top of the income distribution would improve the tax system's equity while increasing revenue mobilisation and reinforcing the social contract. Building the capacity of the tax authorities will be essential to expand collection efficiently and equitably and could lay the groundwork for further reforms. The authorities can complement the ongoing e-filing rollout by enhancing the integrity of the taxpayer database, which will be necessary to expand registration. Improving data collection and data analytics, adopting a risk-based approach to compliance management, and hiring and training more auditors could help ensure that all registered taxpayers report and pay their true tax liabilities.¹⁶

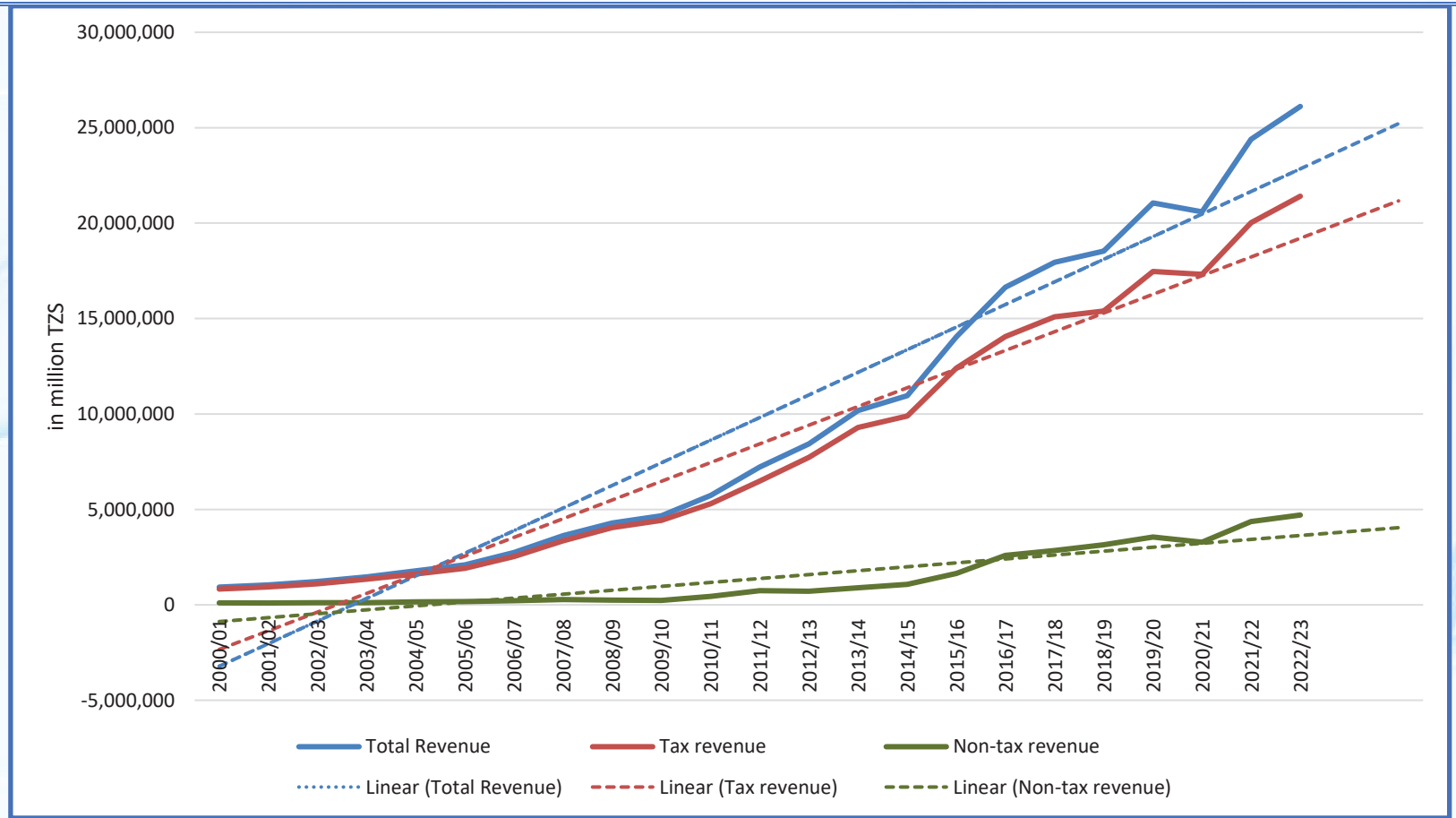
¹⁶ **TANZANIA Economic Update**--The Efficiency and Effectiveness of Fiscal Policy in Tanzania. Issue 19, 2023; World Bank Group

Figure 6: Tanzania's Domestic Revenue Performance in Billion TSHS



Source: Ministry of Finance

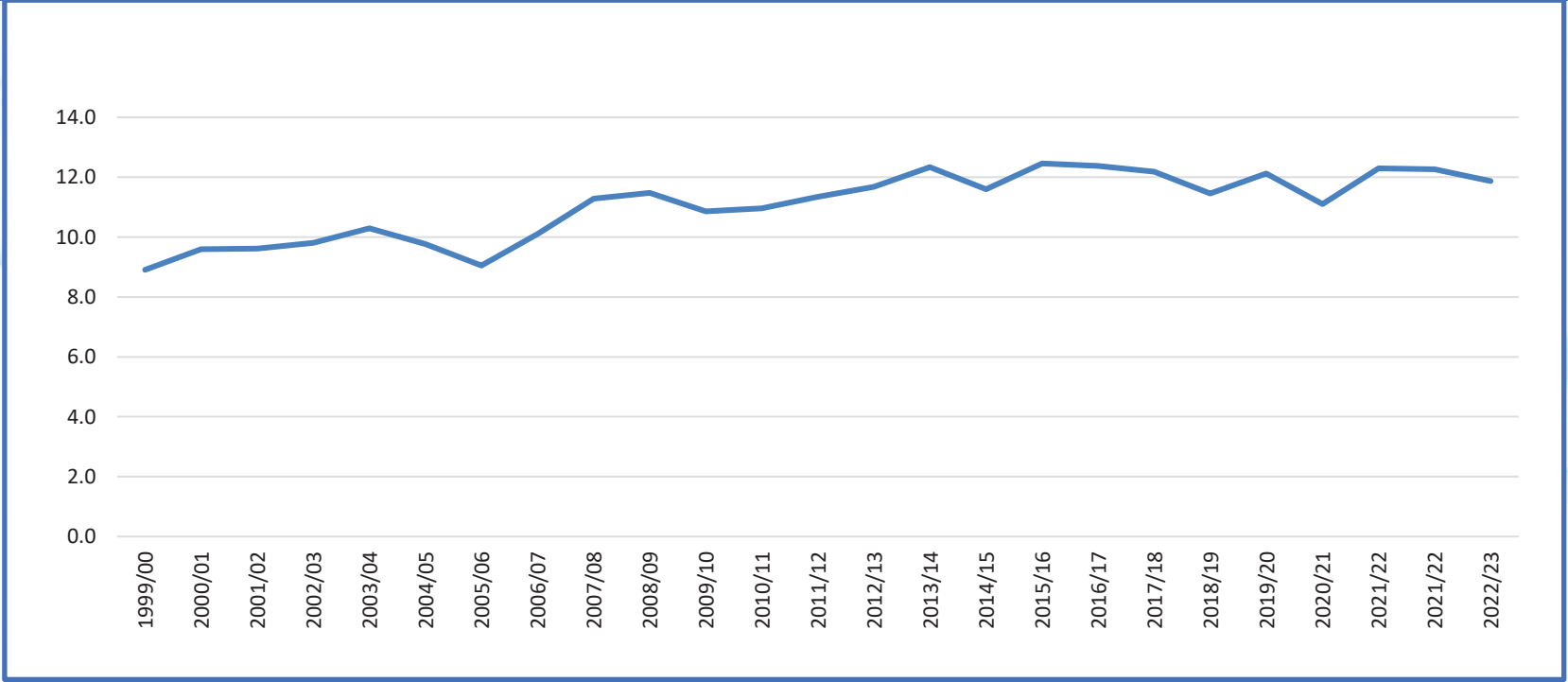
Figure 7: Tanzania's Domestic Revenue Performance in Billion TSHS



Source: Ministry of Finance

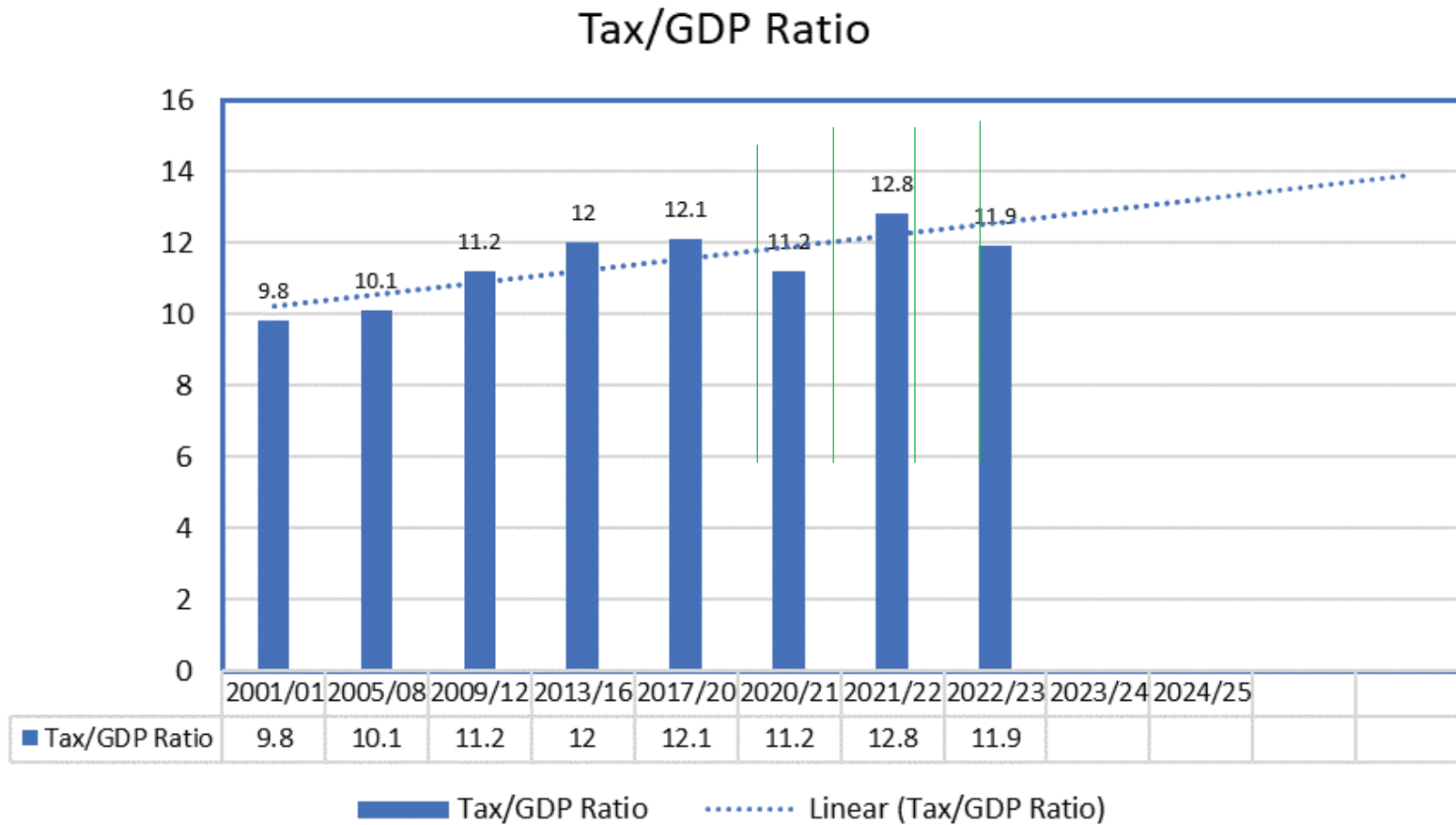
However, as per Figure 5, Despite a revenue-to-GDP ratio of 14.4%, Tanzania’s domestic revenue performance, particularly taxation, compared to comparator SSA countries remains well below the averages: at 11.8% of GDP the country’s tax performance is well below the SSA average of 16.3% and below the EAC average of 13.5%. Figures 8 and 9 show the performance of Tanzania’s tax ratios to GDP, along with their relative trends over time.

Figure 8: Tax/GDP Ratio



Source: Ministry of Finance & Bureau of Statistics

Figure 9: Tax / GDP Ratio



Source: Ministry of Finance & Bureau of Statistics

Tanzania made some progress in expanding tax collection, with the tax-to-GDP ratio increasing from 10 percent in 2004/05 to 11.8 percent in 2022/23. Meanwhile, public spending has increased from 12.6 percent of GDP to 18.2 percent of GDP, which is still lower than the average for Sub-Saharan Africa, low-income countries, and lower-middle-income countries.

The recent global crises have also exacerbated existing societal inequalities and highlighted the importance of raising revenues in an efficient and equitable manner. As in the rest of the world, the impact of the pandemic has been unequal, falling disproportionately on the poor, the vulnerable, and those in contact-intensive sectors. Meanwhile, rising food and fuel prices resulting from the war in Ukraine have hit vulnerable households the hardest.

Against this background, emerging markets and developing economies like Tanzania have been caught up in global monetary tightening policies that were implemented to soften inflationary pressure. These policies have resulted in higher borrowing costs, tighter credit conditions, and increased financial stress. Capital outflows have also impacted countries, causing official gross reserves to deplete and exerting forex pressures. The report on Tanzania Economic Update shows that countries such as Tanzania can strengthen the efficiency and effectiveness of tax and expenditure policies to improve policy outcomes and support inclusive and sustainable growth. Increasing the efficiency and equity of domestic resource mobilisation is, therefore, crucial to help mitigate the negative distributional effects of the pandemic and higher commodity prices.

Tanzania's most urgent reform priorities include measures to improve the efficiency and effectiveness of expenditure programs and to boost domestic revenue mobilisation.¹⁷

¹⁷ **TANZANIA Economic Update**--The Efficiency and Effectiveness of Fiscal Policy in Tanzania. Issue 19, 2023; World Bank Group.

The WB/IDA's recommendations are that the government has the following options in that regard:

- Should adjust VAT, corporate income tax, and excise tax rates to increase domestic revenue mobilisation;
- Excise taxes on tobacco should be carefully re-evaluated to balance revenue and public health objectives;
- Strengthening taxation on wealthier households is vital to improve the equity of the tax system;
- Reinforcing the tax administration's auditing capacity will be necessary to boost collection efficiency and enhance distributional equity, and registration thresholds should also be adjusted to broaden the tax base; and
- The Commitment to Equity (CEQ) methodology could be used to assess the impact of proposed fiscal policy changes in countries.

Further, the WB/IDA notes that Tanzania's economy has been steadily expanding, and the fiscal policies have been successful in reducing income inequality, but there is still room for enhancing these policies to improve public spending in priority programs.

3.3 Case Study 2—IDA SSA Countries with Tax Yields Below 15% of GDP

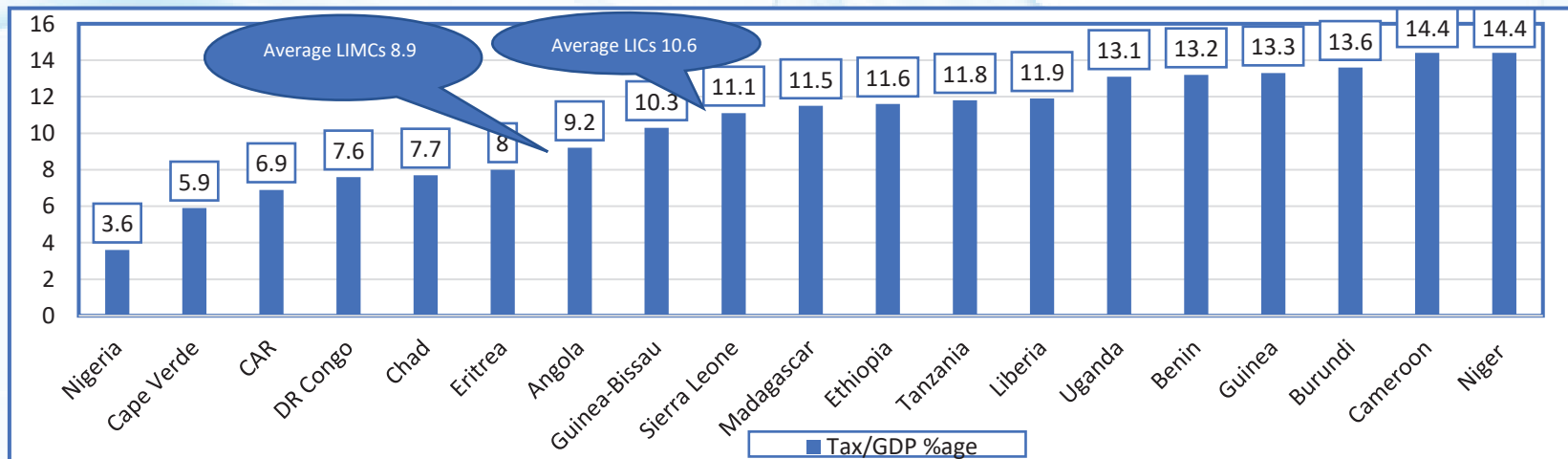
As earlier indicated, Sub-Saharan Africa has been hit by a cascading series of shocks, including the COVID-19 pandemic, Russia's invasion of Ukraine, and increasingly frequent weather events. These shocks have amplified longstanding economic and social challenges and exacerbated fiscal vulnerabilities. Under unchanged fiscal policy, the region's debt-to-GDP ratio will continue to trend upward, increasing by more than 10 percentage points over the next five years. Significant fiscal reforms, especially for countries with tax yield is below 15% of GDP—countries in Figure 10 below, are

urgently needed to rebuild buffers and preserve the sustainability of public finances, while also achieving the region's development goals.

Although fiscal rules and medium-term budget frameworks are in place in most of these countries, their ability to steer fiscal policy remains limited. Evidence suggests that policy lacks an effective anchor and is excessively focused on short-term goals. Hence, four areas of concern are highlighted:

- Fiscal balances are relatively unresponsive to rising debt.
- Deviations from fiscal plans tend to be significant, especially at longer time horizons.
- Countries in sub-Saharan Africa—mostly under this category—have difficulty sustaining elevated primary surpluses.
- Compared to other regions, fiscal deficit ceilings are breached more frequently and by a larger margin.

Figure 10: SSA LICs and LMICs with Tax/GDP Yields Below 15%, 2020



Source: OECD/AUC/ATAF, 2020

Table 1: Tax Yields and Buoyancy Levels for Countries with less than 15% of Tax/GDP

Country	Tax % of GDP, 2020	Tax Buoyancy, 2021	CIT Buoyancy, 2021	PIT Buoyancy, 2021	Taxes on Incomes, etc. % revenue	Taxes on International Trade % revenue	Taxes on goods & services % revenue
Nigeria	3.6	-4.66	2.05	-0.05	--	--	--
Cabo Verde	5.9	0.89	1.72	0.72	19.48	12.85	29.51
C A Republic	6.9	3.11	5.69	-9.0	10.74	15.86	30.15
D. R. Congo	7.6	--	--	--	--	--	--
Chad	7.7	2.2	7.5	-0.24	--	--	--
Eritrea	8.0	-0.25	-2.99	-2.19	--	--	--
Angola	9.2	0.25	-2.38	2.18	34.76	2.87	5.45
Guinea-Bissau	10.3	0.76	4.36	10.2	18.49	18.22	23.41
Sierra Leone	11.1	0.12	1.08	-0.64	--	--	--
Madagascar	11.5	1.23	1.89	1.0	22.48	13.13	51.67
Ethiopia	11.6	-0.56	-0.44	0.2	21.28	17.81	30.29
Tanzania	11.8	0.26	0.02	0.05	26.32	6.74	43.01
Liberia	11.9	-0.29	0.69	0.97	--	--	--
Uganda	13.1	0.76	3.02	1.24	29.7	8.59	42.49
Benin	13.2	0.22	0.10	-0.53	9.57	41.22	8.5
Guinea	13.3	-0.2	--	1.25	10.99	35.79	20.48
Burundi	13.6	3.9	0.57	0.67	18.15	17.42	37.99
Cameroon	14.4	0.08	-1.39	-0.15	21.77	11.24	43.29
Niger	14.4	-042	-2.31	-0.13	23.77	36.37	20.94

Notes:

- **Tax buoyancy**—Tax buoyancy is an important measurement of tax revenue’s sensitivity to changes in GDP. The sign of tax buoyancy is expected to be +ve. A -ve tax buoyancy sign implies that revenues are not a close function of the domestic economy.
- **CIT Buoyancy**—Corporate Income Tax buoyancy is an important measurement of the CIT revenue’s sensitivity /responsiveness / elasticity to changes in GDP,
- **PIT Buoyancy**—Personal Income Tax buoyancy is an important measurement of the PIT revenue’s sensitivity / responsiveness / elasticity to changes in GDP.

Source: OECD/AUC/ATAF, 2020; and USAID Country Dashboard for Respective Countries, March 2024

Policymakers in these countries face a fundamental tension between elevated development needs and low domestic resource mobilisation—this creates difficult policy trade-offs and may lead to excessive indebtedness. In addition, calibrating fiscal targets is much more challenging in the face of large and unpredictable shocks, such as volatile commodity prices, weather events, or conflicts. Also, political instability and

Table 2: Resource-Intensive Countries —Oil Exporters

Income Cluster	Country	Average Tax as %age of GDP
Lower-Middle Income Countries	<ul style="list-style-type: none"> ➤ Nigeria ➤ Chad ➤ Angola ➤ Cameroon 	➤ 8.7

Source: IMF-REO SSA, April 2024

institutional weaknesses often get in the way of fiscal adjustment (when needed) and tend instead to promote destabilizing policy choices. Finally, tight financing conditions and reliance on volatile donor flows limit the

extent to which shocks can be accommodated and the scope for a more gradual approach to adjustment.¹⁸

As per table 1 above, about a quarter of these economies—especially those with positive tax buoyancy indicators—still have some fiscal space and can use it to continue making vital investments in human and physical capital. At the opposite end of the spectrum, a few countries display very large adjustment needs, and it is unlikely that fiscal consolidation alone will be enough to ensure fiscal sustainability (nor would it be desirable). In these specific cases, the necessary adjustment should be part of a comprehensive strategy to rebuild fiscal buffers, possibly including debt reprofiling or restructuring.

¹⁸ Fabio Comelli, Peter Kovacs, Jimena Montoya, and Arthur Sode, led by Antonio David and Luc Eyraud: *Navigating Fiscal Challenges in Sub-Saharan Africa—Resilient Strategies and Credible Anchors in Turbulent Waters*. IMF, 2023.

In these countries, *domestic resource mobilisation* can play a greater role in the adjustment process without necessarily undermining growth to the same extent as seen elsewhere. Careful selection of tax instruments can mitigate the possible negative effects on inequality. In some cases, complementary measures are also needed on the expenditure side, notably by reforming costly and poorly targeted energy subsidies.¹⁹

Table 3: Other Resource Intensive Countries

Income cluster	Country	Average Tax as %age of GDP
Lower-Middle Income Countries	➤ Tanzania ➤ Benin	➤ 12.5
Low-Income Countries	➤ Central African Republic ➤ D.R. of the Congo ➤ Eritrea ➤ Guinea Bissau ➤ Sierra Leone ➤ Liberia ➤ Guinea ➤ Niger	➤ 10.3

Source: IMF-REO SSA, April 2024

DRM volatility is also significantly higher in these countries—as per Table 1 above. Most of these countries rely, to a large extent, on commodity revenues, taxes on international trade, and development aid, which are much more volatile revenue sources than income or property taxes (more common in advanced economies).

Lastly, the majority of resource-intensive economies in SSA are in this category of countries as per Tables 2 and 3 above. The unique characteristics of the natural resource sector exacerbate challenges to international taxation. While international tax issues are not unique to the extractives sector, the inherently weak capacity and revenue-raising potential of the sector make the issues more pertinent in these SSA countries. The dominant role of MNEs in the extractives sector increases the prospects of transfer pricing and other aggressive tax planning and tax minimization schemes such as trade mis-invoicing, trade-in intangibles, and thin capitalization. The prevalence of tax incentives for mining investments also constitutes a significant

¹⁹ Ibid.

challenge. Examples of such incentives include CIT holidays, reduced royalties, and royalty holidays.²⁰

3.4 Case Study 3—IDA SSA Countries with Tax Yields Above 15% OF GDP

The SSA and IDA recipient countries in this category have a much higher revenue buffer than the earlier category of countries—as per Figure 9 and Table 3 below. An interesting element is that a good number of countries under this category are Low-Income Countries. The best case, hence, is that of Mozambique which has a high tax/GDP ratio of 23.2 (Figure 11 below) despite its per capita GDP level of \$440 (Figure 1 above)—the lowest in the category of SSA countries under consideration. It is, therefore, interesting to briefly view the IDA experience with Mozambique.

Enhancing revenue generation capacity was a sub-objective of Mozambique’s second PRSC series (PRSC 3-5). A Central Revenue Authority that integrates the

general administration of taxes and customs in a single entity was created (PRSC 3 prior action) by law and regulations in September 2006 and became operational in November 2006. Project development objective indicators (Creation of the Central Revenue Authority and increase revenue as a share of GDP) were met; the revenue-to-GDP ratio reached 17.8 percent in 2009 against a target of 16.8 percent and compared with a baseline of 15.6 percent in 2006.²¹

Tax reform implementation was good and characterized by continuous efforts to improve the efficiency of the tax administration, consolidation of taxes, and modernization of customs procedures to facilitate trade. As part of the reforms, the 2007–2010 Information Technology Plan (PDTI) for the Central Revenue Authority provided for the development of an adequate system to manage and control information that supports all taxes (Prior Action PRSC 4). Tax legislation was also strengthened following the December 2006 approval of

²⁰ AfDB: The Impact of International Tax Reforms on Natural Resource Revenue Mobilisation in Africa; 2023.

²¹ Tax Revenue Mobilisation: Lessons from World Bank Group Support for Tax Reform. IEG, 2017. WBG

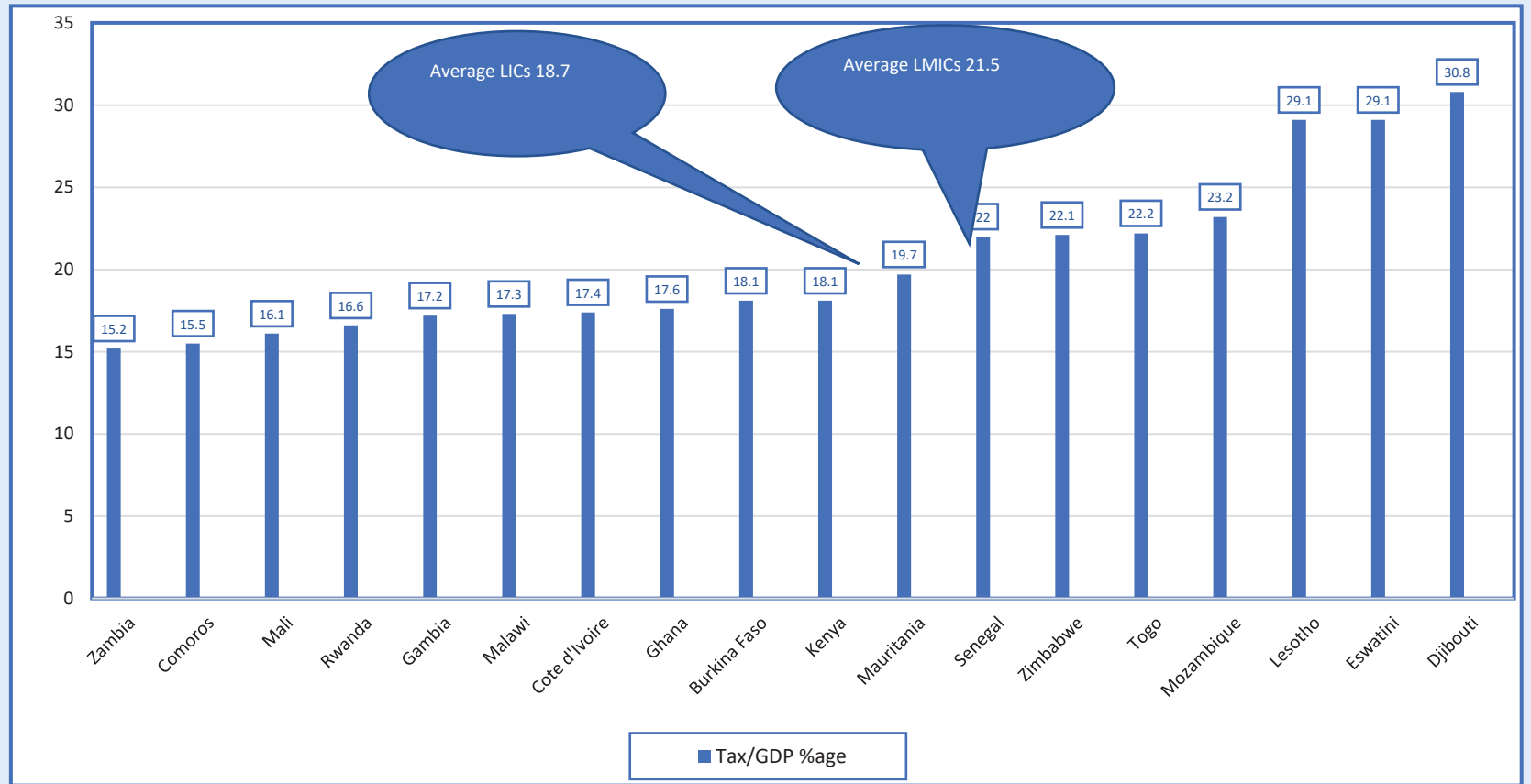
new legislation on the fiscal regimes for the mining and oil sectors, the new laws became effective in mid-2007 and regulations have since been approved to implement them. In December 2007, parliament also approved new tax laws on value-added tax and personal income tax. The new value-added tax (VAT) Code simplified the previous code and clarified the list of VAT-exempt transactions and exemptions for specific goods. The new Personal Income Tax Code simplified the system of direct

income taxation and updated the income thresholds and tax brackets.

A further note is that without a detailed analysis of the impact of tax reforms, it is not possible to attribute the increase in revenue-to-GDP ratio solely to tax reforms as other important factors affect government revenue, *especially in a resource-rich country*. It also not possible to attribute progress to specific tax reforms and/or donor interventions.²²

²² Ibid.

Figure 11: SSA LICs and LMICs with Tax/GDP Yields Above 15%



Source: OECD/AUC/ATAF, 2020

Table 4: Tax Yields and Buoyancy Levels for Countries with more than 15% of Tax/GNI

Country	Tax % of GDP	Tax Buoyancy	CIT Buoyancy	PIT Buoyancy	Taxes on Incomes % revenue	Taxes on International Trade % revenue	Taxes on goods & services % revenue
Zambia	15.2	0.54	3.15	0.92	39.05	4.92	22.64
Comoros	15.5	0.69	1.12	-1.12	--	--	--
Mali	16.1	0.33	0.43	0.71	35.4	10.71	39.27
Rwanda	16.6	-0.44	-0.42	0.64	24.97	4.65	27.67
Gambia	17.2	-0.18	-1.49	2.09	9.73	32.44	28.29
Malawi	17.3	-0.21	-0.2	1.32	38.4	6.58	37.17
Cote d'Ivoire	17.4	0.35	0.55	-8.36	24.25	23.92	--
Ghana	17.6	0.42	1.64	0.18	43.03	10.0	32.27
Burkina Faso	18.1	0.24	-0.06	1.31	25.32	10.63	40.24
Kenya	18.1	-0.08	-0.38	-0.21	30.76	7.83	32.06
Mauritania	19.7	-0.11	-0.65	-1.02	--	--	--
Senegal	22.0	0.43	1.56	0.6	24.86	12.51	40.8
Zimbabwe	22.1	1.52	-0.29	0.6	33.32	7.66	41.23
Togo	22.2	0.29	1.88	1.87	15.97	15.94	40.89
Mozambique	23.2	0.12	-0.19	1.0	34.71	6.17	35.57
Lesotho	29.1	-2.07	2.22	-0.28	23.29	8.76	31.37
Eswatini	29.1	-0.5	-0.59	1.49	--	--	--
Djibouti	30.8	-0.51	--	--	--	--	--

Notes:

- **Tax buoyancy**—Tax buoyancy is an important measurement of tax revenue's sensitivity to changes in GDP. The sign of tax buoyancy is expected to be **+ve**. A **-ve** tax buoyancy sign implies that revenues are not a close function of the domestic economy.
- **CIT Buoyancy**—Corporate Income Tax buoyancy is an important measurement of the CIT revenue's sensitivity /responsiveness/elasticity to changes in GDP,
- **PIT Buoyancy**—Personal Income Tax buoyancy is an important measurement of the PIT revenue's sensitivity/responsiveness/elasticity to changes in GDP.

Source: OECD/AUC/ATAF, 2020; and USAID Country Dashboard for Respective Countries, March 2024

Table 5: Resource-Intensive Countries—OIL Exporters		
Income Cluster	Country	Average Tax as %age of GDP
Lower-Middle Income Countries	➤ Congo Republic	➤ N/A
Low-Income Countries	➤ South Sudan	➤ N/A
Source: IMF-REO SSA, April 2024		

Table 6: Other Resource-Intensive Countries		
Income cluster	Country	Average Tax as %age of GDP
LIMCs	➤ Zambia ➤ Zimbabwe	➤ 18.6
LICs	➤ Burkina Faso ➤ Mali	➤ 17.1
Source: IMF-REO SSA, April 2024		

A key element that is common to both categories of countries is the revenue pervasiveness of tax incentives and exemptions especially for the resource-intensive countries. Competition for inbound investment typically manifests itself through tax incentives. SSA countries provide a vast array of tax incentives in a bid to attract both domestic and foreign investment. The incentives are incorporated into tax legislation (general or 'benchmark' laws), specific mining legislation,

and individual (project-by-project) mining contracts. Multiple tax incentives distort the economic efficiency (labour supply and investment decisions) and technical efficiency (due to the ensuing costs to tax administration) of tax policy.²³

Tax policy employs various mining fiscal instruments to provide incentives. These include taxes on income (e.g. corporate income tax, resource rent taxes, withholding taxes), taxes on production (e.g. mineral royalties), tariffs on trade (e.g. tariffs on import of capital inputs), and others (e.g. stabilization of fiscal terms, competition for managerial and technical skills). The corresponding tax incentives include income tax holidays, accelerated depreciation, investment allowances or tax credits, longer loss carry forwards, withholding tax relief on interest expense dividends, reduced royalties, royalty holidays, import duty relief, and stabilization of fiscal terms.²⁴

There is also considerable heterogeneity in the provision of tax incentives, some being better suited to mining activities than others. Cost-based incentives (e.g. investment allowances, investment tax credits, accelerated depreciation) or tax incentives reducing the overall cost of investment in a project, are easier to monitor and more efficient than profit-based incentives (e.g. income tax holidays, royalty holidays) which are based on some measure of taxable income or profits. Some mining tax incentives are provided in the general tax codes while others are provided in specific contracts (such as royalty-based incentives). Furthermore, tax stabilization and corporate income tax incentives are very palpable across countries.²⁵

²³ AfDB: The Impact of International Tax Reforms on Natural Resource Revenue Mobilisation in Africa; 2023.

²⁴ Ibid.

²⁵ Ibid.

Tax Policy Recommendations

- Policies to tax MNEs at the optimal 18 percent, or 20 percent ETR; and
- Using financial modelling to design appropriate fiscal regimes and estimate costs of tax incentives.

Tax Administration Recommendations

- Invest resources in building the capacity of tax administrations (audit risk analysis, mineral pricing);
- Building tax capacity in mineral and transfer pricing, as well as increased use of governments' audit rights is critical;
- Improved fiscal management, governance and transparency; and
- Automatic Exchange of Information.

3.5 Comparative Assessment of Case Studies Featured

A. The Case for Efficient and Equitable Revenue Mobilisation

A growing body of evidence suggests social and infrastructure spending are critical for promoting resilient growth and inclusion—two mutually reinforcing objectives. Resilient growth supports social development and mobility, while economic inclusion is necessary to sustaining growth and political stability. Resilient growth will also require future spending to be covered without building debt vulnerabilities. Increasing public resources through domestic revenue mobilisation would create space to invest in resilient and inclusive growth in a sustainable manner.

Improving the design of taxes can help balance the efficiency-equity trade-off. For example, measures to broaden the base for consumption taxes are found to be more supportive of growth than raising consumption tax rates. Similarly, income taxes can be designed to minimize the distortions to growth.

It is important to emphasize here that in all tax reform efforts, the equity-efficiency trade-off can only be assessed when evaluating the impact of net taxes: not only the impact of taxes on growth and incentives but also the benefit from financing growth-friendly and equity-enhancing spending.

B. Identifying Sources of Additional Revenue

Tax revenue shortfalls may reflect policy design, tax compliance challenges, or both as indicated in Figures 5 and 6 above showing comparable DRM among SSA countries. *Tax revenues in the IDA recipient SSA countries can be increased while supporting resilient and inclusive growth.*

Potential source of revenue growth in IDA SSA Countries:

- Improving the progressivity of tax systems;
- reducing exemptions;
- Addressing the weaknesses in tax compliance *by reducing tax complexity and strengthening administrative capacity through organisational reforms, enhanced international cooperation on tax issues, and reforms to reduce corruption risks and bolstering institutions;* and
- Effectively addressing both structural features of the country's economy such as informality and challenges in revenue administration.

C. Taxation of the Resource-Intensive Sector

In line with Tables 3 and 4, and 5 and 6 above, a total of SSA countries and IDA recipients that are categorized as resource-intensive are twenty (20). Fourteen (14) of these—ten of which are LICs and four (4) are LMICs are either, oil exporting countries are non-oil exporters, and six (6) countries are oil exporters. With respect to the tax/GDP yield (below and above 15%), the following is the summary of the country categories:

Table 7: Resource-Intensive Countries in SSA / IDA Recipients		
Tax/GDP Yields	Country categories	Number of Countries
Below 15%	Oil Exporters	4 LMICs—Angola, Chad, Cameroon, Nigeria
	Non-Oil Exporters	2 LMICs—Benin, Tanzania
		8 LICs—C.A.R., D.R.C., Eritrea, Guinea, Guinea-Bissau, Liberia, Niger, Sierra Leone

Above 15%	Oil Exporters	1 LMICs—Congo
	Non-Oil Exporters	2 LMICs—Zambia, Zimbabwe
		2 LICs—Burkina Faso, Mali.

The mining sector plays an important role in many SSA countries, but its overall contribution to revenue mobilisation could be enhanced. Tanzania is among the fifteen SSA economies that are considered “**resource-intensive**” (excluding oil), with mining making a significant contribution to countries’ national output, exports, and foreign direct investment (FDI) inflows. But overall revenue from mining in most resource-intensive economies in SSA remains relatively limited.

The capital-intensive nature of the resource-intensive sector—in particular the mining sector—and the long lead times between exploration and production mean that significant costs incurred prior to commencement of production may be ignored in the event the tax authorities prioritize short-term revenue measures, and become statutorily barred from challenge, leading to

substantial revenue losses. Moreover, the administration of the sector is often a shared responsibility between multiple regulatory agencies creating challenges of incomplete data sets for risk assessment purposes (each agency collects and maintains data relevant to their mandate), and duplication of functions, leading to confusion and inefficiency.

To develop capacity, the tax authorities must accelerate the development of sector expertise and implement robust compliance risk management capabilities to enable effective risk identification and mitigation from the onset of resource-intensive activities to protect revenue mobilisation. The best practice is to establish and build resource-intensive expertise within an integrated resource-intensive unit typically within the Large Taxpayers Office to perform non-routine functions such as audit and targeted client assistance.

Fiscal and cost audits are the main tools for budget revenue. A fiscal audit checks that the tax declaration complies with all pertinent laws and contractual requirements. The cost audit is a prerequisite for the fiscal audit: overstating costs—deliberately or accidentally—means understating profits, and thus tax losses. The higher the marginal tax rates—and for excess-profits taxes, they can be well over 50 percent—the greater the temptation for companies to overstate costs. Abusive transfer pricing is an insidious way of doing so.²⁶

Audit rights are described in national legislation or contracts (or both). Usually, a government can ask for any information it deems pertinent. Companies must keep all records on-site, but only for a limited period. After that period, an audit is much more costly and cumbersome. Eventually, the audit rights expire; therefore, auditing of resource projects should start as

²⁶ Charlotte J. Lundgren, Alun H. Thomas, and Robert C. York; Boom, Bust, or Prosperity? Managing Sub-Saharan Africa's Natural Resource Wealth. IMF 2023.

early as during the exploration and development phases. During these phases, the greatest costs are incurred, to be deducted from revenue many years later, when it may be too late to audit. Companies have rights too: once the audit exercise has ended, even if it was poorly done, the audit rights will expire.

A hard-nosed audit of a sophisticated, well-resourced, internationally operating company poses great challenges to developing country governments. One challenge is human resources. The skills and experience to match those of company specialists are hard to develop and retain. Arguably, talented national staff would be better deployed to improving spending, where they have a comparative advantage, than to collecting resource revenue according to international rules. Outsourcing to specialized firms with solid international reputations is the logical solution.²⁷

It may appear expensive but given the revenue to be gained it has the potential to be highly cost effective. The

²⁷ Ibid.

staff of the tax authorities should be trained to organise the outsourcing, and they should be capable of taking up with the resource companies any opinions of the auditors on underpayments or other contentious issues. Auditors should comply with the International Standards on Auditing (ISA).²⁸

Transparency and the involvement of parliament, civil society, and other stakeholders is therefore crucial. Governments could regularly publish an exhaustive accounting of how they used their natural resource auditing rights, and what results they achieved.

D. Compliance Challenges—Administrative and Structural Shortcomings

International cooperation can also affect administrative capacity. Internationalization of global value chains and financial services has created new opportunities for tax evasion and avoidance by large firms and high-net-worth individuals through practices such as profit shifting and concealment of assets and revenue.

²⁸ Ibid.

Meanwhile, the rapid digitalization of the global economy has also generated challenges for revenue administrations.

Beyond administrative capacity, structural bottlenecks, such as large informal sectors, may hinder tax compliance. Large informal sectors often result in a disproportionate tax burden on the formal sector. Furthermore, underfunded social and public services resulting from low contributions by the informal sector could undermine their quality and limit their size, reducing the benefits of compliance and creating an informality trap.

Perceived weaknesses in the control of corruption also create challenges for tax compliance. Given the nature of their role in collecting funds from the private sector, tax authorities are exposed to risks of corruption and collusion. More broadly, weaknesses in control of corruption create opportunities for taxpayers to evade their obligations or obtain undue advantages and for corrupt officials to extract rents, whether during the elaboration of the tax legislation, at all levels of the taxation process or in the resolution of disputes between

governments and tax administrations. To address corruption risks at the tax authorities' level, the Governments should enhance the implementation of a range of safeguards, such as, *inter alia*, internal investigation units, universal electronic payment of taxes, but also taxpayers' education on tax payment obligation.

More broadly, the quality of public institutions matters for compliance. Comparative weaknesses in regulatory quality, voice and accountability, government effectiveness, and rule of law could be detrimental to tax revenue mobilisation. Stronger governance is indeed correlated with better tax performance as sound legal institutions and adequate dispute resolution mechanisms enhance fairness and tax certainty, protect taxpayers' rights, and support the credibility of enforcement, thereby promoting compliance. Tax compliance is also encouraged by stronger trust in government, perception of reciprocity, and retribution of tax payments through the provision of public services. That is, fiscal contracts between the government and citizens should be vividly verifiable.

E. Leveraging Digital Transformation to Collect Taxes

Revenue administrations across the world are embarking on a new wave of digital transformation. Even though earlier waves in automating core functions of revenue administrations—such as e-filing—go back to the 1990s in some advanced and emerging market economies, the current wave is showing the potential to deeply transform the way low-income countries collect taxes. By improving the way that revenue administration functions are carried out:

Digitalization:

- Reduces the burden on taxpayers by simplifying procedures and enhancing service delivery;
- Allows for more effective compliance measures through data collection and matching;
- Improves governance by reducing arbitrary interactions between taxpayers and tax officials; and
- Leaving an audit trail of transactions.

Successful cases involve revenue administrations that:

Invested in a comprehensive digital transformation, including redesigning core functions and the organisational structure (to modernize and simplify process instead of adopting solutions to automate old ways of doing business);

Worked with taxpayers to “educate” them in the use of the new technologies and had a clear taxpayer-oriented vision in place;

Embraced good medium-term planning and proper sequencing to implement change.

Specifically, digitalization reduces physical contacts between taxpayers and tax collectors, thereby reducing the risk of temptations and negotiations on levels and rates of tax payments. While digitalization helps the Governments and the respective tax authorities secure information, it also provides new avenues for fraud as

well as privacy and cybersecurity risks. Individuals and firms can take advantage of new technology to hide information or evade taxes. The risks of fraud arise when taxpayers intentionally falsify information to reduce tax payments, obtain tax refunds, or hide transactions, or when the staff of the tax authorities, contractors, and other trusted parties carry out fraudulent activity. Data breaches through hacking, leaks, and ransomware expose the tax authorities to privacy and disclosure risks (likelihood of the tax authorities to lose control of tax information and personal data) which can further erode citizens' trust in the tax system and consequently reduce voluntary compliance. In line with good practice, the tax authorities should implement cyber security and data protection measures in their systems, as well as establish governance arrangements that will reduce risks to reputation, privacy, and revenue.

²⁹ The terms “informal sector” and “informal economy” are interchangeably used. According to the country’s National Bureau of Statistics (2021), the informal sector is expressed as the number of

F. Formalisation of the Informal Sector

An informal sector or grey economy²⁹ refers to the segment of the economy that is neither taxed nor managed by the government. According to the International Labor Organisation (ILO) broader definition, the informal sector refers to “*all uncovered economic activities by law or in practice*”. The concept has evolved over the years from self-employment in unregistered micro and small-scale enterprises to wage employment and unsecured jobs. The nature of the informal sector is predominantly dominated by domestic/casual workers, without fixed employers, and the self-employed who are mostly hawkers locally known as “*machingas*”. In a nutshell, the nature of the informal sector entails Micro and Small enterprises which are labor-intensive, self-employed, or unpaid workers with uncertain incomes, and unregistered businesses with no financial records. On the other hand, the three vital

individuals employed in the informal sector to the total number of employed individuals in the formal sector.

stages to formalise an entity include business name registration, business licensing, and payment of taxes which partly involve the licensing process.

In most of the SSA countries, it is estimated that the informal sector's contribution to the GDP is 25 percent which is slightly lower than the agriculture sector's contribution to GDP in most countries (IMF, 2017). The sector is, therefore, an important source of livelihood for most of the country's population. With the increasing unemployment in the formal sector, a large share of unemployed youths will consistently be absorbed in the informal sector. Given its sectoral contribution to the GDP of 25 percent, integrating the informal economy into the formal sector is a pertinent policy consideration.

One of the key constraints for the flourishing of the informal sector is to avoid bureaucratic procedures (cumbersome registrations), and unfriendly legal and policy environments (e.g. multiplicity of taxes). The other interpretation is that informality is largely driven by the limited space provided in securing formal jobs. Generally, the constraints are categorized as Regulatory

and Non-regulatory constraints that include factors such as:

- labour legislation (e.g. employee benefits and rights);
- location-related factors (e.g. processes such as the acquisition of land, site development, obtaining utility connections, environmental laws, etc.); and
- reporting requirements (registration, licensing, taxes and duties, property rights, etc.).

Moreover, the sector is also subjected to political interference. While some of the businesspeople in this sector walk around carrying their merchandise around areas with large gathering of people like bus stations and road junctions, others operate in the proximity of formal businesses. While those in large gatherings tend to close roads for other users, those close to foal businesses have negative effects on formal businesses. Removing them from such locations to more formal locations has been a

challenge as politicians tend to protect them as their voters. This has affected the smooth operation of formal business, hence tax collection.

Table 8: Constraints to formalise the informal sector in SSA

Regulatory	Non-regulatory or operational
<ul style="list-style-type: none"> • Labor laws • Absence of a policy for the informal sector (the current SME development policy does not highlight the way MSMEs can graduate to large-scale enterprises etc.) • Reporting: registration, licensing, and taxation • Land acquisition and availability of utilities. 	<ul style="list-style-type: none"> • Access to finances • Infrastructure • Supply-related: access to inputs, capacity building, markets, etc.

Therefore, the interventions should consider ways of minimizing the cost of doing business in the informal sector and formulate policies that are specifically tailored to address regulatory and non-regulatory constraints and address the needs and risks of the informal sector. In this context, the governments’ focus should be to change the sector by promoting its capacity to grow and create productive employment coupled with simplified legal requirements and business procedures to motivate SMEs to formalise their businesses.

4.0 IDA-20 INITIATIVES AND COMMITMENTS MADE FOR DRM

4.1 Introduction

DRM has been a focus of IDA action since the adoption of Country Policy and Institutional Assessment (CPIA) ratings in 1980. DRM is one of the 16 CPIA criteria (see Box 1, below), under the public sector management and institutions cluster, that determine the allocation of IDA resources and is used to evaluate the performance of IDA action.

Box 1: CPIA Criteria				
Cluster	Economic Management	Structural Policies	Policies for Social Inclusion/Equity	Public Sector Management and Institutions
Indicators	1. Macroeconomic Management 2. Fiscal Policy 3. Debt Policy	4. Trade 5. Financial Sector 6. Business Regulatory Environment	7. Gender Equality 8. Equity of Public Resource Use 9. Building Human Resources 10. Social Protection and Labor 11. Policies and Institutions for Environmental Sustainability	12. Property Rights and Rule-based Governance 13. Quality of Budgetary and Financial Management 14. Efficiency of Revenue Mobilisation 15. Quality of Public Administration 16. Transparency, Accountability, and Corruption in the Public Sector

4.2 DRM and IDA Initiatives and Commitments

It is estimated that some 32 IDA countries received support for various aspects of DRM between 2005 and 2019 (IDA 17 and 18) through one or in combination of development policy operations (DPO), investment projects or the IFC's advisory services on business taxation (World Bank, 2023c). IDA reforms of this era have endured small incremental success as opposed to overall commitment targets of lifting tax yields above the 15 percent threshold. Part of the reason behind the limited success of DRM reforms has been the low prioritisation of spending on DRM relative to both commitments and disbursement. For instance, of the US \$65.5 billion committed during IDA 17 and 18, only US\$1.6bil (equivalent to 2.4% of all commitments) went to DRM (Table 9, below).

Table 9: Source and Volume of World Bank Support to Domestic Revenue Mobilisation

Instrument	Commitments Approved During FY12-15		Commitments Approved During FY16-19	
	Number	US\$ Millions	Number	US\$ Millions
Investment projects focused on DRM	20	1020	31	1488
Development policy operations with at least one prior action focused on DRM	65	n/a	84	n/a
Trust-funded projects	8	128	9	68.5
Advisory services and analytics	425	47	322	88

Source: World Bank (2023c)

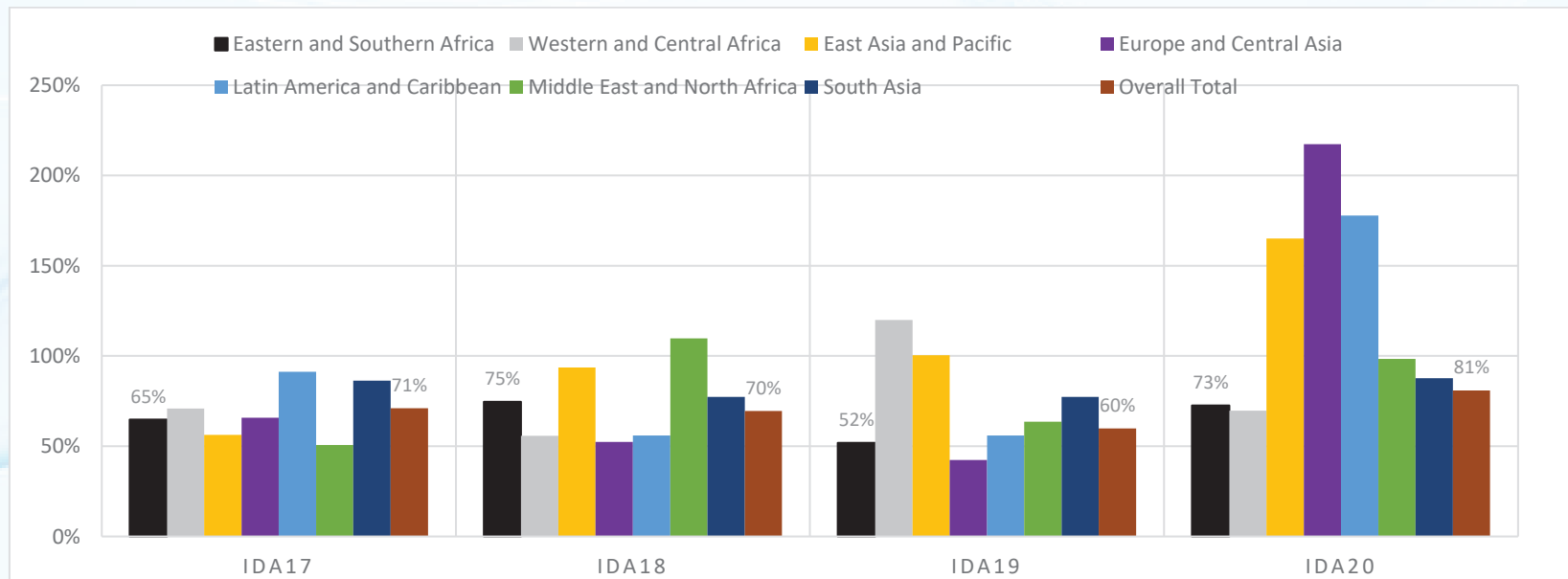
Combined with an average disbursement to commitment ratio of 70 percent (Figure 12, below) during IDA 17 and 18, the actual sums spent on DRM are likely to have been considerably lower. As a result, concerted IDA action and indeed concrete outcomes have at best been mixed and at worst sparsely existent. Limited prioritisation of DRM funding has partly mirrored the initial coupling of DRM with other broader reform areas that have tended to obscure the focus, and specificity of action over the years. For example, initial support of DRM during IDA 15 when it featured as part of the crosscutting pillar focusing on Governance³⁰ was not reinforced by concrete actions in IDA16 which in the aftermath of global food and fuel price shocks, focused on crisis response, gender, climate change, and fragile and conflict at the expense of long-term structural reforms. This contributed to setting back the operationalisation of targeted DRM initiatives, indirectly

contributing to a deterioration of debt risk ratings in 20 percent of IDA recipients between 2014 and 2017 because of widening fiscal deficits driven by expanded infrastructure spending, falling revenues from natural resource exports and currency depreciations, and—in some cases—increased recourse to central bank advances (World Bank, 2018). Further, while IDA 17 saw exclusive support for DRM in small island and fragile and conflict-affected states (FCS) as well as the expansion of DRM support to resource-rich countries under the auspices of the Extractive Industries Transparency Initiative (EITI), the continued bundling of ideally concrete and specific DRM reforms with other broader sub-sector initiatives compounded the difficulties of aligning DRM action with operational targets and objectives leading to an array of ill-targeted and under-focused DRM action.

³⁰ IDA (2008). Report from the Executive Directors of the International Development Association To the Board of Governors Additions to IDA Resources: Fifteenth Replenishment IDA: The Platform for Achieving

Results at the Country Level. See [Microsoft Word - Final IDA15 report.doc \(worldbank.org\)](#)

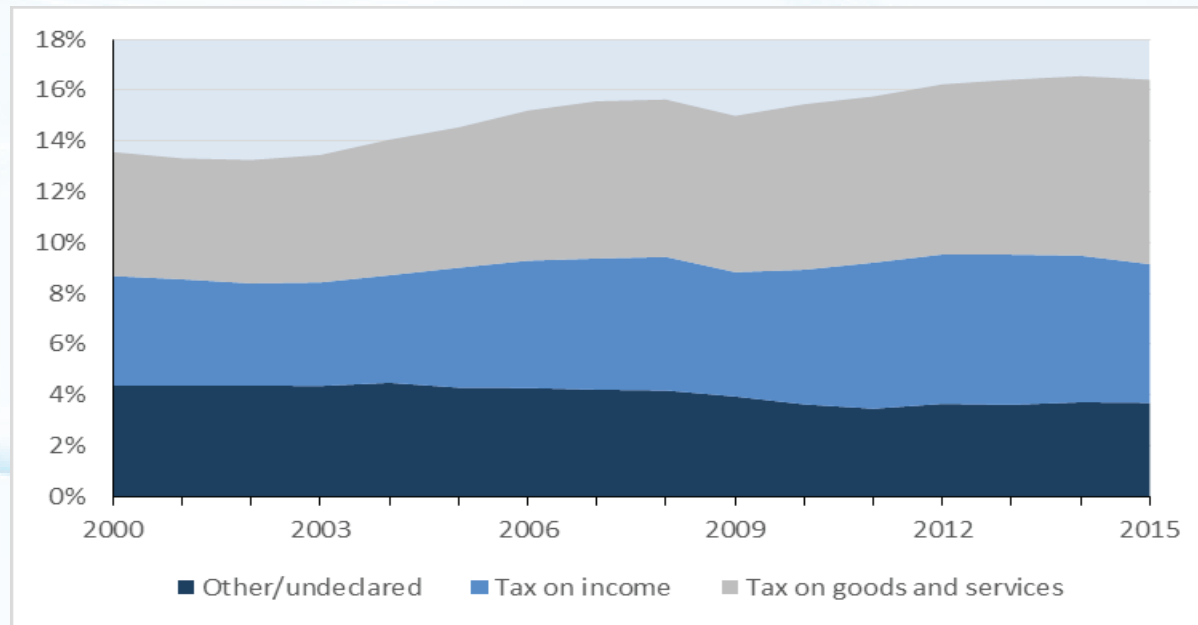
Figure 12: FY15-FY23 IDA Disbursements to Commitments Ratio



Source: Authors' based on World Bank (2024)

The concretisation of DRM action through specific performance targets failed to materialise until IDA 18 in 2017. By 2016, the global recovery from the food and fuel price shocks of the previous decade was nearing completion. However, the recovery also saw historical declines in commodity prices that affected a significant proportion of IDA countries further heightening their balance of payments challenges. Tax receipts in 36% of the 76 IDA-eligible countries and 70% of Fragile and Conflict-affected states had been and stayed below the computed threshold of 15% of GDP necessary for the implementation of basic state functions (Figure 13, below).

Figure 13: Taxation in IDA Countries, Source: IMF World Economic Outlook, April 2016



In response, IDA 18 attempted to broaden the focus on DRM beyond extractive industries by focusing on the pro-poor DRM principles of quality, fairness, and equity of domestic tax. IDA18 also marked the first adoption of DRM-specific targets of at least 15 percent of GDP – considered a threshold for a state to function effectively – while minimizing market distortions and ensuring income growth for the bottom 40 percent.

IDA18 extended support on DRM to 24 countries, a majority of which were in Sub-Saharan Africa. Cognisant of its predecessors' limited success in DRM, IDA 18 pushed for improved global partnerships to address DRM and successfully saw the launch of the Global Tax Program in 2018 (Box 2, below).

Box 2: The Global Tax Program

Launched in June 2018, the Global Tax Program (GTP) is a dedicated initiative that finances technical assistance on revenue policy and administration in low and lower-middle-income countries. The GTP supports advisory services and technical assistance to improve and strengthen tax institutions and revenue mobilisation. The launch of the GTP reflected feedback from IDA recipients for more substantial support for DRM. GTP allocates around 81 percent of its resources to support the expansion of and improvement in the quality of DRM country-level work, with the remaining resources supporting the development of diagnostic tax tools, assessment frameworks, and research. As of April 2024, the GTP portfolio comprises of 78 project activities in over 85 countries, two-thirds of which are IDA-eligible. The GTP is organised around four pillars:

Global tax activities and global public goods

- Development and application of tax diagnostic tools, such as tax policy assessment frameworks and Tax DIAMOND, which identify weaknesses and recommendations for improvements.

Country-level work pillar

- Focuses on improving revenue collection through medium-term revenue strategies based on prior tax diagnostic work, mainly using the Tax Administration Diagnostic Assessment Tool, tax policy assessment frameworks, or Tax DIAMOND.

Actionable research, data, knowledge, and learning

- DRM-focused research and data

Implementation and Supervision

- Program administration and oversight

In addition to the above pillars, the GTP launched a temporal Fiscal Policy Pillar (Crisis Support) in 2021 to adapt and mitigate the social and economic impact of the COVID-19 pandemic. Further, the GTP's global and country-level pillars also provide support for:

- Green-based tax reforms aimed at harnessing existing environment and climate change tools for broad and inclusive tax bases.
- Gender equality tax reforms toward the achievement of gender equality goals; and
- Health-based tax reforms aimed at addressing the effects of tobacco, alcohol, and sugar-sweetened beverages (SSBs).

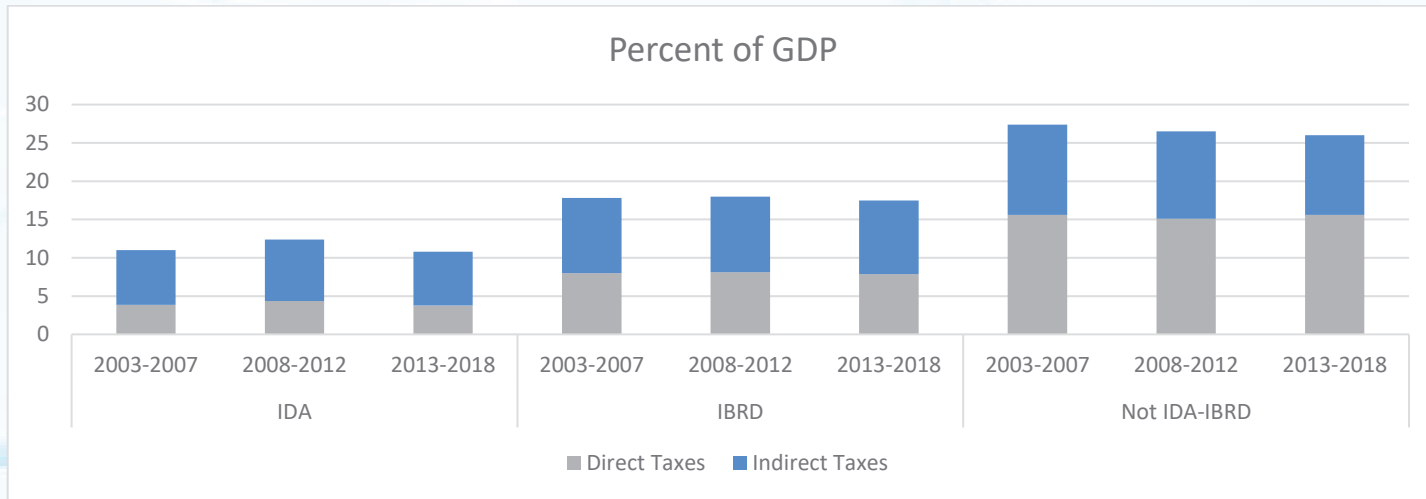
Source: World Bank (2024)

The GTP is credited with galvanising IDA's focus on DRM, and while many IDA-18 recipients were able to increase their tax yields during the three-year cycle, none were able to surpass the 15% of GDP threshold. Nonetheless, IDA 18's targeted approach to DRM succeeded in demonstrating the utility of a coordinated push for improved policy outcomes. This sowed the seeds for more ambitious targeting and strengthened coordination in IDA 19 and 20, both of which have sought to reinforce DRM targets by retaining the same operational target and expanding the breadth operations and technical assistance to recipient countries. IDA 19 (2019-2021) extended DRM support to 36 countries beyond its baseline target of 32 (World Bank, 2023). Yet, despite the numerical reach, reform performance ultimately fell short of the planned target ostensibly because of the global outbreak of Covid-19, and subsequent fiscal responses to the crisis. The World Bank estimates revenue collection to recover in IDA/Blend countries that previously had tax-to-GDP ratios persistently below 15%, with support from IDA. It is estimated that these countries will have improved their unweighted tax-to-GDP ratios by approximately 0.33 of a percentage point over the IDA19 cycle (2019–2022). This average increase, however, falls short of the target of one percentage point that was planned for a three-year cycle.

A combination of lessons from reforms discontinuity and optimistic forecasting of long-term success of IDA 19's DRM reforms saw a consolidation of DRM reforms in IDA 20. The latter initially aimed to achieve a tax-GDP ratio of at least 15 percent in the medium term in some 15 IDA countries through support for equitable (fair and progressive) revenue policies. A midterm appraisal of IDA 20 in November 2023, found the coverage of DRM support to have extended to 21 countries (World Bank, 2023), with recipients who had been receiving support since IDA 18 finally recording nominal improvements in their DRM. IDA 20 continues the institutionalization of policy commitments aimed at supporting DRM and broader Governance and Institutions.

IDA 20 builds on its previous two predecessors to streamline the operational target for DRM, by retaining the targeted improvements of the unweighted tax-to-GDP ratios of 1 percentage point over the three-year IDA cycle. IDA 20 also extends support for two complementary reforms aimed at enabling digital government services and combating illicit financial flows (IFF), both of which have the potential to spur the effectiveness and accountability of DRM initiatives as well as mitigate against practices that erode the tax base through among others, tax evasion. Continued support for DRM under IDA 20 signals a realization for sustained efforts to address historical and institutional deficiencies that have given rise to persistently low tax yields in some IDA countries (see Figure 14, below):

Figure 14: Direct and Indirect Tax Revenue



Source: World Bank (2022)

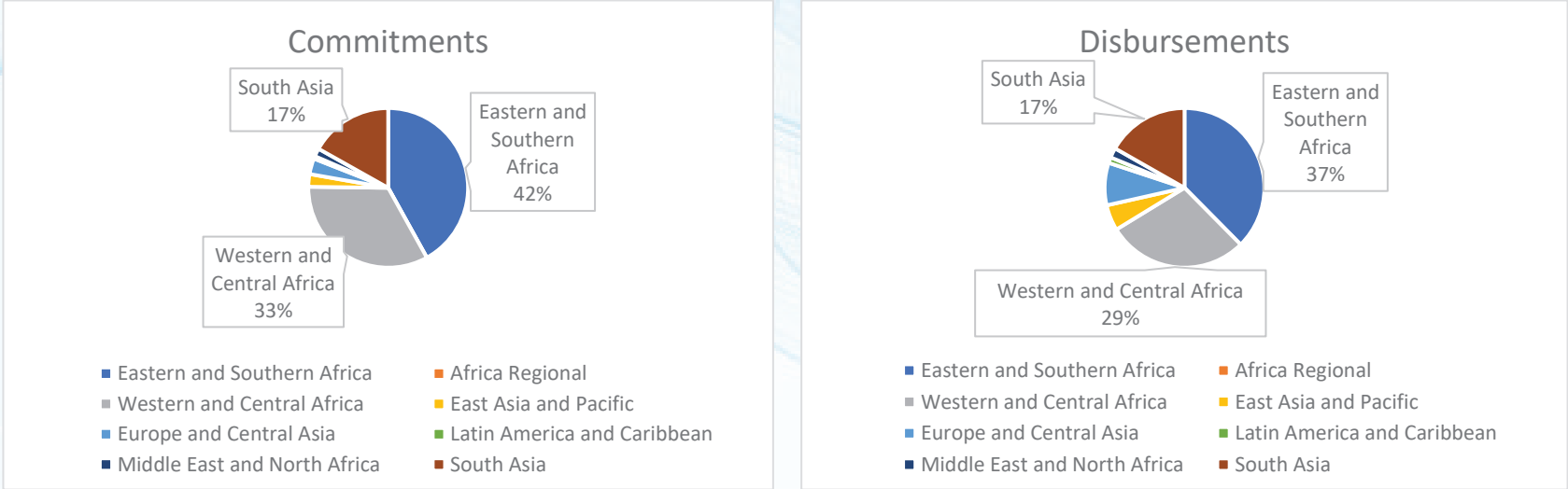
Much of the World Bank’s recent support for DRM has been through development policy operations (DPOs), in which prior actions frequently supported changes in tax rates (value-added taxes, corporate income tax, and personal income tax) or reductions in tax expenditures. Further, additional focus on DRM, especially that of the analytical kind was facilitated through GTP enabled a significant increase in World Bank engagement in DRM. GTP funding allowed the World Bank to increase its analytical support for DRM. However, this has come at an internal price for the World Bank, increasing the pressure on already limited staffing resources within the World Bank and contributing to considerable turnover in staff and management working on tax issues. A recent evaluation found that the share of DRM projects rated

satisfactory was 41 percent, and 35 percent of projects were rated moderately satisfactory. Among IDA countries, the biggest improvement in DRM focused on the performance of tax administration projects (World Bank, 2023c).

4.3 Attainment of IDA-20 Commitments in Sub-Saharan Africa

Sub-Saharan Africa collectively accounts for 77 percent of the US\$34.2 billion committed by IDA 20 in 2023. The region was also the recipient of two-thirds of all total IDA 20 disbursements worth US\$27.7 billion during the same period (Figure 15, below). Further, the region accounts for 26 of the 36 countries' recipients of DRM support under IDA 20. Almost all SSA IDA recipients with the exception of Kenya have tax yields below the 15 percent threshold.

Figure 15: IDA 20 commitments and disbursements



Source: World Bank (2024)

Notwithstanding its overall share of IDA 20 commitments, SSA has historically been the recipient of considerably less IDA disbursements relative to commitments at 68 and 53 percent during IDA 17 and 19 respectively (Table 10, below). Current IDA 20 disbursement to SSA stands at 71 percent of commitments. Notwithstanding the primacy of DRM concerns in SSA, IDA 20's DRM allocation remains at less than 3 percent of aggregate commitments.

Table 10: Disbursement – Commitment Ratio in SSA, IDA17 – 20

Region/Country	Disbursement-Commitment Ratio			
	IDA 17	IDA18	IDA19	IDA20
Eastern and Southern Africa				
Angola				
Burundi	48%		49%	106%
Comoros		243%	47%	35%
Congo, Democratic Republic of	67%	261%	42%	83%
Eritrea				
Ethiopia	76%	332%	57%	110%
Kenya	60%	345%	69%	58%
Lesotho		263%	71%	
Madagascar	77%	282%	32%	40%
Malawi	148%	259%	54%	79%
Mozambique	132%	263%	42%	58%
Rwanda	90%	284%	65%	103%
Sao Tome and Principe		273%	62%	703%
Somalia		255%	29%	60%
South Sudan	175%	316%	23%	54%
Sudan				
Tanzania	53%	456%	46%	71%
Uganda	62%	326%	62%	102%
Zambia	50%	282%	91%	64%
Zimbabwe				
AFE Regional			815%	47%
Total Eastern and Southern Africa	65%	288%	52%	73%

Western and Central Africa				
Benin	137%	261%	46%	74%
Burkina Faso	102%	275%	45%	127%
Cabo Verde	195%	359%	63%	123%
Cameroon	90%	274%	27%	39%
Central African Republic	99%	301%	59%	40%
Chad	75%	267%	30%	30%
Congo, Republic of	45%	293%	72%	87%
Cote d'Ivoire	97%	265%	60%	52%
Gambia, The	45%	249%	147%	116%
Ghana	85%	255%	49%	62%
Guinea	72%	268%	187%	56%
Guinea-Bissau	41%	343%	118%	65%
Liberia	187%	282%	66%	50%
Mali	124%	285%	74%	44%
Mauritania	108%	305%	96%	100%
Niger	89%	267%	42%	95%
Nigeria	74%	1730%	69%	118%
Senegal	71%	291%	64%	56%
Sierra Leone	58%	267%	88%	62%
Togo		297%	54%	57%
AFW regional			214%	120%
Total Western and Central Africa	74%	273%	54%	70%
Africa Regional	78%			
Total Africa	68%	281%	53%	71%

Source: Authors' Calculations from World Bank (2024)

Collectively, the below frontier allocation and disbursement figures make it unlikely that IDA 20 will meet its DRM targets by 2025. Not only do these figures pose risks to the attainment many of the operational targets but the historically low tax yields, creeping reforms fatigue, a stuttering global economic recovery, and the short implementation cycle of IDA 20 further undermine the likelihood of attaining DRM targets in SSA. IDA 20 needs to renew its focus on sustaining hard-worn reforms to guard against adverse political dynamics that have in the past undermined sustainability and, in some instances, led to their reversals once disbursements have been made. These challenges are inherently more pronounced

in the current context as at least half of SSA IDA recipients face general elections during the replenishment cycle. Research has shown a propensity for reversing prior actions supporting reductions in tax expenditures or tax exemptions during election cycles (Ebeke, 2017).

IDA 20 can support these countries by strengthening the design and funding of both development policy operations (DPO) and advisory services and analytics (ASA), particularly those offered under the Global Tax Program. Strengthening the analytical capacities in countries should help with the modernization and expansion of tax bases. Further, with the growth in the use of data in policy, better analytics could in turn improve revenue governance and help develop diverse coalitions of state and non-state actors that could be mobilised against attempts to subvert and/or reverse ongoing reforms. This would develop the necessary institutional scaffolding comprising of aligned norms and practices key to defending the structural integrity of reforms. The extent to which some DRM reforms have been reversed in IDA countries is indicative of possible tension between countries that fail to make concrete and sustained progress on DRM and the successive provision of budget support to those countries. Specifically, the provision of direct budget financing can reduce how urgently and ambitiously clients approach DRM and the importance they assign to avoiding backsliding.

5.0 CONCLUSIONS AND RECOMMENDATIONS

5.1 Conclusions

a) The Countries' Low Tax-to-GDP-Ratio

This Policy Paper has analysed trends and features of domestic resource mobilisation in Sub-Saharan Africa. The paper has established that many Sub-Saharan African countries are lagging behind their counterparts in Asia and the Pacific, Latin America and the Caribbean, and the OECD. The average tax-to-GDP ratio in SSA is 16.3%, Asia and Pacific is 19.1%, Latin America and the Caribbean is 21.9% and OECD is 33.5%. Only 12 SSA Countries have tax to GDP ratio of above 20%. The paper has further established that there are differences in domestic revenue mobilisation between SSA countries although many of the countries have the same socio-economic characteristics. This trend relationship between countries in domestic resource mobilisation is contributed by a number of factors, some of which are outlined below.

b) Large Informal Sector

It has been noted that while these countries have huge informal sectors contributing significantly to their GDP, their sizes differ between one country and another. The informal sector is hardly taxed because it is too expansive because

players in the sector are not organised and difficult to locate administratively. But also, cumbersome procedures within the revenue authorities that require taxpayers to fill a number of forms make compliance costs high among players of the informal sector as they hardly keep daily transaction records. These challenges are in addition to the sector being subjected to political interferences that affect compliance from formal business as a resulting of both formal and informal businesses working on the same locations. As a result, the countries with larger informal sector have very narrow tax bases, leaving many potential taxpayers out of the country's tax system than those with smaller informal sectors.

c) The Countries' Resource-Rich Status

Most of the SSA countries with tax to GDP of less than 15% are among the resource-intensive countries, with abundant of mineral resources and others with oil and gas. Despite endowment of huge natural resources, the countries have not been able to collect enough taxes from this sector. The lower contribution of this sector to tax revenue is partly due to its nature of investment, in which initial capital is so high that it takes time before investors start to realize profit for tax purposes. This has provided loopholes for investors to provide documents that underestimate potential taxable profit. Coupled with the limited capacity for sector experts within revenue authorities to undertake proper audits, this has significantly reduced the tax contribution from this sector.

d) High Prospects for DRM Going Forward

While many of the SSA Countries are lagging in various aspects of domestic revenue mobilisation, they still have a lot of potentials to increase their DRM. Some of these countries, for example, Tanzania, are among the countries with big economies in the region and their growth rate are high over time. This implies that they have strong bases

that need to have proper mechanisms to enhance their DRM. As discussed earlier, while many of these countries have large economies, a large part is contributed by the informal sector, making it hard to organise, increase its productivity, and tax it. As a region also, SSA has a large population. This also gives the sub-continent a competitive advantage for increased market size provided the population is comprised of a large middle-income category. While the middle-income group stimulates local demand, its contribution to money circulation is high, hence increasing a country's tax base.

e) Valuable Contribution of IDA

In partnership with other MDBs—in particular the IMF and AfDB—and key development partners, the IDA has made valuable contributions to enhance the countries' DRM. Key areas of IDA contribution to IDA recipient countries in SSA's DRM include:

- Continued support for the development of a medium-term revenue mobilisation and a public financial management strategy aimed at improving forecasting and aligning revenues with expenditure; and
- Promotion of voluntary compliance through the adoption of behavioural science approaches to tax administration and research.

While the IDA support has been very useful in DRM, the commitment has suffered two challenges: allocations and disbursements. As a result, the expected outcomes of the DRM support have been far lower than the anticipation. Even the current IDA 20, seems to be below the frontier in terms of allocation and disbursement, making it unlikely to meet its DRM targets by 2025.

5.2 Recommendations

5.2.1 DRM and IDA

- a) **Maximizing Revenue from the countries' natural resources: Full Use of Government Audit Rights**--After adopting a good fiscal regime, a crucial step for authorities to maximize revenue from the country's natural resource base is to fully use its audit rights.
- Contracts and fiscal regimes usually give governments a powerful set of audit rights.
 - A fiscal audit checks that the tax declaration complies with all pertinent laws and contractual requirements.
 - The cost audit is a prerequisite for the fiscal audit: overstating costs—deliberately or accidentally—means understating profits, and thus tax losses.
 - In the advent of skills shortages, the government's tax authority should outsource specialized firms with solid international reputations to carry out the cost and fiscal audits.
 - The revenue authorities' staff should be trained to organise the outsourcing, and they should be capable of taking up with the resource companies any opinions of the auditors on underpayments or other contentious issues.
 - Auditors should comply with the International Standards on Auditing (ISA).

- The Governments could regularly publish an exhaustive accounting of how they used their natural resource auditing rights, and what results they achieved.
- MDBs need to support an expedited development of countries' natural resources revenue collection information systems as per PFMRP. An integrated information management system would enable the leveraging of digital technologies to enhance monitoring, transparency, and accountability and thus aid tax administration and compliance management.
- Further, MDBs, through the World Bank Policy Support function as well as the IMF's Article IV consultations could encourage countries to sign and ratify the Inclusive Framework on Base Erosion and Profit Shifting (IFBEPS) which was designed in part to close loopholes in international tax treaties that have inadvertently facilitated profit shifting by multinationals and other forms of tax avoidance. Research has shown that large, medium, and small firms all engage in tax avoidance in many SSA countries. The adoption of IFBEPS could facilitate regular systematic review of countries' international tax policy in the context of the cross-country experience could inform measures to reduce tax avoidance and, in the process, improve overall equity of DRM efforts.

b) With regard to the need for improving both the efficiency and equity of the countries' tax system, our analysis points to the following four priorities:

- *Improving tax policy design to broaden the tax base and increase progressivity and redistributive capacity.*

- *Strengthening revenue administration to improve compliance.* Modernizing revenue administrations and enhancing their efficiency would improve enforcement and compliance. Key requirements include restructuring revenue administrations on a functional basis and granting them greater autonomy, developing taxpayer services to reduce the cost of compliance, reinforcing control procedures, and leveraging digital technologies, and expanding electronic taxpayer services to all main taxes. Enhanced international cooperation can also facilitate information exchange across tax jurisdictions, improving transparency and the integrity and fairness of the tax system.
- *Implementing structural reforms to incentivize tax compliance, formalisation, and economic diversification.* Promoting financial inclusion and discouraging the use of cash could help improve access to financial services and lower the cost of digital payments. These measures can boost tax compliance and incentivize formalisation and economic diversification—two important determinants of revenue performance in the region. Reforms to fight corruption, improve governance, and enhance transparency and communication are also crucial for instilling confidence in the fairness of the tax system.

Sustained efforts are needed for successful reforms to mobilise domestic revenues in SSA. Specifically, and in line with the current IDA 20 recommendations, the following actions and policies should be implemented as per the proposed timelines:

Short-term:

- Re-evaluate excise taxes on tobacco to increase revenue and support public health objectives.

Short to Medium-term:

- Consider adjusting the VAT, CIT, and excise tax rates to boost their productivity and mobilise additional revenue;
- Strengthen taxation on households at the top of the income distribution to improve the tax system's equity and mobilise additional revenue;
- On the policy level, use the CEQ methodology to review proposed changes in taxation and public expenditure policies, including subsidies, to assess their potential impact on household income, poverty, and inequality.

Medium-term:

- Strengthen the tax administration's auditing capacity to expand collection efficiently and equitably;
- Broaden the tax net by realigning registration thresholds;
- On the policy front, broaden the VAT base and use a portion of the revenue generated to increase funding for social services; and
- Consider increasing conditional cash transfers to compensate poor households for the negative impact of an expanded VAT base or other fiscal policy changes.

c) Policy action is needed in three key areas:

- First, strengthen the tax policy and institutional framework to broaden the tax base and increase progressivity and redistributive capacity;

- Second, strengthen the adoption, integration, harmonization, and institutionalisation of financial management information systems; and
- Third, structural reforms should improve incentives for tax compliance, formalisation, and economic diversification.

d) IDA 21—Targeted Recommendations

Based on experiences from previous IDA support, the following targeted recommendations are made to inform IDA 21:

- *Elevate DRM to a standalone thematic policy commitment.* The incorporation of DRM as a cross-cutting theme in the previous IDA supports has led to limited support for concrete action. As a result, DRM efforts have been small in size and short-term in design. All IDA recipient countries need comprehensive long-term assistance on DRM that could be made feasible by dedicated funding windows based on thematic prioritisation.
- *Integrate DRM support to complement expenditure management for a balanced approach to public finances.* While most IDA recipient countries have seen improvements in DRM, weakening budget and expenditure management have led to increased budget deficits further constraining the ability to design effective long-term revenue policies.

e) MDBs Reforms

In the context of the ongoing reforms, two targeted recommendations are henceforth made for MDBs to consider:

Representation at the MBD Executive Boards

- Enhancing representation of the SSA countries at the MDB Executive Boards—IMF, World Bank and the African Development Bank---well beyond the two Executive Board Members for the entire SSA.

The increase in the number of representations at the MDBs will (a) enable these countries and those of SSA to effectively and timely align their policy frameworks—including the DRM policy frameworks—with those developed by the MDBs; and (b) appropriately mobilise resources from the MDBs that enhances the DRM targets in particular the grants and technical assistance resources. Availability of the high concessional resources from the MDBs would also be beneficial for these countries.

Policy Consultation Framework

- The MDBs should all enhance the regular policy consultation framework in the context of the IMF-based Policy Support Instrument (PSI) or the current Policy Coordination Instrument (PCI) rather than through the current conditionality funding.

Enhanced and regular policy consultation framework by the MDBs will strongly benefit these countries in the key macroeconomic and policy areas that will progressively and continuously support the enhancement of their respective DRM.

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