Financing for Sustainable Development Report 2020

Inter-agency Task Force on Financing for Development

United Nations

This report is a joint product of the members of the Inter-agency Task Force on Financing for Development. The Financing for Sustainable Development Office of the United Nations Department of Economic and Social Affairs serves as the coordinator and substantive editor of the Financing for Sustainable Development report.

The online annex of the Task Force (http://developmentfinance.un.org) comprehensively monitors progress in implementation of the Financing for Development outcomes, including the Addis Ababa Action Agenda and relevant means of implementation targets of the Sustainable Development Goals. It provides the complete evidence base for the Task Force's annual report on progress in the seven action areas of the Addis Agenda (chapters III.A–III.G). The report is by necessity more concise and selective and should thus be read in conjunction with the online annex.

Inquiries about the Task Force or its report and online annex can be sent to:

Financing for Sustainable Development Office
Department of Economic and Social Affairs
2 United Nations Plaza (DC2- 2170)
New York, N.Y. 10017
United States of America
+1-212-963-4598

developmentfinance@un.org

http://developmentfinance.un.org

Federal Ministry for Economic Cooperation and Development

The production of this report and the online annex of the Inter-agency Task Force are generously supported by the Federal Ministry for Economic Cooperation and Development of Germany.

How to cite this report:

United Nations, Inter-agency Task Force on Financing for Development, *Financing for Sustainable Development Report 2020*. (New York: United Nations, 2020), available from: https://developmentfinance.un.org/fsdr2020.

United Nations publication
Sales No.E.20.I.4
ISBN 978-92-1-101422-8

DOMESTIC PUBLIC RESOURCES

Chapter III.A

Domestic public resources

1. Key messages and recommendations

Domestic public resources have a unique role to play in financing for sustainable development. The link between revenue collection and effective expenditures for quality public goods and services forms the basis of the social contract between citizens and the state. Member States of the United Nations also recognized that significant additional domestic public resources are necessary to realize sustainable development and committed to enhancing revenue mobilization.

Since 2015, there have been improvements in tax policies and international cooperation in some significant areas, yet five years into the implementation of the agenda, positive reforms have not been fully integrated and aligned across sectors and institutions—nationally or internationally. The slow and steady progress in domestic public resource mobilization is insufficient to match the scale and ambition of the 2030 Agenda for Sustainable Development. Only about 40 per cent of developing countries clearly increased tax-to-gross domestic product (GDP) ratios between 2015 and 2018. Political will for reform and assistance for capacity-building are inadequate, while sustainable development is not yet universally prioritized in expenditure allocation and budget processes.

Many more Members States should be preparing multi-year country plans for tax policy and administration reform, to increase revenue mobilization and support public investment to achieve sustainable development. For medium-term revenue strategies to be effective, they should be country-owned, reflect development priorities, be prepared by the whole of government, and have the full backing of national political leaders. This reinforces the social contract and accountability to citizens, who can demand better service delivery alongside more effective governance.

Fiscal reform plans should also take account of existing capacities and impediments and should focus on the binding constraints to greater revenue raising, which can help countries prioritize actions to raise revenues. Fiscal systems also need sufficient resilience and flexibility so they can face unexpected circumstances, such as the rapid spread of COVID-19 in the first quarter of 2020. In such situations, revenues are likely to decline as economic activity slows, while expenditures may increase, especially health-sector spending.

Governments should invest in technology to support all parts of the fiscal system, such as tax administration, enforcement of laws against financial crimes, and budget execution. Such investment should be aligned with medium-term revenue and expenditure plans, and can be supported by international partners. There is enormous scope to use technology to strengthen public financial management and reap returns in greater revenue mobilization and more efficient spending. This includes relatively old technologies, such as digital databases for expenditure and tax administration, as well as new technologies, such as artificial intelligence and distributed ledgers.

The continued digitalization of the economy is also making tax norms agreed almost a century ago obsolete. ***Any new international tax norms being developed to address challenges from technology must be well-tailored for developing countries—including the least developed and smaller countries—and inclusive of developing-country voices in their formation and agreement. Countries need to be afforded sufficient additional time to determine the advisability of reforms before they are agreed and provided with technical assistance to accurately assess the medium- and long-term impact of proposed changes on their economies.***

While significant progress has been made in international tax cooperation, the interests and voice of developing economies require greater priority and attention. ***The global community could better ensure effective inclusion in tax norm-setting processes; adaptation of tax norms and practices to the realities and needs of developing countries; and greater investment in capacity-building from development partners.***

Countries without access to information, and without sufficient domestic capacity to enforce increasingly complex international tax norms, will be unable to boost revenue mobilization related to cross-border activity.

Policy actions on illicit financial flows (IFFs) lag behind the political rhetoric. To be most effective, efforts for tackling IFFs should focus on specific components. International cooperation is needed to tackle all aspects of IFFs. Especially important actions include spontaneous information-sharing and mutual legal assistance. Internationally, tax-related IFFs are being tackled with some of the international tax cooperation tools. Effective national actions for combatting tax-related, corruption and other kinds of IFFs in all countries include: more capacity to prevent and investigate suspicious transactions; more effective cross-institutional coordination in national enforcement; and more assiduous implementation of national commitments made under the United Nations Convention Against Corruption.

New technologies, such as crypto-assets, are facilitating IFFs, underscoring the importance of concerted enforcement efforts and constant vigilance of the financial system. ***New technology, such as artificial intelligence, can enable better identification of suspicious activity—for example, by matching tax filing data to other data sets, such as customs declarations, financial account information, or real estate transaction registers.*** However, technology should be only one component of a broader political strategy to tackle illicit finance.

Nationally and internationally, corruption occurs as public and non-state actors respond to the incentives and social and economic constructs that are present. Embedding new expectations and social norms, along with shifting political settlements related to accountability, transparency and integrity will require leadership from the top as well as localized, sector- and context-specific actions. ***Countries also need to step up implementation of prior commitments and cooperation on stolen asset recovery and return. More regular and rigorous statistical information-sharing on legal assistance requested and provided, as well as the results in terms of assets returned, can be useful***.

How revenues are spent is as important as the amount mobilized. Medium-term expenditure frameworks, which complement revenue frameworks, bring together a holistic picture of the fiscal system. ***Expenditure frameworks should be aligned to the SDGs which can be facilitated by being part of integrated national financing frameworks (INFFs).*** Some countries have already started mapping their budgets to the Sustainable Development Goals (SDGs). ***Policymakers should embed gender equality and women's economic empowerment in expenditure and strategic procurement across all sectors. Spending should be informed by national disaster risk reduction financing strategies. Similarly, environmental sustainability needs to be made a core element of domestic public investment policies if we are to meet climate goals.*** Multilateral agencies provide tools for these and other areas, including capacity-building.

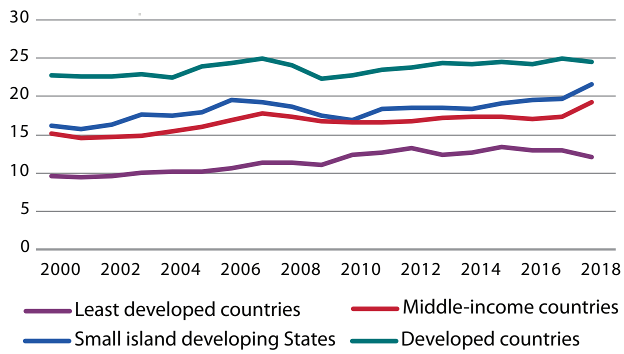
This chapter begins by reviewing trends in taxation, tax administration and tax avoidance and evasion. It then provides an update on international tax cooperation, including an analysis of proposed changes to tax norms related to the digitalization of the economy. The next section provides an examination of IFFs, before the final section explores ways to align expenditure and procurement with sustainable development.

2. Domestic resource mobilization

2.1 Taxation trends and medium-term revenue strategies

In 2018, available data shows that 53 developing countries increased tax revenues,[1] while 46 countries registered a decline. Middle-income countries and small island developing States (SIDS) saw increases in tax revenue (measured as the median tax revenue-to-GDP ratio) to 19.2 per cent and 21.6 per cent, respectively, while least developed countries (LDCs) saw a slight decrease to 12.1 per cent (figure III.A.1).[2] The median tax revenue-to-GDP ratio of developed countries decreased slightly, largely due to personal and corporate tax reform in the United States of America that prompted a drop in tax revenue from 26.8 per cent of GDP in 2017 to 24.3 per cent in 2018.[3] Tax revenues have reached a plateau in most developed countries, ending the trend of annual increases seen since the 2008 financial crisis.

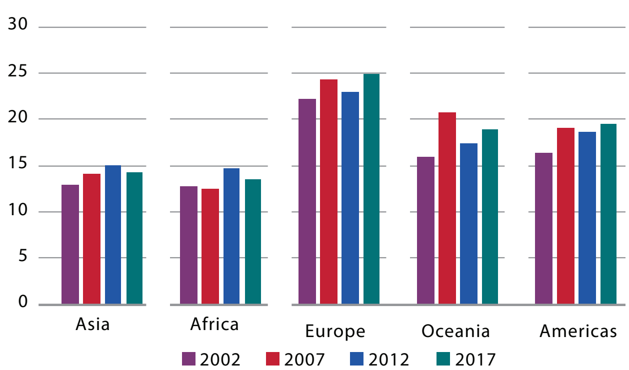
Figure III.A.1
Median tax revenue by country group, 2000–2018
(Percentage of GDP)



Source: IMF.

Tax revenues vary widely by region. Many regions saw little annual change in median tax revenue as a percent of GDP in 2018. Between 2012 and 2017, tax revenues fell in Asia and Africa, regions with the lowest median tax revenue figures as a percent of GDP (figure III.A.2). This is in contrast to Europe, Oceania, and the Americas, which saw a recovery of tax revenues over this period, following a fall in revenues after the 2008 financial crisis.

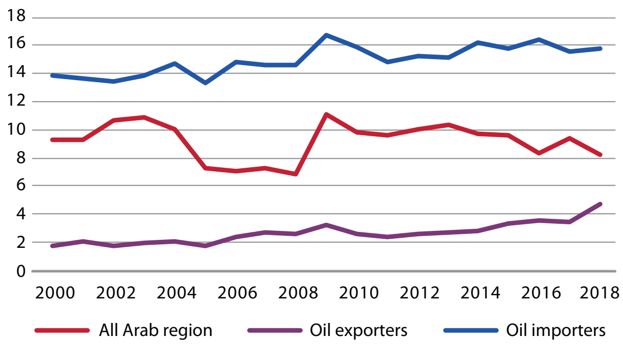
Figure III.A.2
Median tax revenue by region, 2002–2017
(Percentage of GDP)



Source: IMF.

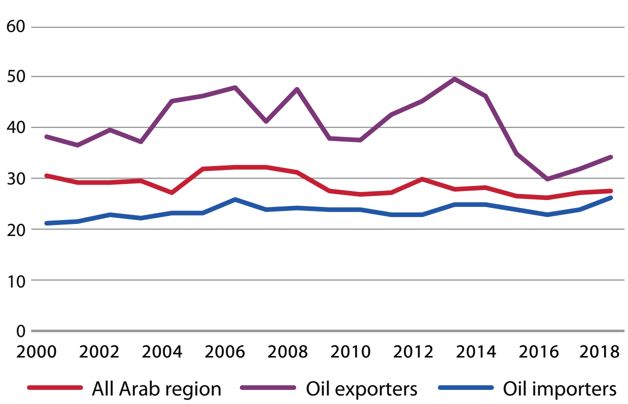
Revenues also vary widely from country to country within a single region. While revenues in Africa fell on average across the region from 2012 to 2017, this mainly reflects the impact of the fall in commodity prices on tax revenues in commodity-dependent countries; tax revenues rose in 21 non-commodity dependent countries over the period. The Arab region is illustrative in this regard. Total revenues (which includes taxes, royalties and other revenues) in oil-producing countries fell over this period, while those of oil importers increased (figures III.A.3 and III.A.4). In the wake of the commodity price falls, many countries in the Arab region expanded tax revenue to offset royalty declines, but this failed to compensate. Oil exporters have introduced fiscal consolidation measures, although oil importers have as well. In this region, additional revenue could be mobilized through tax reforms that improve progressivity and compliance and broaden the tax base.[4]

Figure III.A.3
Median tax revenue, Arab region, 2000–2018
(Percentage of GDP)



Source: IMF.

Figure III.A.4
Median total revenue, Arab region, 2000–2018
(Percentage of GDP)

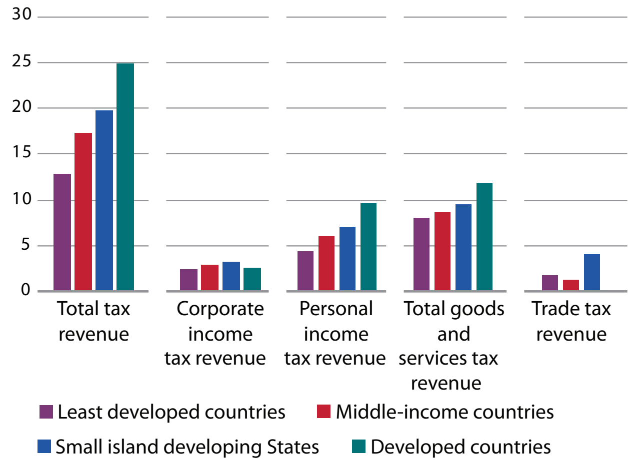


Source: IMF.

Revenue by tax type shows additional structural differences in tax revenues between countries and regions. All countries rely on taxes on goods and services followed by income taxes, with low (and often falling) shares of corporate taxation. Most of the increase in taxes since 2007 came from taxes on goods and services (primarily value added tax (VAT)), with the strongest increases in LDCs and SIDS (figures III.A.5 and III.A.6).

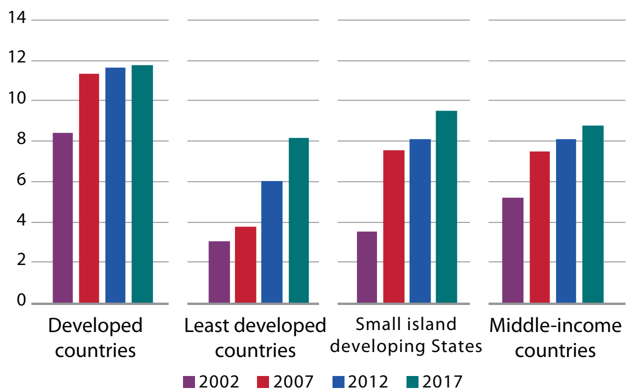
Developing countries are more reliant on corporate income taxes than developed countries, a reliance that in middle-income countries has grown over the last two decades. Developing countries, particularly SIDS, also rely more on trade taxes, although recent increases in tariffs (see chapter III.D) may temporarily affect the tax mix in some large economies.

Figure III.A.5
Median tax revenue by type of tax, 2017
(Percentage of GDP)



Source: IMF.

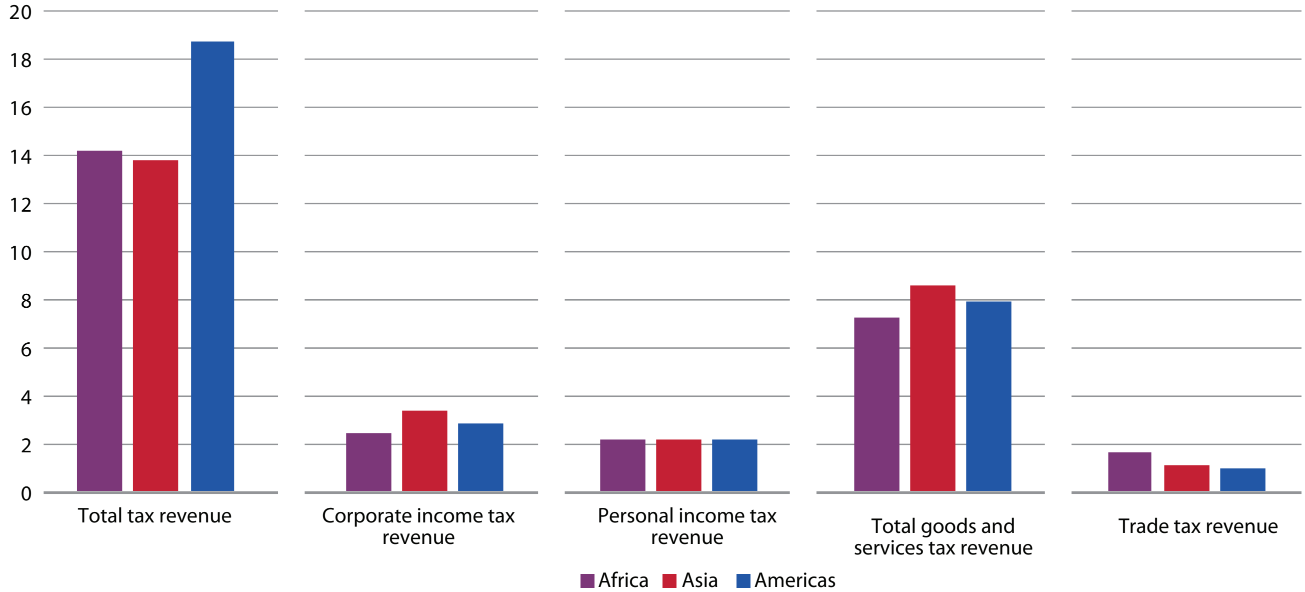
Figure III.A.6
Median goods and services tax revenue, 2002–2017
(Percentage of GDP)



Source: IMF.

Tax policies and decisions on the optimal tax mix for each country will depend on national economic and social structures, as well as national political priorities. But they are also influenced by and must respond to global trends, such as the impact of technological changes on wages and profit shares (see chapters I and II). In a global environment of low interest rates, countries with access to markets may find borrowing more politically expedient than undertaking onerous tax reforms. The political environment for changes in the tax mix also needs to be considered, as widening the tax base means some constituencies that previously were not paying (or were paying very little) income tax will now be asked to make greater contributions to domestic public resources.

Figure III.A.7
Median tax revenue by type of tax, by region, 2017
(Percentage of GDP)



Source: IMF.

Medium-term revenue strategies

The 2019 *Financing for Sustainable Development Report* highlighted the importance of integrated government planning in raising resources and achieving the SDGs. A medium-term revenue strategy (MTRS) can be a cornerstone of effective tax reform and development policy and an important element of broader effective government planning. (Such broader planning can happen through INFFs.) An MTRS is a comprehensive approach to tax reform, based on revenue goals that are aligned with development needs, including social and economic equality, gender parity and inclusion, and environmental impacts. It considers revenue mobilization to support greater public investment as well as the revenue system's impacts on economic and social development. By linking revenue collection to expenditure for quality public service delivery through political and business cycles, an MTRS can strengthen the social contract between citizen and state.

Developing a country-owned MTRS can be a mechanism for Governments to meaningfully address their own unique challenges in revenue mobilization, as well as a framework within which Governments can adapt and adjust reforms as implementation challenges arise. As of 2019, 19 countries are in some stage of development of an MTRS in collaboration with the International Monetary Fund (IMF) or the World Bank Group.[5] Twelve other countries have begun the process of dialogue pre-formulation, including workshops, consultations with stakeholders, and initial tax policy analysis.

2.2 Tax administration

Strengthened tax administration is an important component of medium-term planning. Tax administration suffers from lower capacity in LDCs and some middle-income countries. Low-income countries have approximately one tenth of the staffing of high-income countries (figure III.A.8). In all income groups, population per tax administration employee increased between 2016 and 2017, suggesting either decreasing capacity of tax administration or an increase in productivity of staff, perhaps through adoption of technology. The percentage of female staff and executives in tax administration increases with higher country-income levels (figure III.A.9). More equitable representation of women among staff at tax administrations and in finance ministries, which often make tax policy, can assist in ensuring that the gender impacts of fiscal policies are more effectively included in decision-making.

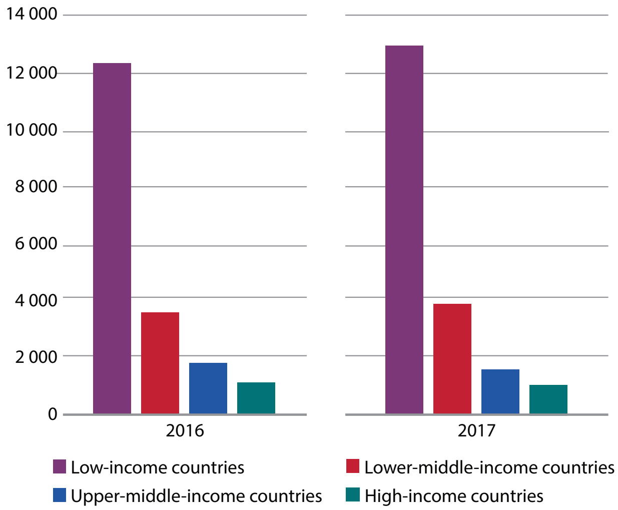
There are also other tools available that can help countries as they prepare revenue strategies. For example, the Tax Administration Diagnostic Assessment Tool (TADAT) is an assessment framework used to measure key components of a tax administration.[6] As at end-January 2020, 92 TADAT assessments have been conducted. The framework is being used (both formally and informally) to guide high-level decisions on tax administration reform efforts. Additionally, some customs administrations are using relevant elements of the TADAT framework—such as risk management, voluntary compliance and revenue accounting—to monitor performance and implement remedial measures.

Adoption of technological tools can increase capacity and productivity of tax administration staff and compliance with a tax regime. There are key differences in the use of technology in tax administration among countries of different income levels. For example, effective adoption of electronic filing not only streamlines efforts for the tax administration but can also reduce compliance costs for taxpayers.[7] Use of e-filing is significantly lower in low-income countries than in middle- or high-income countries, although rates increased from 2016-2017 across all groups (figure III.A.10). Similarly, lower-middle-income countries have the highest adoption rates on average of electronic payments, which lag in low-income countries (figure III.A.11). This indicates significant scope for improvements in efficiency of administration through adoption of digital technologies.

Figure III.A.8

Median population per full-time tax administration employee, by income group, 2016–2017

(Number of population)

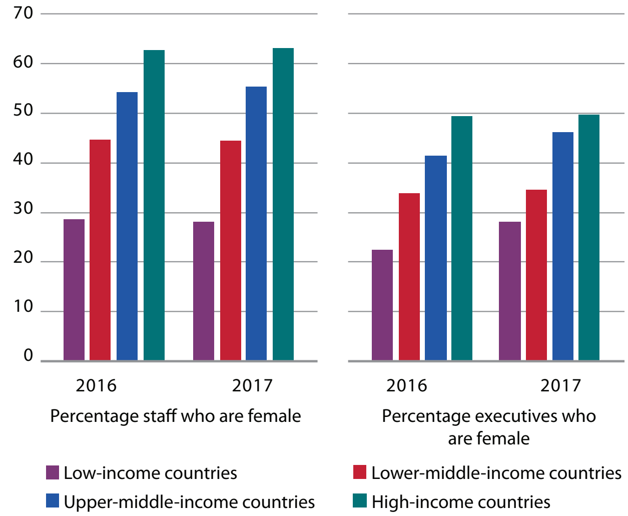


Source: IMF, International Survey on Revenue Administration.

Figure III.A.9

Average percentage of female staff and executives in tax administration, by income group, 2016–2017

(Percentage of staff)

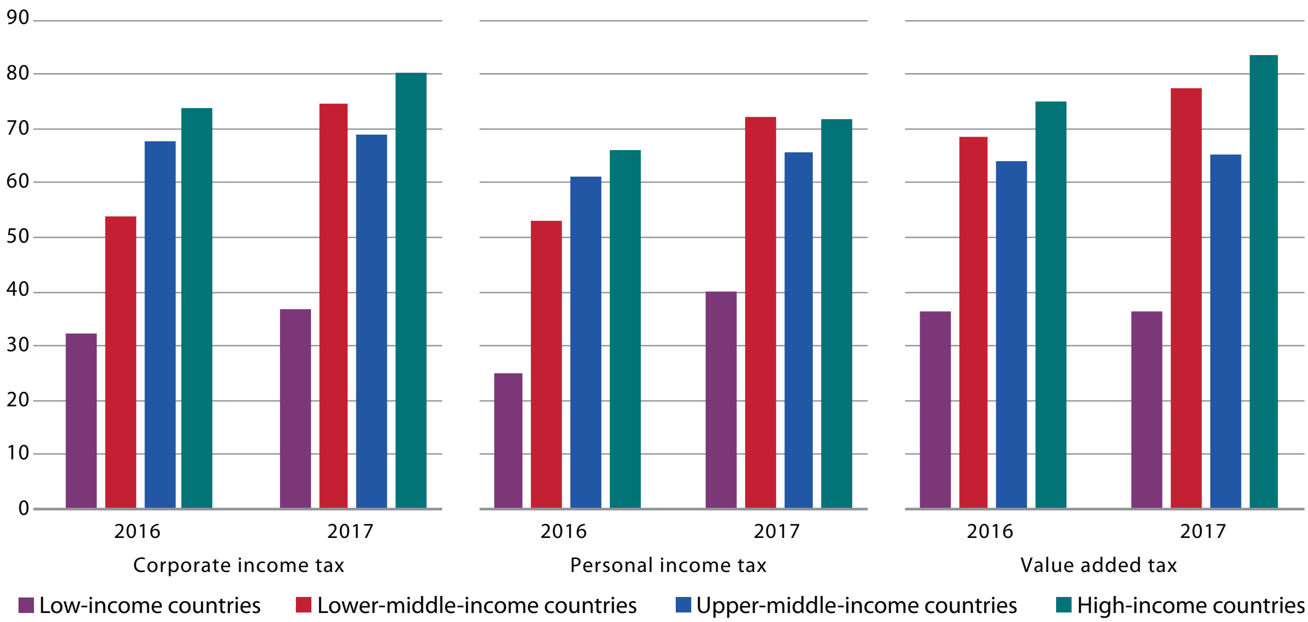


Source: IMF, International Survey on Revenue Administration.

Figure III.A.10

Average percent of returns e-filed by type of tax, by income group, 2016–2017

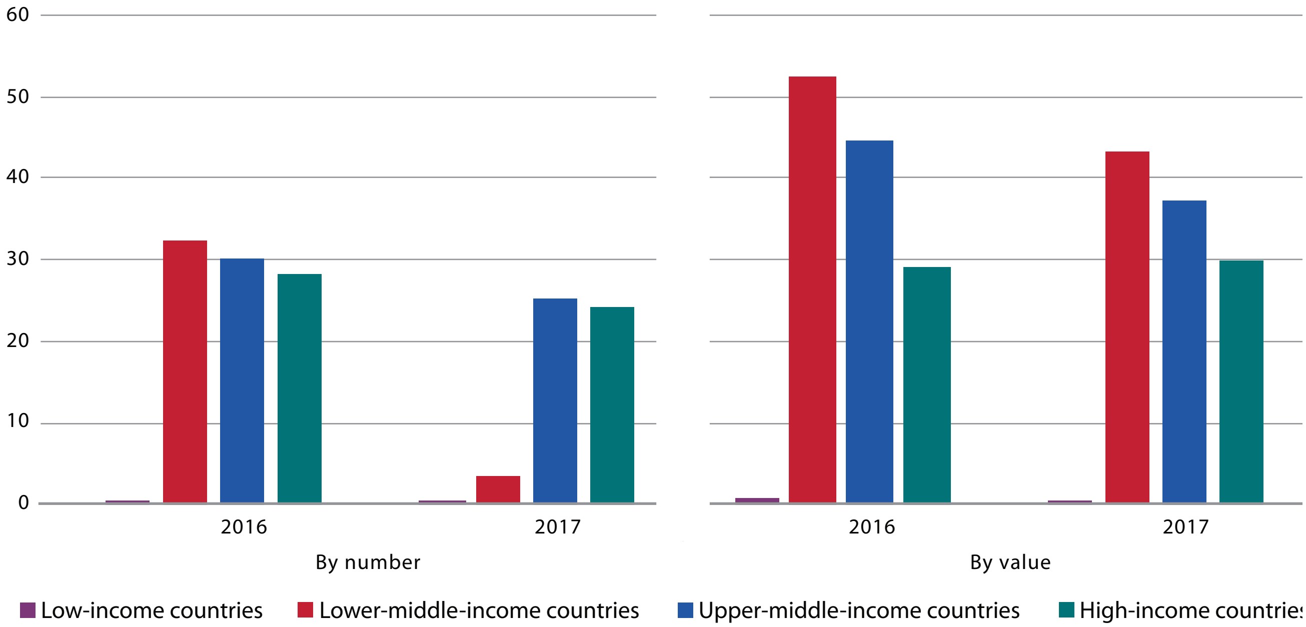
(Percentage of returns)



Source: IMF, International Survey on Revenue Administration.

Traditional technology and software solutions can simplify tax administration and provide an enhanced suite of e-services for taxpayers, with options ranging from integrated, purpose-built solutions to purchased, best-of-breed components to a comprehensive, commercial, off-the-shelf tax administration solution.[8] International partners are already helping countries with such solutions. Digital technology is also creating new tools to improve tax compliance and reduce the administrative burden on taxpayers. For example, technology can help strengthen accuracy of information in tax administration databases. Connected devices, such as secure electronic cash registers, can measure and transmit accurate real-time data and boost tax compliance by addressing unreported sales.[9] The technology at the heart of the sharing and gig economy also creates data, which can be used to facilitate transparency and simplification of tax obligations, with minimal burden on taxpayers and administrations alike.[10]

Figure III.A.11
Average percent of electronic tax payments, by income group, 2016–2017
(Percentage of returns)



Source: IMF, International Survey on Revenue Administration.

Big data approaches (see chapter II) can help identify suspicious or incorrect information. Combined with artificial intelligence (AI), it can also be used to improve identification of tax evaders. Some country authorities have experimented with using hack-a-thons—intense technology development sessions involving programmers and public officials—to quickly develop new AI tools that make use of multiple databases to validate information. Such approaches rely on the ability of multiple agencies and ministries, as well as potentially subnational authorities, to share information while maintaining trust and privacy. In the most advance practices, Governments can use non-government data to help validate governmental data or flag suspicious information.

For most developing countries, it is still too early to assess the impact of advanced technologies (such as AI), determine good practices, and target investments likely to have higher returns. However, the technologies do hold promise for countries at all levels of development. Investment in revenue administration, including in technology adoption, should be considered carefully alongside the entire package of revenue reforms, with investment that is tied to medium-term plans and coherent with the overall financing framework. International partners can back these investments with financing and capacity-building.

2.3 Tax avoidance and evasion

Revenue losses due to tax avoidance and evasion have direct negative impacts on the ability of the state to provide public and social services and indirect impacts on inequality and trust in the government and effectiveness of the state.

As taxes are a key component of the social contract, the perception of fairness of the system and the quality of public services can impact the likelihood of payment in full by individual taxpayers. If the taxpayer believes the tax system to be fair, that others with similar income are also paying their taxes, and that the quality of public services matches the tax burden, trust in the tax system may grow and even a taxpayer with the ability to evade taxes may not believe evasion is justified.[11] In practice, this virtuous circle can take many years to achieve, as changing social norms related to tax payment is difficult. Efforts to enhance tax compliance through raising trust need to be complemented with effective and credible enforcement and facilitation measures.[12]

Additionally, taxation of multinational entities (MNEs) is more complicated given their ambiguous participation in national social contracts. There is some evidence that MNEs pay proportionately less tax than small and medium-sized enterprises (SMEs),[13] and it is clear that actual taxes paid are much lower than statutory tax rates, often by design.[14] Multinational enterprises design their tax strategies at headquarters and may not participate in the social contract in any particular host country in the same way as a domestic enterprise. Internal MNE payment and other systems may incentivize staff to design corporate tax strategies that avoid corporate taxation in the host country.[15]

There are gray areas between tax avoidance/minimization techniques and unlawful tax evasion. For example, especially aggressive transfer-pricing approaches can be found, on further scrutiny by tax authorities, to have crossed over the blurry line between avoidance and evasion. Cross-country analysis of data from the International Survey on Revenue Administration shows that for tax audits—including those of individual and corporate taxpayers and across all types of audits (comprehensive, issue oriented and desk based)—rates of success are above 50 per cent. Figure III.A.12 shows that a very high percentage of comprehensive audits find that taxpayers are underreporting, although the relatively higher success rates in lower-income countries relate to a much lower number of audits. Data from the United States shows that around 70 per cent of corporate income tax returns undergoing further examination are subject to additional tax payments after examination,[16] although the majority of audits do not result in prosecutions for tax evasion. There are two implications: some taxpayers are using aggressive tax strategies that cross the blurry line, but it also indicates the need for greater clarity in the law to reduce the presence of gray areas.

The Task Force has regularly provided references to estimates of international corporate tax avoidance and evasion, predominantly in the form of corporate tax base erosion and profit shifting (table III.A.1). New research confirms previous findings that developing countries are more susceptible to profit shifting by multinational corporations than developed countries.[17]

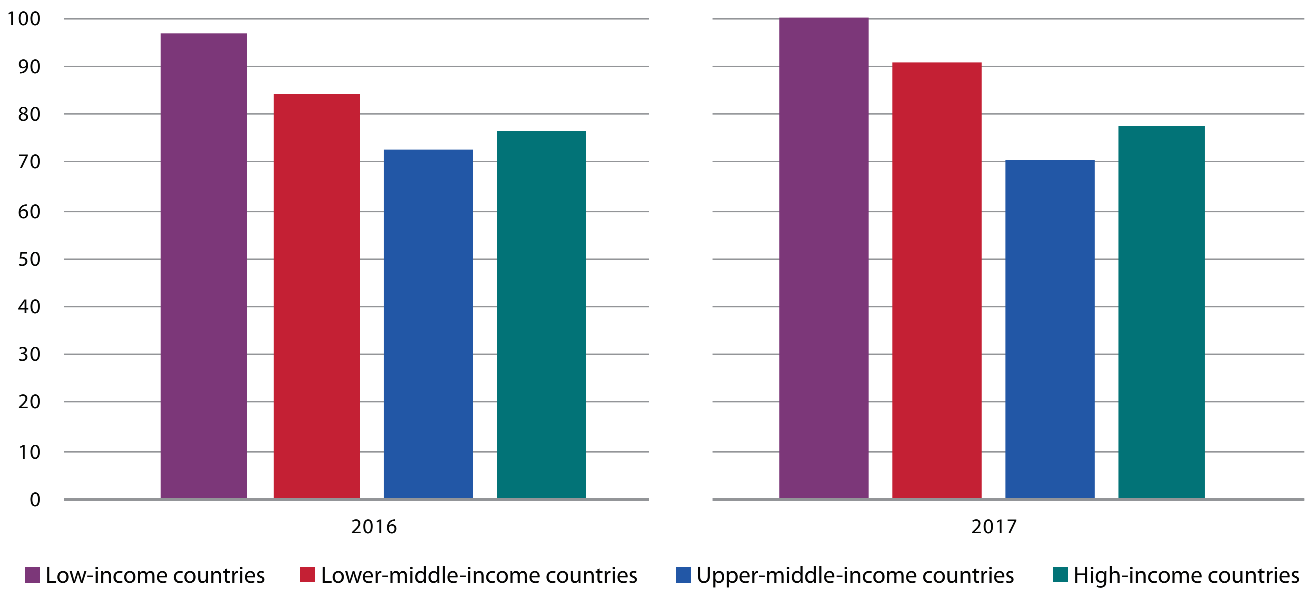
3. International tax cooperation

The Addis Agenda recognizes the need to scale up international tax cooperation as a complement to national tax policy and administration reform. The globalization of financial activities, and the advances in technology that reduce barriers to goods and financial flows, necessitate countries working together on tax matters and combatting illicit finance (see section 4). Through cooperation, countries can address the challenges of corporate and personal tax avoidance and evasion while encouraging investment through fair distribution of taxing rights.

3.1 Progress on tax transparency

Tax transparency and exchange of information between Governments provides tax authorities with access to banking, ownership, accounting and

Figure III.A.12
Comprehensive audit hit rate, by income group, 2016–2017
(Percentage of audits)



Source: IMF, International Survey on Revenue Administration.

Table III.A.1
Selected international corporate tax avoidance estimates

Volume estimate	*Underlying data used*	*Estimate provider*
Tax loss of 0.07% of world gross product in 2015 (approx. $50 billion) from profit shifting	Meta-analysis of estimates of impact of tax rates on profit declaration	Beer, S., Mooij, R. de, & Liu, L. (2019). "International Corporate Tax Avoidance: A Review of the Channels, Magnitudes, and Blind Spots". Journal of Economic Surveys.
Tax loss of $660 billion in 2012, or almost 1% of world gross domestic product	Survey of US multinational groups carried out by the Bureau of Economic Analysis	Cobham, Alex, & Janský, P. (2019). "Measuring misalignment: The location of US multinationals' economic activity versus the location of their profits". Development Policy Review, 37(1), 91–110.
Tax loss of $194 billion in 2016	Differential reporting of foreign direct investment shares based on reported rates of return	Janský, P., & Palanský, M. (2019) "Estimating the scale of profit shifting and tax revenue losses related to foreign direct investment". Int Tax Public Finance, 26, 1048–1103.

Source: Inter-agency Task Force on Financing for Development.
Note: Volume estimates are not comparable.

other types of information necessary for tackling cross-border tax evasion and avoidance. New and updated legal instruments to promote exchange of tax information and mutual assistance among tax authorities have had a significant impact on tax collection.

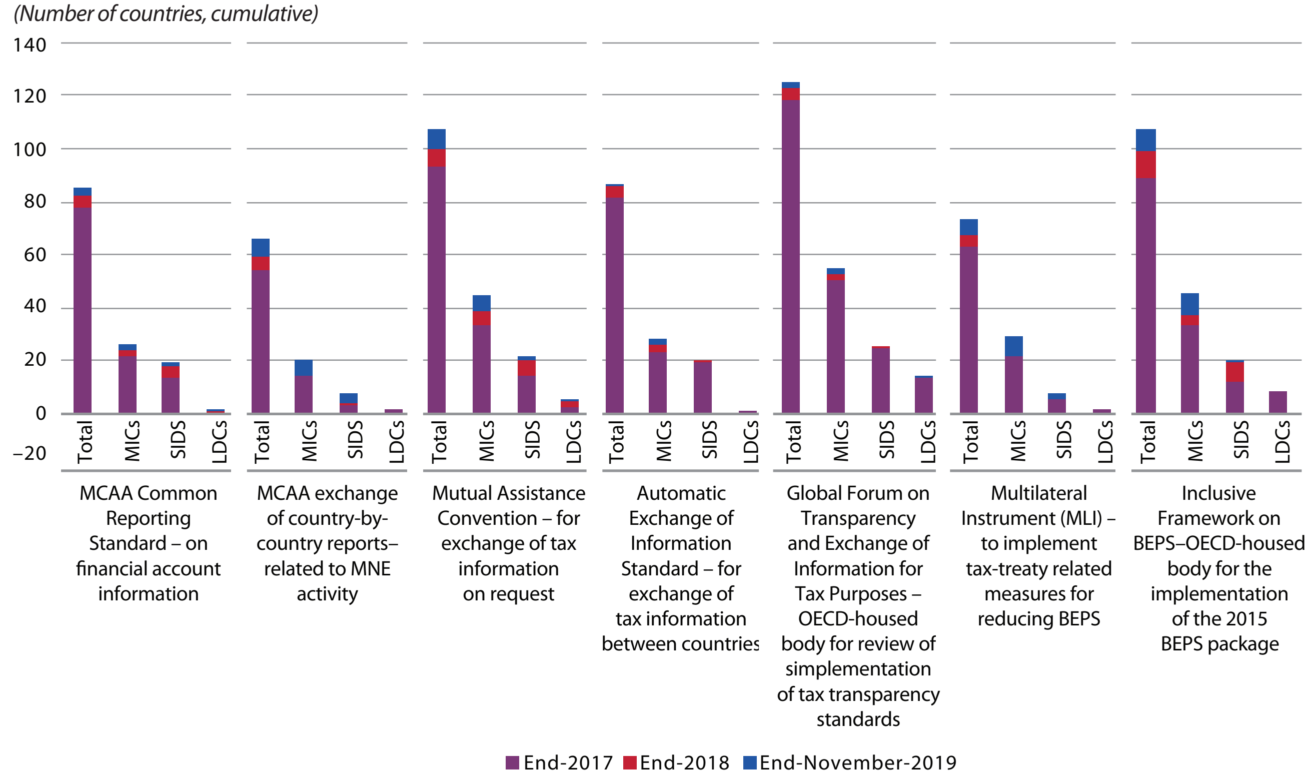
As shown in figure III.A.13, many developing countries do not participate in international tax cooperation instruments, with slow growth in participation since 2017. LDCs in particular lag significantly behind in their participation. For non-participating countries, most of which have not had a role in shaping the underlying tax norms, choosing whether to participate requires an assessment on multiple dimensions, which may include whether the rules are well adapted to their circumstances, whether they have the capacity to implement the rules effectively, and the possible opportunity costs of deprioritizing other potential tax policy or administrative reforms.

The Global Forum conducts peer reviews of all its member jurisdictions for compliance with international standards for transparency and exchange of information for tax purposes. This includes both exchange of information on request—which includes banking, ownership, financial accounting and other types of information—and automatic exchange of information on financial accounts of non-residents. A survey of Global Forum members provides indicative information that exchange of information requests have been increasing over time.[18]

To receive information on the financial accounts of non-residents automatically, countries must not only adhere to the relevant conventions, but must also reciprocally activate a bilateral relationship and satisfy confidentiality requirements. So far, 95 members of the Global Forum have begun exchanging financial account information automatically. Information on 47 million financial accounts with a total value of around €4.9 trillion were exchanged through 4,500 bilateral exchange relationships in 2018. The number of bilateral relationships grew to over 6,000 in 2019. In aggregate, middle-income countries now have over 1,500 relationships for receiving information, although no LDCs are receiving data from automatic exchanges. A number of developing countries have either elected not to receive information or have not yet passed the confidentiality requirements to be able to receive.

Using this data (i.e., checking whether the data received matches taxpayer declarations) requires sophisticated tax information systems and human capacity. Such information systems can make use of AI and machine learning to identify suspicious activity and accounts that should be more rigorously examined (see chapter II). As automatic exchanges commenced only recently, there is no comprehensive data yet on the amount of tax recovered due to the discovery of misreported information by the taxpayer. Still, taxpayers may fear audits and thus provide more accurate declarations of offshore assets, paying more tax as a result. Participation in voluntary disclosure programmes[19] and data on deposits in offshore accounts (see section 4.2 below) back this assumption. These changes in behaviour mean that any calculation of the payoff from investing in a more technologically sophisticated tax administration may be underestimated.

Figure III.A.13
Participation in international tax cooperation instruments, 2017–2019
(Number of countries, cumulative)



Source: OECD.
Note: Middle-income countries (MICs). Small island developing States (SIDS). Least developed countries (LDCs). Multilateral Competent Authority Agreement (MCAA).

One of the most highly sought changes in tax information exchange relates to the exchange of country-by-country reports of MNEs. Country-by-country information can help tax authorities assess the risk that MNEs are not fairly applying arm's length transfer pricing (i.e., valuing internal group transactions at fair market prices, and thus not shifting profits to low cost jurisdictions). The development of country-by-country reporting for MNEs was agreed as part of the OECD/G20 BEPS Action Plan in 2015 and will be reviewed this year. Forthcoming changes to tax norms related to MNE taxation in the context of increased digitalization (see section 3.2), may warrant changes to the information that is shared, either in these reports or through new reporting requirements.

As of end-2019, over three quarters of the members of the Inclusive Framework on Base Erosion and Profit Shifting (BEPS) have introduced a country-by-country reporting filing requirement. As a result, substantially every MNE with consolidated group revenue above €750 million is now preparing country-by-country reports for their home jurisdiction. However, host jurisdictions can only get access to non-local country-by-country reports by agreeing to another international instrument and having a bilateral match. At end-November 2019, there were more than 2,000 bilateral exchange-of-information relationships for country-by-country reporting; 933 of these involve middle-income countries, up from 745 in 2018 and 477 in 2017. Currently no LDCs receive country-by-country reports through information exchange.

3.2 Taxation of the digital economy

The 2019 *Financing for Sustainable Development Report* outlined the conceptual issues countries face as they grapple with taxation of the digital economy (see also chapter II). The growth of e-commerce and digital business models can disrupt different fiscal systems, including indirect and direct taxation.

The increased supply of goods or services across borders has introduced challenges to collecting VAT and goods and services taxes (GST). The complexity of organizing, administering and enforcing VAT/GST payment under traditional rules when the supplier and the digital platform are not located in the jurisdiction of the customer can cause considerable revenue losses if no appropriate measures are taken. A key question is what role country authorities expect of digital platforms in the collection of VAT/GST on online sales and whether the legal framework is in place to enable them to play that role. The Organization for Economic Cooperation and Development (OECD) has developed standards to address the complexity, including through VAT/GST-collection obligations for e-commerce marketplaces and other digital platforms. Over 50 countries, including 12 middle-income countries, have already implemented these standards, and other developing countries are looking to do so. Rather than trying to collect VAT/GST from digital platforms, other countries are making collection a requirement for other actors in the supply chain, such as financial institutions issuing credit cards in their jurisdictions. Such approaches are relatively new, and it is too early to assess their effectiveness.

In relation to the taxation of multinational corporate profits, digitalization changes the demands on residence-based and source-based taxation because it is now easier to operate in a market without triggering tax residency rules. In the traditional tax rules, taxation in the source country is usually based on physical presence in the jurisdiction. Once the right to tax the MNE has been established, MNE profits are allocated between jurisdictions based on the arm's length principle (i.e., using market prices to value internal group transactions). However, arm's length pricing may not adequately reflect value creation in highly digitalized businesses, when intangible assets are an important part of value creation, or if interactions with users creates value for businesses. This has led to questions about the appropriate threshold of economic engagement that justifies the right for corporate income taxation in a jurisdiction and the most appropriate methods of profit allocation.

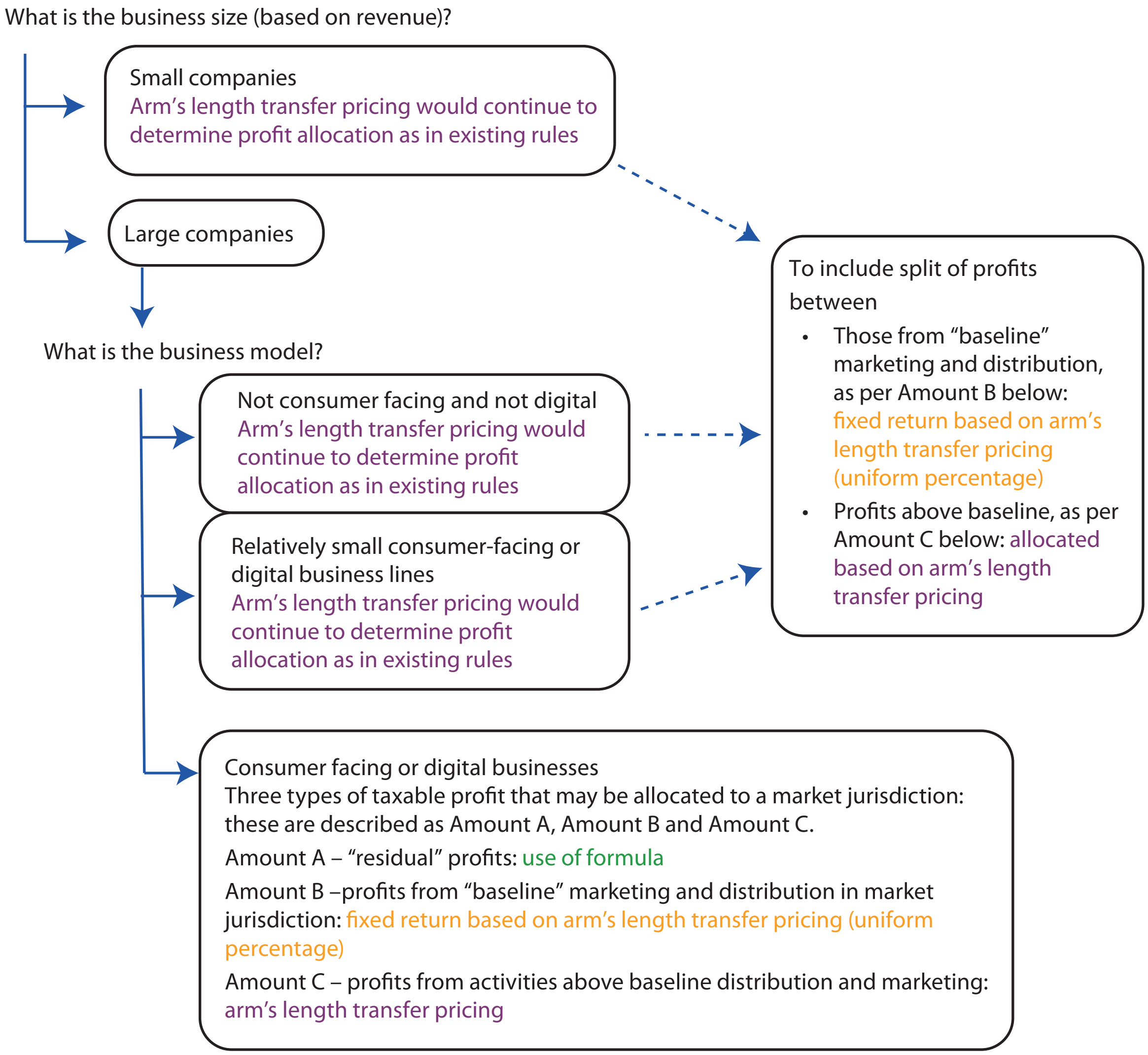
The policy discussions on how to address the range of challenges have advanced significantly since 2019. At the OECD-housed Inclusive Framework on BEPS, a Programme of Work was agreed as the basis for negotiations in May 2019, which contained two pillars of work: (i) a review of the rules that determine if a business has a taxable presence (called "nexus" in tax agreements) and how profits should be allocated; and (ii) global minimum taxation rules giving jurisdictions the right to "tax back" when taxpayers are subject to low levels of effective taxation in other jurisdictions (called the Global Anti-Base Erosion proposal, or "GloBE" for short).

For pillar one, the OECD secretariat had issued a proposal for a "unified approach".[20] It would create (i) a new definition of which businesses have a taxable presence that does not rely on physical presence, and; (ii) a profit allocation rule that uses formulas, rather than arm's length pricing, for apportioning some of their profit. This approach is more complex than the original ideas outlined in the 2019 *Financing for Sustainable Development Report*. Rather than redefining what is a taxable presence for all businesses, the unified approach proposes that a new definition only applies to companies that either have highly digital business models or are consumer-facing businesses. Second, the proposal on profit allocation suggests that, for these businesses, corporate profit would be split into three different components with different rules applying to each component (figure III.A.14). The proposal does not yet include precise definitions or thresholds for each component. One of those three different components relates to baseline distribution and marketing, for which the proposal is suggesting a simplification of existing rules so that there is a fixed amount of profit allocated to the source country. This new fixed remuneration could be applied to all businesses.

The complexity of the proposal has generated significant debate and disagreement on the wisdom of adopting such rules and their usefulness to developing countries.[21] Recently, one systemically important country proposed that the new pillar one norms be implemented on a safe harbour basis,[22] which would allow companies to either opt in or opt out of the rules globally. This could, depending on the regime for those that opt out, put Governments' tax collection in a weaker place than today.

A further feature of the proposal is the creation of effective and binding dispute prevention and resolution mechanisms to improve tax certainty. Currently, given the sovereign nature of tax, countries generally resolve tax disputes with taxpayers domestically. However, as the adjustments made by a tax authority in one country may lead to double taxation of an MNE, many countries agree, through their tax treaties, to mutual agreement procedures through which the tax authorities of the countries involved seek to resolve the double taxation. These procedures are not mandatory, and country authorities generally retain sovereignty to determine what is the appropriate amount of tax due in their jurisdiction. The new proposal creates a new approach to allocating profits internationally and, as a result, suggests new methods to resolve disputes and prevent double taxation. It seeks to limit the ability of countries to seek tax payments that they

Figure III.A.14
Unified approach to profit allocation



Source: UN DESA.

determine are due, although the details have not yet been agreed. Mandatory binding arbitration on tax disputes is opposed by many developing countries, not least because many countries have negative perceptions of binding arbitration brought under investor-statement dispute settlement clauses that are part of many international trade and investment agreements (see chapter III.D).

On pillar two, related to minimum taxation, the proposal aims to enable countries to subject all corporate profits of MNE groups to a minimum level of effective taxation. It includes a number of complementary mechanisms: income inclusion at the level of shareholders, application to foreign branches and subsidiaries, denying deductions for certain intragroup payments, source-based taxation of other payments, and coordination with other rules. The actual minimum rate of tax to be applied under the pillar two proposal has not yet been discussed by the Inclusive Framework.

The members of the Inclusive Framework agreed to a statement on the two-pillar approach in January 2020, which affirmed their commitment to reach an agreement on a consensus-based solution by the end of 2020,[23] but also recognized that significant divergences will need to be resolved. Many Inclusive Framework members have expressed concern that implementing pillar one on a safe harbour basis could raise major difficulties, increase uncertainty and fail to meet all of the policy objectives of the process. The members aim for final decisions to be taken by consensus and as a package, with agreement on key policy features at the next meeting in July 2020.

Many countries have questioned the wisdom of agreeing to new rules without full and accurate economic impact assessments. Assessments are difficult to prepare because of a lack of accurate country-by-country information for all MNEs and significant uncertainty over the final thresholds and definitions that would be applied. Preliminary analysis prepared by the OECD, presented in February 2020, estimates the increase in global tax revenue as a result of the two pillars combined at up to $100 billion annually.[24] The estimates of revenue gains are concentrated in developed countries with large economies, but, as a percentage of corporate tax revenues, are broadly similar across jurisdictions at all income levels.

Discussions are also ongoing in the United Nations Committee of Experts on International Cooperation in Tax Matters' Subcommittee on Tax Challenges Related to the Digitalization of the Economy. The United Nations is holding a large workshop in September 2020 to build the capacity of developing country officials who will be advising their ministers and participating in the international negotiations on taxation of the digitalized economic activity. This capacity may also help authorities engage in regional tax cooperation mechanisms to coordinate measures, as well as consider alternatives in case no agreement is reached. Norms that are better adapted to developing-country capacities will necessitate less capacity-building, and thus may more quickly deliver financial returns in terms of increased revenue.

The 2019 *Financing for Sustainable Development Report* set out several dimensions of analysis that should be undertaken on proposed new tax norms: (i) the enforceability of the proposals given tax administration capacities; (ii) impact on existing tax policies; and (iii) the distributional impact of the proposals. These remain recommended dimensions of analysis that Member States should undertake. They can guide an understanding of whether new proposals will further exacerbate tax gaps described in the first section of this chapter, lead to increased revenue mobilization, or undermine the long-term ability of Governments to align tax policies with sustainable development. In the Addis Agenda, Member States emphasized the importance of inclusive cooperation and dialogue among national authorities on international tax matters. This emphasis should be retained as countries decide on tax norms that could potentially be in place for another century.

Box III.A.1
Platform for Collaboration on Tax

The Platform for Collaboration on Tax (PCT) is a joint effort, launched in 2016, by the United Nations, World Bank Group, International Monetary Fund, and Organization for Economic Cooperation and Development (OECD) to intensify cooperation on tax issues across international institutions. The PCT work plan, outlined in its most recent progress report,[a] consists of three main workstreams: (i) detailed exchange of information on domestic revenue mobilization capacity development activities; (ii) analytical activities; and (iii) outreach activities.

The platform partners have developed an online information platform that consolidates the data from the four organizations that is being launched as part of the revamped PCT website in March 2020. Additionally, PCT partners have continued to coordinate on work related to medium-term revenue strategies (MTRS) and develop toolkits for developing countries. PCT partners are also working on the revision of the guidelines on the tax treatment of official development assistance by actively participating, along with the OECD Development Assistance Committee, in the relevant subcommittee of the United Nations Tax Committee. PCT partners also offer training on the application of PCT toolkits. Plans for 2020 also include the organization of two regional workshops around MTRS.

a World Bank, "Platform for Collaboration on Tax: PCT Progress Report 2018-2019 (English)".

3.3 Capacity-building efforts

The discussion above underscores the importance of strengthening capacities for tax policy design, administration and enforcement. Such investment has high returns and should support country-owned and country-created strategies for revenue mobilization. To meet the needs of a changing world, tax capacity-building also needs to adapt. Indeed, when developing countries agree to new norms in their interests, they often need to build new capacities to implement those norms effectively. Yet, there is no single best strategy for provision of capacity-building, nor a single type of intervention that is more effective across all countries. In 2016, the Platform for Collaboration on Tax (box III.A.1) made recommendations on enhancing the effectiveness of external support in building tax capacity in developing countries, which remain relevant to capacity-building partners.[25]

There are now four years of data on the volumes of official development assistance (ODA) dedicated to enhancing domestic public resource mobilization. In 2018, ODA disbursed for this purpose jumped 23 per cent year on year to reach $261 million, or 0.22 per cent of ODA, still short of the 2016 peak of $329 million.

The PCT partners are increasing their capacity-building. Examples include Tax Inspectors Without Borders, a joint initiative of OECD and the United Nations Development Programme; technical assistance related to implementing new or revised tax transparency and exchange of information standards; the United Nations trainings of tax officials, back-to-back with meetings of the United Nations Tax Committee and its subcommittees; the approximately 180 person years of technical assistance in the latest fiscal year provided by IMF; and the World Bank's new public-private partnerships on the use of innovative technologies for tax administrations.

4. Illicit financial flows

Combating illicit financial flows (IFFs) involves an essential development challenge, as IFFs reduce the availability of valuable resources for achievement of the 2030 Agenda. There is no agreed definition on what constitutes "illicit financial flows" and this term still generates disagreement. The Task Force agreed in 2017 that there are generally three components of IFFs (although not mutually exclusive or comprehensive): (i) IFFs originating from transnational criminal activity; (ii) corruption-related IFFs; and (iii) tax-related IFFs (figure III.A.15). As the different components are not comparable, the Task Force has noted that separate analysis of channels or components is more effective and can prevent double counting in aggregations.

Because IFFs are, by definition, a cross-border phenomenon, action to combat them needs to be taken at both national and international levels. Policy responses are best considered in a component-by-component or channel-by-channel approach, although some measures can be effective against multiple types of IFFs. IFFs, regardless of the component, will typically pass through or involve many people. Proxies, advisors, intermediaries, financial institution staff, and professional service providers (e.g., lawyers, accountants) are all involved in the typical chain of transactions that move a resource to the resulting asset. Companies and firms that control markets, direct financial flows, pay bribes, or set the stage for state capture are involved. This emphasizes the importance of the eco-system of institutions needed to combat illicit financial flows; it is not just financial intelligence units, tax administrations, and customs agencies. Standard-setting and regulation, supervision and enforcement are also relevant to combatting the enablers of illicit finance. A more synchronized whole-of-government approach is needed, including professional service and financial regulators and supervisors, prosecutors, the judiciary, foreign and finance ministries, and political decision-makers. Internationally, greater focus on improving policy coherence must continue to be a priority,

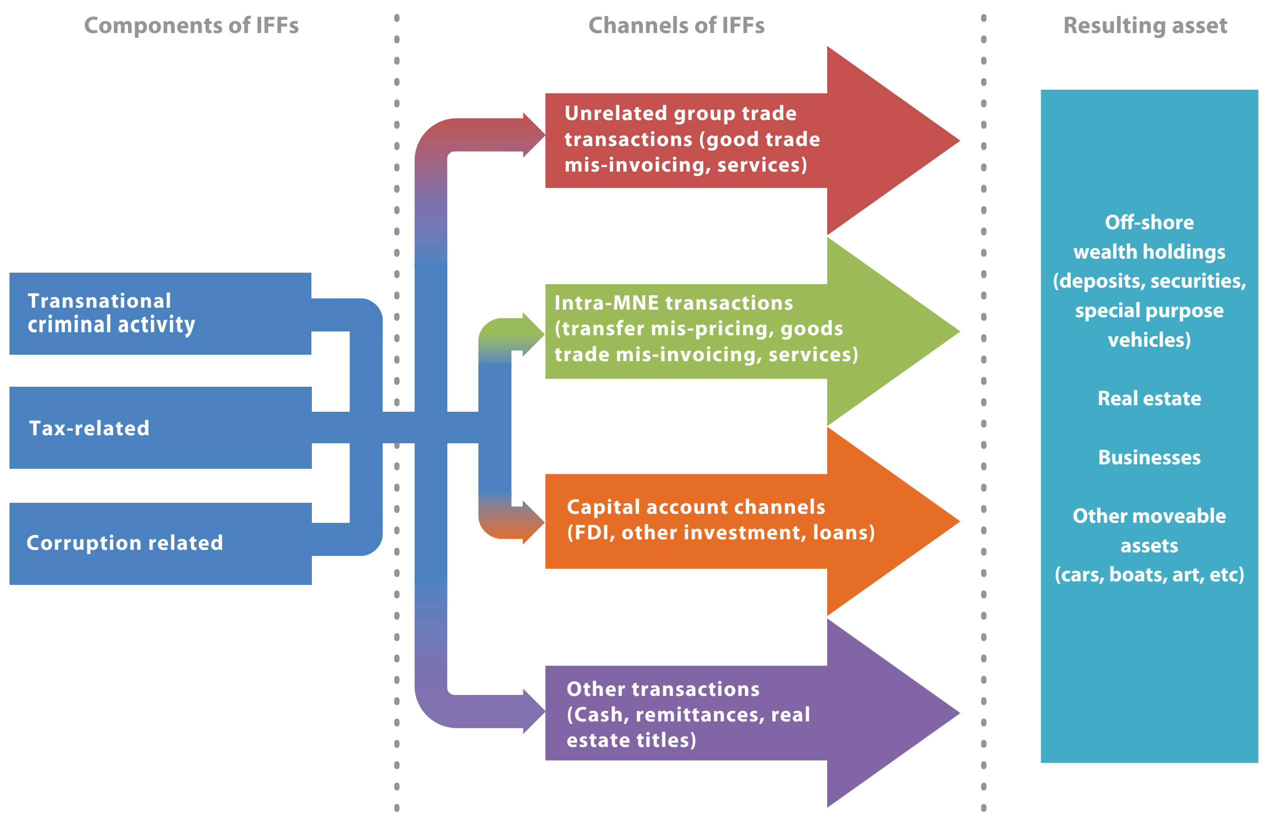
4.1 Volume estimates

In early 2019, the United Nations Conference on Trade and Development and the United Nations Office on Drugs and Crime (UNODC)—the joint custodians of SDG Indicator 16.4.1 on illicit financial flows—established a Task Force on the Statistical Measurement of Illicit Financial Flows, composed of representatives of official statistics, tax and customs authorities of several countries in Europe, Africa and Latin America, as well as international institutions, including Eurostat, the IMF, OECD and the United Nations Economic Commission for Africa.

A conceptual framework for IFFs, including a concise definition and typology to define the scope of measurement was submitted to the Inter-agency and Expert Group on SDG indicators (IAEG-SDG), which develops the global indicator framework for the SDGs. In October 2019, the IAEG-SDGs endorsed a reclassification of the indicator to Tier II, signifying that it is conceptually clear, has an internationally established methodology and standards, but that data is not yet regularly produced by countries. This framework defines IFFs "as financial flows that are illicit in origin, transfer or use; that reflect an exchange of value instead of purely financial transactions; and that cross country borders." Four main categories of IFFs are identified in this conceptual framework, according to the activity generating them: tax and commercial practices, illegal markets, theft and terrorism financing, and corruption. In essence, it further refines this Task Force's schematic approach (figure III.A.15), by dividing IFFs related to criminal activity into two separate categories: (i) illegal markets and (ii) theft and terrorism financing.

The next steps include the development of statistical methodologies to underpin estimations at country level. These estimates will shed light on the most appropriate statistical methodologies to estimate IFFs and provide additional evidence to help policymakers prepare or target interventions.[26]

Figure III.A.15
Schematic diagram of illicit financial flows



Source: Inter-agency Task Force on Financing for Development.

Note: Resulting asset will be considered a 'stolen asset' if it is the product of corruption-related IFFs. Components of IFFs include both source of funds and motivations of IFFs and may not be mutually exclusive. Individual transactions from different channels may be combined by actors to try to obscure the source, motivation and/or use of funds. Arrows do not represent estimates of the magnitude of flows, and are illustrative rather than comprehensive."

4.2 Policy measures for tax-related IFFs

Tax-related IFFs are being tackled with some of the international tax cooperation tools described earlier, which increase tax transparency and exchange of information and make it more difficult to hide wealth or transactions through offshore structures. The global exchange of information network facilitates access to the information and assistance from the destination (or intermediary) countries for IFFs. A recent study finds that bank deposits in international financial centres from non-bank counterparties, which increased significantly from the early 2000s to 2008, fell by 24 per cent ($410 billion) by the first quarter of 2019. These falls are significantly correlated with the country hosting the financial centre signing automatic exchange-of-information agreements.[27]

The Global Forum has incorporated into its standards a requirement to ensure the availability of beneficial ownership information for all legal entities and arrangements. This is resulting in a synergy between the Financial Action Task Force (FATF) (see section 4.4) and the Global Forum processes, and enables extensive peer review of countries performance on beneficial ownership information, covering both legal framework and enforcement in practice. Since 2016, one third of the recommendations (164 out of 418) issued to jurisdictions in Global Forum peer reviews have pertained to beneficial ownership information, indicating that more needs to be done to fully implement the beneficial ownership requirements.

The techniques used to launder the proceeds of crimes and to commit tax crimes are often similar. There is a need to improve cooperation between tax and anti-money-laundering authorities. International institutions have provided tools and training for how tax authorities can assist in money-laundering awareness.[28] Key lessons are the need for efficient information-sharing and a culture and mechanisms of cooperation between the two types of authorities.

4.3 Tackling corruption and state capture

Corruption is a complex social, political and economic phenomenon that affects all countries. Many international organizations have adopted a definition of corruption that encompasses the abuse of public office for private gain. The United Nations Convention against Corruption (UNCAC) lists bribery, embezzlement, abuse of functions, trading in influence, obstruction of justice, and money-laundering as types of corruption. Private corruption, which involves the misuse of any entrusted position for private gain at the expense of the interest of a company or society, is included. Many corrupt transactions involve both public officials and private sector actors. Corruption often involves entrenched power structures, systems of societal relations, and social norms which together form a system of incentives that bind a network of actors into a governance arrangement that does not involve impersonal application of neutral rules.[29] By undermining trust in Governments, corruption not only results in immediate potential loss of resources but also undermines the social contract. This reinforces political settlements that involve low public resource mobilization and ineffective service delivery by Governments.

The impacts of corruption come in political, economic, social, and even environmental outcomes. Corruption may lead to higher profits for the companies involved, as well as reductions in public revenue and inefficient public expenditure. The impact of corruption on growth has been studied extensively. Empirical research finds that GDP per capita is positively correlated with a perceptions-based indicator called "control of corruption,"[30] but causal relationships are difficult to establish, in part because of the difficulty in accurately measuring corruption.

Different acts of corruption also have vastly different impacts on sustainable development and the breaking of the social contract. Grand scale theft of public assets and state capture have fiscal implications, and possibly broader macroeconomic ones, while also destroying public trust of the state. Highly localized low-ticket bribery related to service delivery generally does not impact on the fiscal system nor have a broader macroeconomic impact, although it can have significant impacts on the victims of bribery who may be extremely poor and thus may suffer disproportionately even from a small bribe. There is evidence in several spheres for corruption being associated with worse environmental outcomes.[31]

Extractive industries, due to the large volumes of transactions, rents and profits connected with mining and fossil fuel exploitation, seem to attract more attention from corrupt actors than other sectors. This relationship has motivated the early and more advanced development of transparency norms in the sector, such as the Extractive Industry Transparency Initiative and the European Union's adoption of an Accounting Directive that has, since 2016, required public country-by-country reporting of payments to Governments by the extractive and logging industries. On the positive side, surveys of firms in many countries suggest a decline in bribery.

Programmes that have successfully reduced corruption have been associated with much higher tax revenue generation.[32] National frameworks for transparency and accountability can reduce the opportunities for corruption, but the success of any particular framework in reducing corruption will depend on the national political settlement and institutional arrangements.[33] Procurement policies (see section 5.2) can be models for public transparency and accountability. Political arrangements can sometimes undermine both the effective enforcement of formal rules and corruption prevention strategies. In these contexts, anti-corruption interventions can be prioritized based on political feasibility and the criticality of the sector to wider anti-corruption efforts. Interventions can thus be organized sequentially based on the scale of impact on sustainable development prospects.[34]

Technology can be useful in disrupting existing norms or incentives. For example, using technology to distribute government service access can empower citizen voice, change the dynamics of service delivery, and bolster the social contract. Long-term success usually requires redistributing power and changing norms, for which a new stable political settlement must be found.

The UNCAC is the only legally binding universal anti-corruption instrument. The Convention's far-reaching approach and the mandatory character of many of its provisions make it a unique tool. The Convention covers the four main pillars of anti-corruption: preventive measures; criminalization of corruption and law enforcement; international cooperation; and asset recovery. Based on peer reviews in the areas of criminalization of corruption and law enforcement and international cooperation, conducted under the Implementation Review Mechanism of UNCAC, a set of non-binding recommendations and conclusions can help guide Member States.[35] Highlights of these good practices include (i) strengthening data collection; (ii) the adoption of comprehensive legislation for the confiscation of proceeds of crime; (iii) access to information by law enforcement authorities; (iv) the cooperation of private sector with anti-corruption authorities; and (v) expanding the spontaneous transmission of information that could assist in investigations and criminal proceedings in other countries.

4.4 Money-laundering standards

Combating money-laundering helps to preserve the integrity of financial institutions, both formal and informal, and protect the smooth operation of the international financial system. The UNCAC includes article 14, which obligates all States parties to set up a regulatory regime for financial institutions in order to deter and detect all forms of money-laundering, while article 23 requires the criminalization of the laundering of proceeds of crime. In the Addis Agenda, Member States committed to identify, assess and act on money-laundering risks, including through effective implementation of the FATF standards on anti-money-laundering/counter-terrorism financing. As its 40 members and observers include all members of the Group of 20, and all major financial centres, FATF standards operate as de facto global standards for the world's financial system. FATF conducts peer review for adherence to its standards, as do nine FATF-style regional bodies covering most countries of the world.

4.5 Asset recovery and return

The process of tracing, freezing, confiscating and returning stolen assets to their country of origin is usually a complex and lengthy one, involving multiple jurisdictions and often complicated by technical, legal or political barriers. Chapter V of UNCAC provides the framework for the return of stolen assets, requiring States parties to take measures to restrain, seize, confiscate, and return the proceeds of corruption.

The Stolen Asset Recovery (StAR) Initiative, a joint project of the World Bank Group and UNODC, promotes implementation of Chapter V of UNCAC. StAR is currently conducting a new survey on international asset recovery efforts in corruption cases. The study aims to collect data on global progress in international efforts to recover and return proceeds of corruption in a systematic and internationally comparable way. Better data on corruption-related asset recoveries and returns worldwide is needed to promote the timely return of proceeds of corruption; identify trends in asset recovery practices and volumes; provide an evidence base for policymaking; promote transparency and accountability in international asset recovery; and measure progress towards commitments. More specific recommendations in the area of asset recovery are also being distilled from the second cycle of peer reviews under the UNCAC Implementation Review Mechanism, which is currently in progress.

4.6 International responses

On the global level, international institutions continue to support countries. The World Bank will be issuing a Global Corruption Report in mid-2020. The IMF executive board plans to do a stock-take on the institution's work on IFFs in September 2020, which will showcase the Fund's wide-ranging work in this area and identify gaps to be addressed. One area for possible further cooperation is in developing the technological tools that can be used to help identify and combat IFFs. While such tools will need to be adapted to individual country contexts and risk factors, the creation of AI software that can be applied in many jurisdictions could introduce efficiencies of scale, thereby lowering costs for individual countries. Regional tax and anti-money-laundering cooperation bodies can be venues for exploring joint work. However, they cannot be one-off developments, as the software and tools will need to constantly evolve to spot the latest loopholes and threats.

In early March 2020, the President of the General Assembly and the President of the Economic and Social Council jointly launched a High-level Panel on International Financial Accountability, Transparency and Integrity (FACTI Panel). The panel will produce an interim report outlining its analysis in July 2020, and its final report providing recommendations in February 2021. The General Assembly is organizing a Special Session on corruption in April 2021.

5. Expenditure and strategic procurement in public budgets

As the main vehicle for implementing government policy, the budget should be intimately linked with the attainment of SDGs. Budget processes are a critical link in the chain connecting sustainable development objectives, strategies and plans, public spending and, finally, outcomes.[36] A well-formulated medium-term budget framework (MTBF) is a natural platform for integrating the SDGs with domestic public resource allocation. These MTBFs need to be coherent and consistent with other elements of a country's INFF.

Most countries require significant additional spending to achieve the SDGs. By making use of multi-year estimates of expenditure and revenue to frame budget decisions, an MTBF enables a strategic approach to budget preparation and spending priorities. This highlights the costs and potential trade-offs of various policies. For example, some types of transport policies which provide short-term economic gains ultimately conflict with climate objectives. Strong MTBFs are based on an iterative budget process that aims to reconcile the top-down fiscal discipline set by ministries of finance with bottom-up costing of policies by spending ministries. Effective MTBFs need not be overly rigid, as line ministries may need some flexibility to adapt to developments on the ground, such as a disaster or epidemic. Indeed, the outbreak of COVID-19 in early 2020 demonstrates this need for spending flexibility, as governments facing rapid spread of the disease needed to use emergency spending to bolster public health systems, including for provision of medical care for those who caught the virus and for implementation of preventative measures.

In the shorter-term, financial management information systems (FMIS) support the automation and integration of public financial management processes including budget formulation, budget execution, accounting, and reporting. These technological tools have been increasing in efficiency and effectiveness since they started to be widely adopted in the 1980s. FMIS can significantly improve the efficiency and equity of government operations and service delivery. If used effectively and strategically, they also offer potential for increasing participation, transparency and accountability in expenditure. More advanced FMIS can directly integrate with the provision of e-governance, where public services are provided online (see chapter II).

5.1 Financial instruments for expenditure

Governments have honed their public financial management skills over decades. While each government's procedures and tools might be slightly different, countries have standard ways to budget and spend resources. Still, many are looking for new tools, instruments and innovations that can lead to better expenditure which is more focussed on the SDGs.

In private sector financial markets, an assessment of a company's creditworthiness and efficiency generally begins with an analysis of three types of information that companies report: income statements - which report revenue and expenditure; balance sheets – which report assets and liabilities; and cash flow statements – which look at cash availability, the most liquid of financial assets. Private financial instruments (see chapter III.B) seek to combine different liquidity and risk return profiles so as to maximise the efficiency of financing. Yet, for the most part, public financial instruments treat public finance on an income or cash basis along with consideration of debt and debt sustainability (see chapter III.F). Few governments know the value of their public assets, nor how they those assets are used for sustainable development purposes.[37]

This is changing as there is a concerted effort to better understand public assets and their effect on public financial sustainability. In July 2019, the IMF released the most comprehensive dataset available on public sector balance sheets.[38] Further work has sought to estimate public sector balance sheet strength, taking into account different aspects of what governments own in addition to what they owe.[39] Practitioners at national development banks point out that using well-managed development banks as a tool for public investment allows for a more transparent accounting of both the assets and liabilities of the state (see chapter III.F).[40]

There is also interest in instruments that bring together public and private actors in different combinations of responsibility for delivery of public goods and services and with varying degrees of division of financial and operational risks and financial rewards between the parties. The Task Force wrote extensively about public-private partnerships (PPPs) in 2018, noting that project and country characteristics and national policy priorities would determine which financing model is best suited for specific investments.[41] In its 2017 report, the Task Force identified principles for effective use of blended finance and PPPs that were embedded in the Addis Agenda (see chapter III.C).[42]

A newer form of public-private financial instrument for service delivery is the social impact bond. Rather than using a contract to specify services a private entity will provide, as in a traditional PPP, in a social impact bond the government compensates a private partner for achieving specified outcomes. It then allows a service provider to deliver services towards that outcome without specifying the specific services to be provided.

A social impact bond is not a bond in the traditional sense. An investor provides upfront financing for the work of a service provider (often an NGO), but the government only repays the investor if the ultimate outcome is delivered. The advantages of such an approach are that it may allow the service providers to innovate and try new ways of working that would not be allowed under either regular public service delivery or a PPP arrangement, and achieve better outcomes. However, social impact bonds can be challenging as standards for success have to be clearly specified. Because the population of service recipients is unique in each use, it is incredibly difficult to set uniform thresholds or metrics for appropriate outcome targets and verification metrics. Failed service provision is also possible, as is inequitable treatment of service recipients, especially if the primate partner aims to cut costs. It may also have negative impact on work conditions and terms of service for public employees. Finally, some critics point out that investors may profit off the delivery of public services, which may exacerbate inequality and undermine the social contract. These instruments have been tried in both developed and developing country settings, but there is insufficient empirical evidence on their effectiveness across use cases to make a determination on their advisability.

5.2 Procurement effectiveness and alignment with sustainable development strategies

Public procurement frameworks can be used as strategic tools to reinforce sustainable development, as noted in the Addis Agenda. Given public procurement's weight in most economies and national budgets, improvements in the efficiency and effectiveness of this key government function, beyond mere rule-compliance, are an important lever for improving public spending.

Governments are increasingly employing public procurement to achieve policy objectives that are aligned with the 2030 Agenda, such as promoting innovation, sustainability, social inclusiveness and SMEs. Increasing fiscal pressures have further highlighted the potential gains from public procurement reforms.[43] As of 2018, all OECD countries reported to have developed procurement policies towards broader policy objectives, such as a green investment, promotion of SMEs, and innovation. Between 2016 and 2018, there has been an upward trend in the development of policies addressing green procurement and, particularly, responsible business conduct (figure III.A.16).[44]

Public investment in infrastructure

Infrastructure stimulates economic growth and plays a key role in the SDGs, with positive spillovers across sectors. The Task Force provided analysis of how to undertake quality investment in infrastructure in its 2017 and 2018 reports.

Given the enormous infrastructure investment needs, public, private, domestic and international resources will be required. However, public and private sources of finance are not substitutable. Each has its own incentive structures, goals and mandates. Meeting infrastructure investment needs will require credible financing plans, which can be incorporated into INFFs. Raising public revenues and reallocating existing spending to infrastructure should be key elements of such plans, but may not be sufficient. For countries with moderate debt levels, additional borrowing might be possible, especially for projects that generate financial returns. Galvanizing private sector involvement is possible, but the associated fiscal costs and risks need to be carefully managed (see chapter III.B). [45]

Given financing constraints, countries will also need to deliver more infrastructure "bang" for their public investment "buck". More than a third of public investment spending is lost through inefficiency, with larger efficiency gaps in LDCs and other developing countries.[46] Stronger infrastructure governance can lead to higher output and efficiency of public investment while also deterring corrupt behaviour, which poses great risks, particularly for large projects. Improving infrastructure governance could close more than half of the observed efficiency gap. Better public infrastructure governance can also help Member States attract more private financing for infrastructure, if they desire to pursue blended finance options (see chapter III.C). The IMF Public Investment Management Assessment (PIMA) tool helps countries strengthen key infrastructure governance institutions (figure III.A.17). The tool offers a comprehensive framework that helps evaluate Governments' procedures and processes used to provide infrastructure to the public.

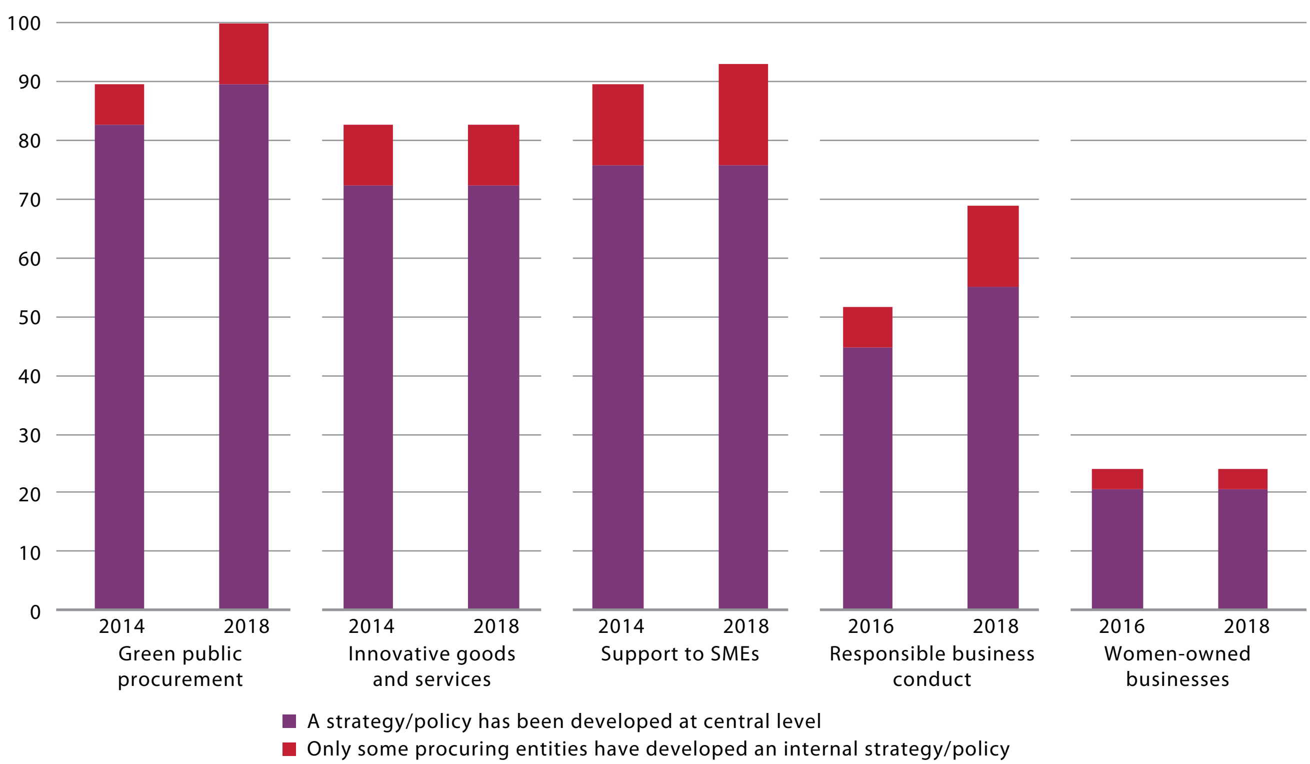
Procurement resilience

Rising economic losses due to disasters and the subsequent cost of recovery and reconstruction can deplete public financing for SDG investment. To protect public investments and strengthen stability, disaster risk considerations should be systematically embedded into domestic public financing, including expenditure and strategic procurement planning. In most countries, expenditure for disaster risk reduction in public budgets is marginal and inconsistent. Domestic public finance, including dedicated budget lines for disaster risk reduction within sectoral budgets, along with disaster-risk-informed public procurement, can be an effective entry point for mainstreaming disaster risk reduction across public investment.

Several countries have developed hazard maps, risk assessments and risk profiles at national, subnational and local levels which can ensure a context-specific, disaster-risk-informed approach to public expenditure and procurement. With risk-sensitive budget reviews, countries can identify gaps in public budgetary allocation for disaster risk reduction across sectors. Some countries have established national funds for disaster risk reduction and prevention. These provide a mechanism for Governments to co-finance investments in risk reduction with the private sector at national and local levels. Others have applied disaster risk screening tools to integrate risk reduction in public investment planning, expenditure and procurement. However, no single instrument is optimal for all risk scenarios. Disaster risk reduction financing strategies require a risk-layered approach. In the extensive risk layer (high probability and low expected loss), investment for risk reduction and prevention is the most cost-efficient. In the intensive risk layer (low probability and high expected loss), risk reduction is often financially prohibitive, especially in LDCs and SIDS. Where risk must be retained, risk transfer schemes, such as insurance, and catastrophe bonds can be more cost-efficient (see chapter III.C). However, it is critical to integrate measures to incentivize risk reduction across these tools.

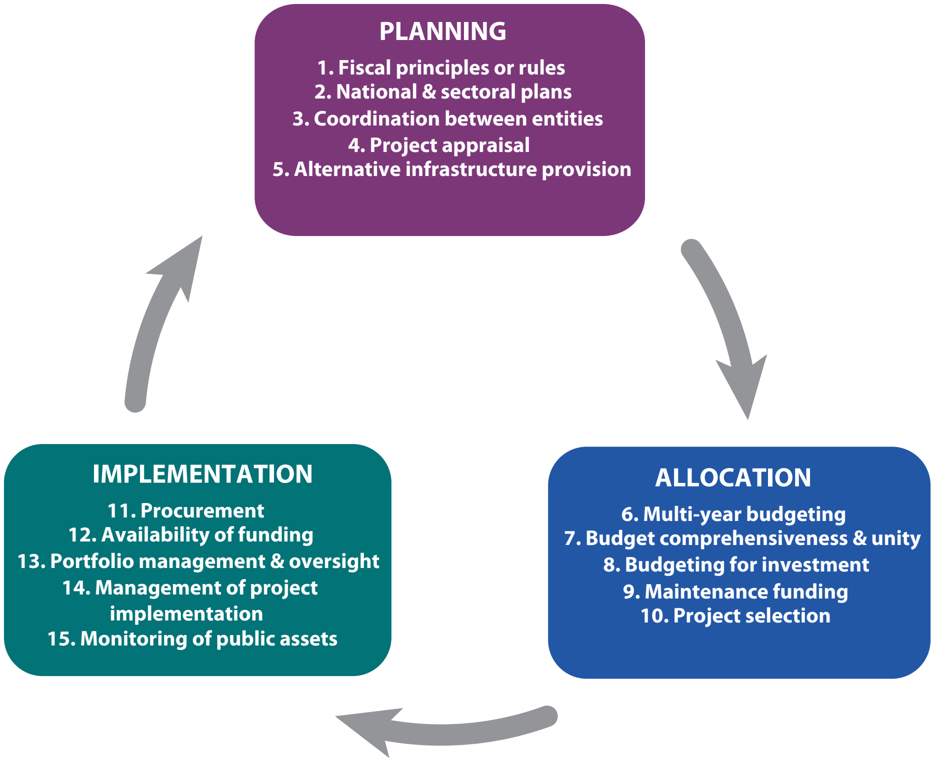
Disaster risk reduction financing strategies should be aligned with the objectives of national disaster risk reduction strategies and incorporated into broader planning processes, such as through an INFF. Their implementation should be enabled by clearly defined, comprehensive disaster risk reduction legal and regulatory frameworks. Technical assistance is available from international partners for countries that need to build the capacity for developing such strategies and regulatory frameworks. These

Figure III.A.16
Existence of a strategy/policy to pursue secondary policy objectives in public procurement, 2014 and 2018
(Percentage of countries surveyed)



Source: OECD.
Note: Based on data from 29 countries that answered both the 2018 and one of the 2016/2014 surveys on public procurement.

Figure III.A.17
Overview of the Public Investment Management Assessment framework



Source: IMF.

issues need to be better mainstreamed into all the assistance provided by multilateral institutions.

Incorporating gender equality

Gender responsive budgeting (GRB) enables Governments to plan and budget for efforts to support achievement of gender equality objectives. Although progress has been made in implementing GRB globally, significant gaps remain. SDG Indicator 5.c.1, the international standard for GRB, assesses government efforts to put in place gender-focused policies, gender-responsive public finance management systems and budget transparency. An analysis of 69 countries and areas reporting on Indicator 5.c.1 in 2018 found that 19 per cent fully met those criteria and 59 per cent approached the requirements. The data also revealed a gap in policy implementation. Among the same set of countries, 90 per cent had policies and programmes in place to address gender gaps, but only 43 per cent reported adequate resource allocations to implement them.

Countries implementing GRB have been more likely to issue directives and/or guidelines and use sex-disaggregated data to inform budgeting. Actions that link resource allocations with assessment of outcomes and impact are less common but essential. Fewer countries are conducting ex ante gender impact assessments, producing gender budget statements and/or gender audits of the budget. When conducted, they can provide insight into the contributions of gender policies and the expenditures for their implementation to meaningful outputs and outcomes. Audits can enable Governments to make corrections/changes in the next budget cycle to improve the achievement of intended gender equality results.

Deliberate integration of gender assessments into policy formulation is possible. Countries with the most advanced GRB practice are effectively mainstreaming gender in each step of their budget planning, execution and reporting processes and working across all sectors. When done well, these actions produce data and learning to inform strategic decisions in the next cycle and increase transparency of gender budget information to strengthen government accountability.

Alignment of overall budgets is not the only way to advance gender equality through public expenditure. Some developed countries use public procurement to encourage government contracting with women-owned/led small businesses.[47] Indeed, corporations in certain developed economies, such as the United States of America, have designed policies that actively seek out women-owned businesses and other diverse suppliers as part of their overall business strategies.[48] As discussed in chapter III.B, women-owned/led businesses face constraints in access to capital, human resources, and even an inequitable legal environment. Government procurement policies can focus on removing barriers and developing the capacity of these suppliers to compete with other businesses.

Tools for procurement performance evaluation

A new tool to track the performance of public procurement systems is the 2019 revision to the Methodology for Assessing Procurement Systems

(MAPS). MAPS was originally created by a joint initiative of the World Bank and the OECD Development Assistance Committee, and was revised to make it more universal and to support countries in implementing public procurement systems aligned with the SDGs. It helps countries to conduct assessments of their procurement system in order to determine their performance across 14 indicators in four clusters. Integrity is one of the areas that features prominently in the MAPS, reflecting its importance for a well-functioning public procurement system.

5.3 Transparency and accountability in public finance

Accountable public financial management institutions and systems play a crucial role in implementation of national policies for sustainable development and poverty reduction. The establishment of new national social contracts will be enhanced with transparency and accountability of budgets and more effective service delivery. While there are no universal tools for benchmarking transparency and accountability of budget processes, many developing countries make use of the Public Expenditure and Financial Accountability (PEFA) framework.[49] PEFA assessments conducted between 2006 and 2016 (by an average of 27 countries per year) show an upward trend in aggregate PEFA scores over time. Nevertheless, the overall trend in year-on-year performance has been relatively slow moving and well below "good practice" scores. Over time, the external scrutiny and audit pillar has consistently had the worst average performance, while the cross- cutting comprehensiveness and transparency pillar has had the best performance.

Endnotes

1 Data is based on revenues excluding social insurance contributions.

2 2018 data includes fewer observations than 2017, so changes in the median may be only a statistical artifact.

3 OECD, Revenue Statistics 2019 (Paris, OECD, 05 December 2019). Available at https://doi.org/10.1787/0bbc27da-en.

4 ESCWA, "The Arab Financing for Development Scorecard: Domestic public resources", E/ESCWA/C.9/2019/6(Part I), 19 September 2019. Available at https://www.unescwa.org/sites/www.unescwa.org/files/events/files/1901005.pdf. .

5 World Bank, "Platform for Collaboration on Tax: PCT Progress Report 2018-2019 (English)" (Washington, D.C., World Bank Group, 2019). Available at http://documents.worldbank.org/curated/en/702411559936259607/Platform-for-Collaboration-on-Tax-PCT-Progress-Report-2018-2019.

6 See Tax Administration Diagnostic Assessment Tool, "Overview." Available at https://www.tadat.org/overview.

7 Anna Kochanova, Zahid Hasnain, and Bradley Larson, "Does E-Government Improve Government Capacity? Evidence from Tax Compliance Costs, Tax Revenue, and Public Procurement Competitiveness", The World Bank Economic Review, vol. 34, Issue 1 (30 May 2018), pp. 101-120.

8 OECD, "Introducing a Commercial off-the-Shelf Software Solution" (Paris, OECD, 2019). Available at http://www.oecd.org/tax/forum-on-tax-administration/publications-and-products/introducing-a-commercial-off-the-shelf-software-solution.pdf.

9 OECD, "Implementing Online Cash Registers: Benefits, Considerations and Guidance" (Paris, OECD, 2019). Available at http://www.oecd.org/tax/forum-on-tax-administration/publications-and-products/implementing-online-cash-registers-benefits-considerations-and-guidance.pdf.

10 OECD, The Sharing and Gig Economy: Effective Taxation of Platform Sellers: Forum on Tax Administration (Paris, OECD, 2019). Available at https://doi.org/10.1787/574b61f8-en.

11 Lee, Daniel Jeong-Dae, "Cheating the Government: Does Taxpayer Perception Matter?", (Bangkok, UN ESCAP); Fredrik Matias Sjoberg and others, "Voice and Punishment: A Global Survey Experiment on Tax Morale", Policy Research Working Paper (Washington, D.C., World Bank Group, 15 May 2019). Available at http://documents.worldbank.org/curated/en/986411557941098413/Voice-and-Punishment-A-Global-Survey-Experiment-on-Tax-Morale.

12 Wilson Prichard and others, "Innovations in Tax Compliance: Conceptual Framework", Policy Research Working Paper (Washington, D.C., World Bank Group, October 1, 2019). Available at http://documents.worldbank.org/curated/en/816431569957130111/Innovations-in-Tax-Compliance-Conceptual-Framework.

13 S.M. Ali Abbas and Alexander Klemm, "A Partial Race to the Bottom: Corporate Tax Developments in Emerging and Developing Economies", International Tax and Public Finance, vol. 20, Issue 4 (2013), pp. 596-617; Pieter Buyl and Annelies Roggeman, "Do SMEs Face a Higher Tax Burden? Evidence from Belgian Tax Return Data", Prague Economic Papers, vol. 2019, Issue 6 (2019), pp. 729-747; Francisco J. Delgado, Elena Fernández-Rodríguez and Antonio Martínez-Arias, "Corporation Effective Tax Rates and Company Size: Evidence from Germany," Economic Research-Ekonomska Istraživanja, vol. 31, Issue 1 (2018), pp. 2081-2099. Available at https://doi.org/10.1080/1331677X.2018.1543056.

14 OECD, "Corporate Tax Statistics: First Edition" (Paris, OECD, 2019). Available at http://www.oecd.org/tax/tax-policy/corporate-tax-statistics-database-first-edition.pdf.

15 Niels Johannesen, Thomas Tørsløv and Ludvig Wier, "Are Less Developed Countries More Exposed to Multinational Tax Avoidance? Method and Evidence from Micro-Data", The World Bank Economic Review (forthcoming) (24 October 2019). Available at https://doi.org/10.1093/wber/lhz002.

16 IRS, "Internal Revenue Service Data Book 2018" (Washington, D.C., IRS, May 2019).

17 Niels Johannesen, Thomas Tørsløv and Ludvig Wier, "Are Less Developed Countries More Exposed to Multinational Tax Avoidance? Method and Evidence from Micro-Data".

18 OECD, "Transparency and Exchange of Information for Tax Purposes: Multilateral Co-Operation Changing the World, 10th Anniversary Report" (Paris, OECD, 24 November 2019). Available at https://www.oecd.org/tax/transparency/global-forum-10-years-report.pdf.

19 OECD, "Transparency and Exchange of Information for Tax Purposes: Multilateral Co-Operation Changing the World, 10th Anniversary Report".

20 OECD, "Secretariat Proposal for a 'Unified Approach' under Pillar One", Public consultation document (Paris, OECD, 2019). Available at https://www.oecd.org/tax/beps/public-consultation-document-secretariat-proposal-unified-approach-pillar-one.pdf.

21 World Bank, "Platform for Collaboration on Tax: PCT Progress Report 2018-2019 (English)".

22 Safe harbours typically are aimed at increasing tax certainty, and thus reduce the ability of tax authorities to challenge and audit the taxpayer that has adopted into the generally less complex safe harbour rules.

23 OECD, "Statement by the OECD/G20 Inclusive Framework on BEPS on the Two-Pillar Approach to Address the Tax Challenges Arising from the Digitalisation of the Economy" (Paris, OECD, 2020). Available at https://www.oecd.org/tax/beps/statement-by-the-oecd-g20-inclusive-framework-on-beps-january-2020.pdf.

24 OECD, "Webcast: Update on Economic Analysis and Impact Assessment". Available at https://www.oecd.org/tax/beps/webcast-economic-analysis-impact-assessment-february-2020.htm.

25 See Box 3, Chapter III.A of Financing for Development: Progress and Prospects 2017, pp. 41.

26 Academics have continued to develop methodologies to estimate IFFs at the national level, see Gilles Carbonnier and Rahul Mehrotra, "Abnormal Pricing in International Commodity Trade: Empirical Evidence from Switzerland", Discussion Paper No. R4D-IFF-WP01-2019 (January 2019); Cyril Chalendard, Gaël Raballand and Antsa Rakotoarisoa, "The use of detailed statistical data in customs reforms: The case of Madagascar", Development Policy Review, vol. 37, Issue 4 (14 November 2017), pp.546-563; World Customs Organization, "Illicit Financial Flows via Trade Mis-invoicing Study Report 2018" (Brussels, World Customs Organization, 2018). Available at http://www.wcoomd.org/-/media/wco/public/global/pdf/media/newsroom/reports/2018/wco-study-report-on-iffs_tm.pdf?la=en.

27 Pierce O'Reilly, Kevin Parra Ramirez, and Michael A. Stemmer, "Exchange of Information and Bank Deposits in International Financial Centres," OECD Taxation Working Papers No. 46 (Paris, OECD, 28 November 2019). Available at https://www.oecd-ilibrary.org/content/paper/025bfebe-en.

28 See for example the OECD Money Laundering and Terrorist Financing Awareness Handbook for Tax Examiners and Tax Auditors; and the joint OECD-WB publication on Improving Co-operation between Tax Authorities and Anti-Corruption Authorities in Combating Tax Crime and Corruption.

29 World Bank, World Development Report 2017: Governance and the Law (Washington, D.C., World Bank Group, 2017).

30 IMF, Fiscal Monitor: Curbing Corruption, (Washington, D.C., IMF, April 2019). Available at https://www.imf.org/en/Publications/FM/Issues/2019/03/18/fiscal-monitor-april-2019.

31 Alexandra Leitão, "Corruption and the Environmental Kuznets Curve: Empirical Evidence for Sulfur", Ecological Economics, vol. 69, Issue 11 (15 September 2010), pp. 2191–2201. Available at https://doi.org/10.1016/j.ecolecon.2010.06.004.

32 IMF, Fiscal Monitor: Curbing Corruption.

33 Michael Johnston, Syndromes of Corruption: Wealth, Power, and Democracy (Cambridge University Press, 2005).

34 World Bank, World Development Report 2017: Governance and the Law.

35 See Conference of the States Parties to the United Nations Convention against Corruption, "Set of non-binding recommendations and conclusions based on lessons learned regarding the implementation of chapters III and IV of the United Nations Convention against Corruption: Note by the Secretariat" (United Nations publication, CAC/COSP/2019/3, 17 September 2019).

36 United Nations, World Public Sector Report 2019 (United Nations publication, Sales no.: E.19.II.H.1). Available at https://publicadministration.un.org/en/Research/World-Public-Sector-Reports.

37 IMF, Fiscal Monitor: Managing Public Wealth (Washington, D.C., IMF, October 2018). Available at https://www.imf.org/en/Publications/FM/Issues/2018/10/04/fiscal-monitor-october-2018.

38 IMF, "Public Sector Balance Sheet (PSBS)" (2019). Available at https://data.imf.org/?sk=82A91796-0326-4629-9E1D-C7F8422B8BE6.

39 Ibid.

40 United Nations, World Public Sector Report 2019.

41 Financing for Development: Progress and Prospects 2018, Report of the Inter-agency Task Force on Financing for Development (United Nations publication, Sales no. E.18.I.5). Available at http://digitallibrary.un.org/record/3801757.

42 Financing for Development: Progress and Prospects, Report of the Inter-agency Task Force on Financing for Development 2017 (United Nations publication, Sales no. E.17.I.5). Available at http://digitallibrary.un.org/record/3801760.

43 OECD, Government at a Glance 2019 (Paris, OECD, 2019). Available at https://doi.org/10.1787/8ccf5c38-en.

44 Ibid.; OECD, Reforming Public Procurement: Progress in Implementing the 2015 OECD Recommendation, OECD Public Governance Reviews (Paris, OECD, 2019).

45 Gaspar, V., Amaglobeli, M. D., Garcia-Escribano, M. M., Prady, D., & Soto, M. (2019). Fiscal policy and development: human, social, and physical investments for the SDGs. International Monetary Fund.

46 IMF, chapter 3 (forthcoming; Washington, D.C., IMF).

47 Sergio Fernandez, Deanna Malatesta, and Craig R. Smith, "Race, Gender, and Government Contracting: Different Explanations or New Prospects for Theory?", Public Administration Review, vol. 73, Issue 1 (18 December 2012), pp. 109-120. Available at https://doi.org/10.1111/j.1540-6210.2012.02684.x.

48 Keric Chin, The Power of Procurement: How to Source from Women-Owned Businesses (New York, UN Women, 2017). Available at https://www.unwomen.org/digital-library/publications/2017/3/the-power-of-procurement.

49 PEFA was initiated in 2001 by The European Commission, the IMF, World Bank, and the governments of France, Norway, Switzerland, and the United Kingdom.