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Evaluation of Revenue Projects Synthesis Report Volume I

by

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The former Overseas Development Administration (ODA) became the Department for International Development (DFID) in May 1997. Although for convenience the acronym DFID has been used throughout the study, it should be remembered that some of the events, actions, etc. covered occurred within the period of ODA's existence.

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PREFACE

Each year the Department for International Development (DFID) commissions a number of independent evaluation studies. The purpose of DFID's evaluation programme is to examine rigorously the implementation and impact of selected projects and to learn lessons from them so that these can be applied to current and future projects and programmes. It should be borne in mind that the projects examined were the products of their time, and that the policies they reflected and procedures they followed may, in many cases, have changed in the light of DFID's developing knowledge.

The Evaluation Department (EvD) of DFID is independent of DFID's spending divisions and reports directly to DFID's Principal Finance Officer. This report represents the views of the consultants who carried out the review, and were drawn from Emerging Market Economics Ltd, in association with Consulting Africa, the University of Birmingham, and the MA Consulting Group. Members of country teams are identified in the country reports.

This is a synthesis of evaluations of revenue-related projects supported by DFID and its predecessor, the Overseas Development Administration (ODA). Its main aim is to improve the effectiveness of support for the development of the revenue function in partner countries, by identifying and disseminating good practice in the design, implementation, monitoring and evaluating of revenue projects. The 1997 White Paper, "Eliminating World Poverty: A Challenge for the 21st Century" requires DFID's activities to be justified by their contribution to the reduction of poverty, and therefore the impact of revenue support on poverty reduction was examined.

The synthesis follows the preparation, as Phase I of the study, of an inception report that set out a detailed evaluation methodology, including a review of relevant literature and, after consultation with DFID, the identification of four DFID projects as case studies and desk reviews and, during Phase II, completion of the following activities:

- An initial desk study of relevant literature.
- Preparations of desk reviews of the following projects:

1. The Ghana Reintroduction of VAT Project
2. The Uganda Revenue Authority Project
3. The Zambia Revenue Authority Consolidation Project
4. The Pakistan General Sales Tax Strengthening Project

- Field visits to the projects in Ghana, Uganda and Zambia.
- Preparation of draft reports on the projects, which were circulated for comment to individuals and organisations who were closely involved.

In Phase III the draft synthesis report was prepared, drawing upon the results of the country case studies and the results of a 1997 review of the institutional aspects of revenue administration projects in Africa. The draft was then discussed at a workshop on taxation and poverty held in Nairobi in June 2000, and attended by representatives of interested governments and donor organisations.

Drafts of the complete Evaluation of DFID-Supported Revenue Projects, including the synthesis as Volume I and the country studies as a supporting Volume II, were submitted to DFID's Principal Finance Officer to note the main conclusions and lessons learned, and presented for discussion at DFID's Portfolio Review Committee in December 2000, by Evaluation Department and the Lead Author.

This process is designed to ensure the production of high quality reports and evaluation summaries (EVSUMs), which highlight the major lessons learned.

The evaluation was managed by Éamon Cassidy, Fiona Shera and Paul Balogun, and edited for printing by Bernard Jordan and Jennifer Gibb.

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ABBREVIATIONS AND ACRONYMS

ASYCUDA	Automated System for Customs Data
BHC	British High Commission
CBR	Central Board of Revenue
CSO	Civil Society Organisation
DFID	Department for International Development
DT	Direct Tax (or Taxation)
EvD	Evaluation Department (DFID)
GDP	Gross Domestic Product
GID	Government and Institutions Department (DFID)
GoG	Government of the Republic of Ghana
GoZ	Government of Zambia
GRVAT	Ghana Reintroduction of VAT Project
GST	General Sales Tax
GUTA	Ghana Union of Traders' Associations
IMF	International Monetary Fund
Kw.	Kwaca (Zambian currency)
LTD	Large Tax Payer Department
LTU	Large Tax Payer Unit
NGO	Non-governmental Organisation
ODA	Overseas Development Administration
OPR	Output to Purpose Review
OVI	Objectively Verifiable Indicator
PCR	Project Completion Report
PT	Presumptive Income Tax
STW	Sales Tax Wing
TCO	Technical Co-operation Officer
TIN	Tax-payer Identification Number
TPU	Tax Policy Unit
UMA	Uganda Manufacturers Association
URA	Uganda Revenue Authority
VAT	Value Added Tax
VIPS	Computer software for VAT management (developed by the Crown Agents)
ZRA	Zambia Revenue Authority
ZRACP	Zambia Revenue Authority Consolidation Project

GLOSSARY OF TAXATION TERMINOLOGY

ASYCUDA	A software system used for Customs administration.
Avoidance	The reduction in liability for a tax by a tax-payer through legally acceptable mechanisms.
Benefit taxation	The raising of taxes on the direct beneficiaries of government expenditures.
Buoyancy	A buoyant tax instrument (or system) is one for which the tax yield/GDP ratio is constant or rises with GDP.
Compliance costs	Costs (other than the tax payment itself) incurred by the tax-payer in complying with the requirements of tax legislation.
Evasion	The use of illegal means to avoid a tax liability.
FASTs	Flexible Anti-Smuggling Teams.
Incidence	The study of tax burdens.
Neutral	A neutral tax instrument (or system) is one which does not introduce distortions in the behaviour and decisions of economic agents.
Presumptive Tax	A method of taxation which determines the level of income and sales which may be imputed to a particular category of tax-payer and imposes a tax on that basis. Used primarily for difficult-to-tax areas of the economy.
Progressivity	A tax is progressive if the burden of the tax forms a higher proportion of the income of rich individuals than of poor individuals.
Regressivity	A tax is regressive if the burden of the tax forms a lower proportion of the income of rich individuals than of poor individuals.
Shifting	The movement of tax burdens as a result of changes in relative prices induced by a tax. A tax is forward-shifted if it is passed on to consumers of the taxed good or service through output price increases. A tax is backward-shifted if it is passed back to factor supplies in reduced factor prices.
Tax burden	The economic loss incurred by those who bear the weight of a tax (they may not be the people on whom the tax is imposed).
Tax expenditure	Concessions or exemptions from a "normal" tax structure that reduce government collection and, because the government policy objectives could be achieved through a subsidy or other direct outlays, are regarded as equivalent to budget expenditure.

SUMMARY

The main finding of this synthesis is that where the policy and institutional contexts are favourable, the support of a project can help revenue authorities to rapidly and substantially increase revenue collection. This occurred in Uganda in the early 1990s. To date, the major impact on poverty of the projects that have been evaluated is probably in aiding macroeconomic stabilisation and therefore addressing constraints on long-term economic growth. Linkages between increased revenue collection and increased pro-poor expenditure were not found, and would necessitate significant improvement in governments' budgetary systems.

BACKGROUND

S.1 Since 1992, the Department for International Development (DFID) has supported over 40 projects to strengthen the administration and collection of revenue. This synthesis report presents the main findings, conclusions and lessons from an evaluation of DFID's support to revenue collection authorities during the 1990s. The supporting evaluation was undertaken over a 15-month period during 1999 and 2000. It included a review of relevant literature, desk studies and country visits to projects in three countries – Zambia, Ghana and Uganda – and a desk study of a revenue project in Pakistan. These activities were followed by a workshop that included participants from the African organisations involved, at which the preliminary conclusions were discussed.

MAIN FINDINGS

THE EFFICIENCY AND EFFECTIVENESS OF THE PROJECTS

S.2 The projects evaluated were successful at a technical level. Through a wide range of specific interventions in management systems, human resource development and organisational changes, all four projects have increased the **capacity** of the respective revenue agencies to collect revenue. The quality of technical assistance provided has been generally high. DFID is respected as a leading provider of support to revenue administration. In general, the management teams of both the projects and DFID have shown the ability to respond effectively to external events and to flaws in initial designs and appraisals to ensure the efficiency and effectiveness of the projects as capacity-building interventions (Chapter 2).[1]

S.3 The projects in Zambia, Uganda and Pakistan aimed to increase national revenue/Gross Domestic Product (GDP) ratios during the lifetime of the projects, while the Ghana project aimed at neutrality in collection. Clear evidence of both strong positive effects on revenue and of no apparent response was found (Paragraph 24).

[1] Cross-references are to relevant sections, sub-sections or paragraphs in the Main Report.

S.4 In Uganda, it is reasonable to link the initial support of the project with a period of strong revenue growth. The revenue/GDP ratio rose from 5.7 per cent to 11 per cent during the Uganda Revenue Authority (URA) consolidation period, when DFID provided the authority with strong line management and systems support. However, since DFID's support was scaled down in the mid-1990s, in response to perceived problems of governance in the revenue authority, the revenue/GDP ratio has stagnated. In Zambia, the major impact of the project has been to allow the Zambia Revenue Authority (ZRA) to maintain the revenue/GDP ratio, despite the poor macroeconomic situation. In neither Ghana nor Pakistan has increased capacity been translated into increased revenue. In Ghana, the project was confined to supporting the VAT Service, and strong performance in VAT collection has helped to offset a reduction in the overall revenue/GDP ratio stemming from poor performance of other instruments during a period of macroeconomic stagnation (paragraphs 19–23).

S.5 While evidence shows that stand-alone revenue projects can have immediate effects upon the revenue collected, these depend on a supportive policy and institutional environment. In most countries, these conditions either did not exist or were temporary. It is clearly difficult and risky to decide whether revenue projects are justified under such circumstances, and whether support should be maintained during periods of adverse policy or poor government commitment to implementing agreed changes (ibid.).

S.6 The scope for longer-term effects is clearly tied to attention to a range of organisational issues within the revenue authorities as well as more contextual policy and institutional issues. This was clearly the case in Africa, where recently created revenue authorities, semi-independent of central government, were themselves created as a response to the perceived difficulties of reforming revenue organisations that were still firmly embedded within the civil service. However, the initial benefits achieved from the establishment of independent revenue authorities, with improved terms and conditions, tend to be eroded over time, as the disparities and anomalies that arise relative to the wider civil service create opposition (ibid.).

THE IMPACT OF THE PROJECTS

S.7 All the projects evaluated were designed before the publication of the 1997 DFID White Paper, which established the elimination of poverty as DFID's single overarching aim. This is reflected in, by present day standards, insufficient appraisal of the robustness of the linkages between enhanced revenue collection and positive impacts on poverty. In practice, projects were designed to support the implementation of the tax reform agenda advocated by the International Monetary Fund (IMF) and the World Bank. This includes the progressive reduction in trade taxes, broadening of the tax base, the adoption of broad systems of indirect taxation with relatively low and uniform rates, and a reduction in direct taxation rates to international norms (Chapter 5.1).

S.8 Support for the administration and collection of revenue can have an impact on poverty in three main ways:

- the decision on who pays what taxes (the characteristics of tax incidence of the tax instruments selected).
- enhanced revenues that are then used by governments to maintain or enhance pro-poor expenditure.
- the impact of enhanced revenue on easing constraints on growth (Chapter 3.1).

Tax incidence

S.9 Projects assisted by DFID did not support regressive tax regimes or regressive new instruments. Rather, they supported the redesign of tax structures that reinforced moves towards a broader tax base, lower maximum rates, and a reduction in dependence on trade taxes. Support for implementing tax reform in both Ghana and Uganda has allowed governments to reduce trade taxes, where incidence fell mainly on low-income rural producers (of coffee in Uganda and cocoa in Ghana). The relatively benign incidence characteristics of the new indirect taxes observed in the three African countries reflect the strategy adopted by governments to gain political support for the development of the emerging indirect tax systems. These systems are characterised by widespread exemptions, with many low-income budget goods exempted or zero-rated for Value Added Tax (VAT). Whether this strategy can be sustained when governments face pressure to increase revenue, is questionable. The impact of support to the reform of systems of direct taxation has also been favourable except in Zambia, where non-adjustment in tax bands to reflect high inflation has meant that increasing numbers of the poor in formal employment now pay direct taxes. There is also a perception that the focus by revenue authorities on ensuring compliance by known tax-payers is encouraging businesses to either deregister or to remain in the informal sector. While minimising taxes, this inevitably constrains their potential for growth (paragraph 28).

Enhanced pro-poor expenditure

S.10 The link between incremental revenue and pro-poor current public expenditure is often cited as the main poverty-impact justification for DFID's support for revenue projects. The basic finding is that, at least within the typical project timeframe of two to three years, the relationship between increases in revenue collected and incremental pro-poor spending is weak or in some cases even non-existent. This reflects two sets of interrelated problems. First, persistent fiscal deficits and crises, the need to meet macroeconomic conditions set by the IMF, and cash budgeting systems in which fiscal shortfalls disproportionately affect development expenditure, are the major drivers of expenditure. Second, in the countries evaluated, weak budgetary planning and systems for management of expenditure further eroded the likelihood of revenue being linked to pro-poor expenditure (Chapter 3.3).

Reducing constraints on growth

S.11 This linkage is important in all three of the African economies reviewed, although in each case the finding is a matter of interpretation and judgement rather than of proof. In Uganda, the early achievements of the revenue authority in building up the revenue base from 5.7 per cent of GDP to 11 per cent constituted a major element in the successful macroeconomic stabilisation programme effected during the early 1990s. In Zambia, the effect of strong revenue performance has been to reduce the severity of the fiscal balances that would have emerged in the late 1990s without the project. In Ghana, the establishment of an efficient VAT service is a prerequisite for addressing and managing the core fiscal constraint, domestic debt (Chapter 3.4).

S.12 The impact that revenue can have on poverty by addressing the constraints on growth operates over a medium to long term, but its cumulative effect may be substantial. It raises an interesting and difficult trade-off between supporting activities and projects that give an immediate but restricted reduction in poverty and those that lay the foundations for more fundamental poverty reduction through policies based on growth (ibid.).

Do revenue projects fit into a poverty reduction strategy?

S.13 The short answer is yes they can. Evidence from this evaluation indicates that in the short term such projects can help countries to achieve the macroeconomic stabilisation considered crucial for economic normalisation and resumed growth. In the context of the recent Poverty Reduction Strategies supported by the IMF, the World Bank and most bilateral donors, an effectively functioning revenue administration is an essential part of an economy that is functioning successfully (Chapter 6.1.3).

S.14 In the longer term, revenue projects can also help recipient countries to create the capacity to address seriously the reduction of poverty by, for example, supporting the introduction of new broad based tax instruments (e.g. VAT in Ghana) or through improving the capabilities of the revenue authorities (all countries) (ibid.).

EMERGING ISSUES

S.15 Overall revenue performance (measured in terms of the revenue/GDP ratio) appears to have reached a plateau in Zambia, Uganda and Ghana at a level below that needed to achieve fiscal sustainability and the provision of an acceptable level of public service. This leads to continuing pressure for an increase in sustainable sources of revenue. Two areas are typically under review: extending the tax net to achieve more effective coverage of the informal sector, and moves to reduce the generous exemptions and zero-ratings usually provided for VAT. Significant moves in respect of either of these options are likely to create a tension between revenue performance and deterioration of tax incidence, and potentially to have an impact on poverty (Chapters 3.6.1, 3.6.2).

S.16 Overall IMF and ministry of finance negotiations usually determine the framework for tax policy, yet the government's ability to analyse tax policy was deficient in all the countries studied. In some cases this was because revenue authorities had been granted over-strong mandates in the development of tax policy. This is the case in Pakistan where the tax policy function resides in the Central Board of Revenue. Problems with the delineation of the roles of the Ministry of Finance and the revenue authority persist in Zambia, and were formerly a problem in Uganda. Poor formulation of tax policy is having a directly negative effect in Zambia through a failure to limit the impact of fiscal drag on the lowest income direct tax-payers. It is useful to differentiate between three levels of "tax policy analysis". First, the strategic level, which will continue to be determined by the ministry of finance in consultation with the IMF. Second, the tax instrument level, at which detailed tax settings are made in the context of the annual budget; this is the preserve of government and requires strengthening in several countries, especially in terms of making the budget more pro-poor. Third, tax collection analysis: the revenue authorities increasingly need to develop their analytical capability in order to plan cost-effective strategies for collection. There is scope for DFID support at the second and third levels, which would not interfere with the strategic fiscal advice provided by the IMF and could strengthen the focus on poverty of fiscal policy (Chapters 3.6.4 and 5.2).

S.17 None of the case study countries has yet articulated a coherent strategy for taxation of the informal sector, though efforts to improve tax-payer compliance for existing instruments is having some effect. Uganda is attempting to introduce a presumptive tax to extend the tax net on direct taxation through a simplified schedule with lower compliance costs and lower effective tax rates. The revenue authority has not yet wholly embraced this instrument. The elaboration of a coherent strategy for taxing the informal sector is an area where DFID might provide useful technical support in future (Chapter 3.6.2). As countries try to tackle the taxation of the informal sector more systematically it will be important to keep under review the possibility that there could be gender impacts (Chapter 3.5.1).

MAIN LESSONS LEARNED

For recipient governments (Paragraph 123)

S.18 Many of the findings and lessons of this evaluation are of interest principally to governments, as these face the challenge of continuing to increase revenue performance while pursuing increasingly pro-poor policies (paragraph 123). Sustained improvements in the effectiveness of revenue collection, and positive impacts on poverty, require governments to:

- provide a governance framework within which revenue authorities can perform effectively without continual compromise (S.6).

- respect the independence of the revenue authority and address the need to maintain incentives for staff within such service (ibid.).

- recognise the need for improved analysis of tax policy below the level of negotiations with the international financial institutions (S.16).

- address taxation of the informal sector and devise cost-effective strategies that meet the objective of sustained revenue growth but do not jeopardise poverty reduction objectives (S.17).

- recognise that weaknesses in budgetary and expenditure management systems will undermine the potential economic and political returns on investment in the revenue services (S.5).

For revenue authorities

S.19 Lessons for revenue authorities include (paragraph 124):

- the need to balance the use of scarce resources to maximise tax collection from existing known tax-payers and the use of resources to extend the tax base to include those who are currently evading tax. To date, authorities have focused excessively on the existing tax-payers to meet targets set by the IMF and ministries of finance. As a first step, they need to develop information systems that allow them to consider the cost-effectiveness of alternative options (S.9, 15 and 17).

- the need to work closely with government to develop equitable and cost-effective strategies for taxing the informal and agricultural sectors. To the extent that the debate on these topics hinges on tax collectibility, the revenue authorities should be involved in the review of options (ibid.).

- the need to upgrade direct tax information systems to the standards that now typically prevail for indirect tax instruments. This can only be achieved through accelerated computerisation.

For DFID

S.20 This report concludes that revenue projects do, indeed, have a place in DFID's portfolio. Lessons from the evaluation indicate several actions that DFID might consider while identifying, appraising and monitoring future projects which would increase the probability of their being effective and having positive impacts on poverty (paragraphs 125, 126).

S.21 DFID should distinguish clearly between the analysis that should be made during the development of country strategies and that which should be made during the identification, appraisal and implementation of specific projects. This is particularly important for the revenue projects, where impacts, especially on poverty, occur indirectly. For example, development of the country strategy is the appropriate opportunity for considering whether the positive economic and institutional environment, upon which revenue projects will depend if an impact on poverty is to be realised, actually exists. DFID's country programme teams should, while developing the country strategy:

- **consider whether revenue support projects are useful:** where expenditure management systems are poor, revenue projects may not be appropriate. In such circumstances, support should only be considered if the government is broadly heading towards implementing improved pro-poor budgetary management systems. For example, it is doubtful whether renewed support to revenue collection in Pakistan is warranted under present conditions (paragraph 126a).

- **focus on fiscal, not tax or expenditure, incidence:** look at the net incidence of revenue and the expected decisions that accompany the allocation of expenditure. Revenues are not normally hypothecated, so assessments of expenditure incidence will be likely only to judge the progressivity of expenditure in broad terms (paragraph 126b).

S.22 If the broader analysis suggests that support to the revenue function is appropriate, issues that should be considered would include:

- **maintaining the focus of revenue projects on strengthening the revenue function:** while the current and prospective poverty profile of government expenditure is important in determining the appropriateness of revenue interventions, revenue projects should not normally incorporate support to expenditure-related activities and outputs, which require a different set of skills. The current DFID practice of technically confining revenue projects to the revenue function should be maintained, rather than pursuing the option of expanding the remits of projects to address expenditure side issues (paragraph 126d).

- **being realistic in assessing government commitment to, and opportunity for, change:** assess the degree to which there is political support within both government and the civil service for the important institutional changes required. In Africa, where donors are supporting the introduction of the semi-autonomous revenue authority model, it is clear that there are limits on the extent to which governments are willing, or able, to implement aspects of the model. In this context, evidence suggests that project conditionalities have often been ineffectual (Chapter 4.3).

- **that any beneficial anti-corruption effect that a revenue project might have is likely to be short-lived:** while revenue projects can have an important impact in restricting corruption at the middle level within the revenue authority, such gains may be short-lived if they are not embedded in a government-wide set of activities that aim to eradicate corruption. The capacity for revenue projects to influence the wider corruption environment, by creating islands of good practice, is limited (paragraph 122).

- **if the introduction of new revenue instruments is being considered, assess the degree of broad political support** (ibid.).

- **build tax policy into projects where appropriate:** the commitment by the IMF to tie concessional lending to support for a poverty-reduction strategy provides a context in many potential recipient countries for provision of technical and capability-building support to tax policy. This will normally be to the ministry of finance, the proper guardian of tax policy. Such support could be delivered either as a component of a larger tax administration project or as a stand-alone tax policy project (paragraph 126c).

- **consider extending project support to pro-poor civil society organisations (CSO) and other organisations to influence the budgetary process:** there is clearly a role for other stakeholders, such as business organisations, pro-poor non-governmental organisations (NGOs) and other CSOs, etc. in a more democratised budgetary process. The evaluation case studies have revealed a range of practices in terms of openness of the budget to lobbying and pressure groups. There is a discrepancy between the level of organisation and effectiveness of the industrial and commercial lobby groups on the one hand and pro-poor organisations on the other. DFID could support the strengthening of analytical and representational capacity in some of the latter as a way of giving the poor a voice in the budget, for example, through small grants or matching grants to civil society organisations (paragraph 126e).

1. INTRODUCTION

1.1 BACKGROUND

1. The Department for International Development's (DFID) Evaluation of Revenue Projects aims to provide a broad and comprehensive review of DFID's experience in support of revenue collection. Since 1992 some 40 of such projects have been supported. Expenditure has been concentrated on ten projects in Africa. The objectives of the evaluation are to assess the appropriateness, efficiency and effectiveness of DFID's support to the achievement of wider economic and social goals in the partner countries, and to identify good practice in the design, implementation and monitoring and evaluation of revenue projects. The focus of the evaluation, as agreed in the Inception Report, was to assess how well DFID's support for the revenue function fitted into the wider portfolio in the context of DFID's strong orientation towards poverty reduction, as set out in the 1997 White Paper. The present evaluation follows a study of DFID revenue administration projects undertaken in 1997/98 by the University of Birmingham (University of Birmingham, 1998), which concentrated on institutional aspects of ongoing revenue projects in Africa (paragraph 80).

2. The Terms of Reference for the evaluation are set out in Annex A.

1.2 APPROACH TO THE STUDY

3. The evaluation has been approached in three phases: under Phase I the consultants prepared an inception report which elaborated the evaluation methodology and proposed case study work in three countries – Ghana, Zambia and Pakistan. In the event fieldwork in Pakistan was not possible, because of the military coup in October 1999 and the subsequent freezing of DFID's assistance to that country. It was decided to add a case study for Uganda, and to limit work on Pakistan to a review of the project files and discussions with DFID and the project staff available in the UK.

4. In Phase II of the study, which ran between September 1999 and March 2000, field visits were made to the three case study projects. Histories and reports on the four selected projects were prepared and circulated for comments. The reports for all four countries are to be found in Volume II of this report.

5. Under Phase III, this Synthesis Report brought together the findings from the case studies and reviews of the implications of the findings for DFID's current and future support for the revenue function. A workshop on taxation and poverty was held in June 2000 in Nairobi to discuss the preliminary findings of the evaluation. Representatives from the case study governments and projects, DFID staff and other donors attended the workshop. A draft of this Synthesis Report was tabled at the workshop.

1.3 THE EVALUATION AND THE PROJECT LOGICAL FRAMEWORKS

6. It needs to be emphasised that the terms of reference for the evaluation are broader in scope than the projects that were evaluated in that they raise issues that typically fall outside the logical frameworks for the selected projects. These logical frameworks usually concentrate on goals, purposes and outputs that are tied closely to the improvement of revenue collection and the development of institutional capacity for revenue collection.

1.4 LAYOUT OF THE REPORT

7. This report is organised as follows: Chapter 2 includes reviews of the overall findings for the four case studies and an assessment of their achievement of the purposes and goals set out in the logical framework for each project. Chapter 3 reviews the findings on the central issue of the impact of revenue projects on poverty, concentrating on three principal economic mechanisms identified in the evaluation methodology. Chapter 4 examines institutional development in the organisations supported by DFID's revenue projects. Chapter 5 reviews issues relating to project appraisal and country strategy. Chapter 6 summarises the conclusions drawn from the evaluation and their implications for DFID's future support to the revenue function.

2. FINDINGS IN THE CASE STUDIES

2.1 PROJECTS SELECTED

8. The selection of projects focused on obtaining a selection of the larger projects (which are mostly in Africa) that would provide a suitable basis for comparison. Four projects were selected for close study:

- The Ghana Reintroduction of Value Added Tax Project (GRVAT).
- The Pakistan General Sales Tax Strengthening Project.
- The Uganda Revenue Authority Project.
- The Zambia Revenue Authority Consolidation Project (ZRACP).

2.2 PROJECT RESULTS AT PURPOSE AND GOAL LEVEL

9. Annex B is a summary of the project design and principal findings of this evaluation in relation to the performance of these four projects at Purpose and Goal level.

2.2.1 THE GHANA REINTRODUCTION OF VALUE ADDED TAX PROJECT

10. In spite of an observed decline in the revenue/Gross Domestic Product (GDP) ratio in Ghana in recent years the evaluation team concludes that the project has been successful in achieving its goal: to improve the revenue-raising capacity of the Government of Ghana (GoG). The successful introduction of Value Added Tax (VAT) has expanded the tax base and provided the government with a buoyant tax instrument for future revenue collection. The potential to raise revenue in the future is further enhanced by the institutional capacity that has been created, the low rate of VAT, and the widespread exemptions that currently prevail.

11. The project has also achieved its purpose. During 1999 and 2000 the project supported the reintroduction of an effective and sustainable VAT system. The institution is well established, the legislative base is sound, the public have accepted the VAT, the core staff have been trained, a VIPS information system (computer software for VAT management) is fully functioning, and the enforcement base is now being strengthened. There remain, however, a number of weaknesses in the system, including inadequate provision in the budget, which does not allow sufficient funding for the operating expenses needed to strengthen enforcement. Also relations with the other revenue departments have not been sufficiently developed.

2.2.2 THE PAKISTAN GENERAL SALES TAX STRENGTHENING PROJECT

12. The project purpose was to increase the capacity of the Central Board of Revenue (CBR) to reform

and administer its tax collection system, and the project goal was to increase revenue collection at lower cost and through improved efficiency. The project's outputs related to developing and introducing new VAT-type systems and procedures within the Sales Tax Wing (STW) of the Board of Revenue as well as training staff and developing an understanding among tax-payers of the new system and their responsibilities within it. The primary justification for the project was that it would support the objectives of the International Monetary Fund (IMF) and the government to mobilise revenue in Pakistan.

13. To find out whether the project achieved its goal, it is useful to distinguish between the short and medium term. In the short term (during the first three years of the project) sales tax revenue as a share of GDP was stagnant and then fell. This decline can be attributed to external factors, such as the reduction in the rate of tax and a decline in the large scale manufacturing sector, and therefore does not reflect a deterioration in the capacity of the Board of Revenue to collect general sales tax revenue effectively. Moreover, in spite of the targets set for raising revenue during the first few years of the project, the nature of DFID's assistance meant that incremental revenue was unlikely to be realised in the short term as a result of the project. In the medium to long term, however, given the expansion of the tax base and the improved capacity of the Board of Revenue, revenue from the general sales tax is likely to increase. The evaluation team therefore concludes that the project goal is likely to be achieved in the medium to long term, but not within the timeframe envisaged at the beginning of the project.

14. When assessing the project's performance against its purpose, it appears to have performed fairly well. Administration of the sales tax has been significantly strengthened and the project has been central to achieving this. However, during Phases I and II the project failed to realise all the expected gains. For example, by the end of Phase I new processes and procedures were not fully in place, and improvements in tax-payer compliance during Phase II were limited. These shortfalls were attributed to the difficult environment in which the project was being implemented and the limited timeframe permitted. The conclusion was that the project had made a significant contribution to enhancing the capacity of the Revenue Board to administer the general sales tax and by doing so had partially achieved its purpose, as measured against the Objectively Verifiable Indicators (OVIs) set out in the logical framework.

2.2.3 THE UGANDA REVENUE AUTHORITY PROJECT

15. The support of DFID to the Uganda Revenue Authority (URA) has been both important and effective in building the authority as a sustainable entity for revenue collection. Initial efforts to establish basic administrative systems in the authority were successful. Subsequently, as a result of DFID's assistance, good progress has been made in creating a sound organisational structure, attracting and retaining staff and improving staff motivation, improving the quality of management, and developing a sound relationship between the Board and the Executive. However, the process of institutional capacity-building remains incomplete and further progress is required to develop information systems, improve corporate planning, and combat corruption.

2.2.4 THE ZAMBIA CONSOLIDATION OF REVENUE PROJECT

16. The project has been successful in raising revenue in the short term in spite of the observed fall in real revenue collection. Several important factors are currently depressing revenue collection, including negative macroeconomic growth, the effect of the past policy of liberal tax exemptions, the negative effect of a large stock of arrears in inflationary conditions, and illiquidity resulting from the near insolvency of the mining sector. When allowance is made for these factors the Zambia Revenue Authority (ZRA) is seen to be achieving a very high level of performance, and the project is achieving its goal.

17. The project has also largely achieved its purpose "to develop into an effective, efficient and well-managed organisation with Zambian top management". The inadequacies identified in a DFID report in 1997 (DFID, 1997a) have been effectively addressed and the project is successfully pursuing organisational and management improvements. Of the four senior management posts previously held by expatriates, Zambians have filled three, the one expatriate remaining in post being the Commissioner General.

2.2.5 SUMMARY OF FINDINGS

18. To summarise, the four case study projects have for the most part been effective in the achievement of objectives at Goal and Purpose level. As discussed later in this report, however, major problems with implementation have tended to reduce the overall cost-effectiveness of this type of project, taking into account the periods when projects were seriously malfunctioning as a result of shortcomings in design and management.

2.3 THE IMPACT ON REVENUE COLLECTION (SHORT TERM)

19. The case study projects all aimed to increase revenue collection during the project lifetime (with the exception of the Ghana Reintroduction of VAT Project, which aimed at neutrality in collection). Given the importance of increased revenue in driving the effects and impacts of the project on poverty, the evaluation team tried to assess each project's impact on revenue collection for both the short and the longer term.

20. Assessment of the effect of DFID's projects on revenue collection raises a number of methodological issues:

- DFID's projects typically constitute only a part of the increased revenue effort in the recipient countries, since its support is provided in a context of increased national effort to reorganise their revenue services. Attribution of specific impacts from DFID support is, in general, difficult.

- the projects generally adopted targets for revenue collection expressed in terms of the revenue/GDP ratio, which were expected to rise by a few points over the period of the project. This ratio is, however, sensitive to a wide range of other influences at macroeconomic level and from activity in the business sector. Any positive impact made by DFID may, therefore, be obscured by negative extraneous factors.

21. Box 1 illustrates the pitfalls in assessing the impact of a project on revenue collection based on recent experience in Zambia, in which revenue effort was offset by the negative effects of the declining macroeconomy and tight financial environment.

22. With these methodological caveats, there are clear instances in the case studies of strong positive effects on revenue, but also of an apparent lack of revenue response. The projects in both Uganda and Zambia went through periods of strong revenue growth that it is reasonable to link to DFID's projects. In Uganda, during the first phase of the project, the revenue/GDP ratio rose from 5.7 per cent to 11 per cent in the revenue authority's consolidation period, when DFID provided the authority with strong line management and systems support. When DFID's support was scaled down in the mid-1990s, however, in response to perceived problems of governance in the authority, it entered a period of revenue stagnation.

23. An alternative method of determining the impact of DFID activity on short-term revenue is to assess the impact of specific management, system or other improvements spearheaded by DFID projects. In this context the projects in both Zambia and Ghana provide evidence of specific short-term revenue-enhancing innovations.

24. The conclusion is that, where conditions are favourable, such as in Uganda in the early 1990s, DFID support can have a substantial effect on revenue collection even in the short term. However, such an impact is by no means assured. Where political commitment is lacking or collection efforts are undermined by internal corruption and problems with governance, DFID's efforts may be ineffective. In all cases it is difficult to measure the specific impact of a DFID project on short-term revenue, and only broad conclusions can be drawn.

Box 1: Assessment of project impact on short term revenue collection (ZRACP)

ZRA's impact on short term revenue collection, must be judged against a counterfactual situation, which should take into account at least the following factors:

- Economic contraction in 1998 (overall 2 per cent) but with much sharper contraction in manufacturing, including the mining sector, followed by a larger reduction in 1999.

- The specific effect of the collapse of the mining sector in 1998/99 – the crisis of non-payment in the industrial/commercial sector that is reflected both in industrial bankruptcies and in the increase in tax arrears in recent years.

- Low buoyancy: The buoyancy of revenue in relation to GDP is low in Zambia and depends critically on the sectoral breakdown of changes in GDP: the direct tax system shows only limited progressivity, and significant parts of the economy (the informal sector and much of agriculture) fall outside the tax system.

- Inflation: Consideration must be also given to the effect of inflation on tax revenue. While in principle inflation can be expected to increase real revenues as a result of bracket creep (real effective rates rising as tax-payers pass into higher unadjusted nominal tax brackets), there are strong reasons for expecting the effect of inflation on real tax revenues to be negative in Zambia: first, the tax system is only very modestly progressive in its nominal structure; second, there have been large arrears of tax outstanding throughout the period of project implementation which imply that the real value of tax collections falls as taxes are paid with a lag. With inflation of 25-30 per cent, total arrears of the order of Kw. 200 billion and delays in payment often stretching into years, this effect (the so-called "Olivera-Tanzi effect") is undoubtedly important in Zambia.

- Exemptions: Finally, during the period up to 1998 the GoZ continued to grant significant numbers of exemptions to corporations.

When allowance is made for these factors the ZRA is seen to have performed well in terms of maintaining the revenue ratio in unfavourable circumstances.

3. THE IMPACT OF REVENUE PROJECTS ON POVERTY

3.1 METHODOLOGY

25. The central issue addressed by the evaluation is the impact of DFID's revenue projects on poverty. The methodology adopted concentrated on three main hypotheses about the ways in which these revenue projects might impact on poverty:

(i) Tax Incidence: the impact on poverty through the direct and indirect incidence of the tax instruments supported.

(ii) Revenue–current expenditure linkages: successful projects could increase the resources at government's disposal, leading to enhanced or extended provision of poverty-reducing services through the government budget.

(iii) Revenue–growth linkages: a longer-term impact on poverty resulting from the effect of increased revenue on macroeconomic stabilisation and the rate of economic growth.

26. This chapter sets out the evaluation team's findings in respect of each of these three linkages.

3.2 TAX INCIDENCE

27. In assessing the impact of DFID project activity on tax incidence several aspects were taken into account:

- support from DFID for revenue collection is frequently given in the context of changes in the overall tax structure and, in particular, increased dependence on broad instruments of direct and indirect taxation that replace revenues formerly collected from trade taxes. In this context the relevant comparison is between the former and the new tax structures.

- assessment of the direct incidence of tax instruments must be based on the actual pattern of compliance. In all the case study countries there is a wide gap between the legal tax burden and the effective tax burden as a result of tax evasion and non-compliance by large segments of the legally taxable population. The scope and pattern of exemptions are also important.

- a DFID project frequently aims to improve tax administration, which can affect levels of tax compliance, and hence the pattern of effective tax incidence.

28. The evaluation team's overall finding is that **the effect of DFID revenue project activity on poverty derived from changes in direct tax incidence mechanisms has generally been benign** and (with one exception discussed below) the evaluation team did not encounter any DFID support for instruments that tended to increase the regressivity of the supported revenue structures. There were two important reasons for this conclusion. One is the tendency for current tax reform measures to reduce trade taxes, where incidence falls mainly on low-income rural producers (of coffee in Uganda and cocoa in Ghana). The other are the extensive exemptions (and in the case of VAT, zero-ratings) that have usually been applied to new indirect tax instruments to ensure political support for their introduction. These frequently have the effect of exempting a large part of the low-income consumption bundle, the informal sector and the agricultural sector. However, to the extent that revenue growth will not be sustainable without reducing the number of exemptions, we question whether such a benign tax structure can be maintained. (This issue is analysed in Section 3.6 below)

29. This broad conclusion is based on the following principal findings in relation to tax incidence in the case study projects.

30. *Zambia:* the Zambia Revenue Authority Consolidation Project is supporting the full range of tax instruments administered by the revenue authority. The success in raising the revenue/GDP ratio has facilitated the revenue system's shift away from dependence on trade taxes to a greater reliance on domestic taxation and especially VAT. The VAT is characterised by extensive exemptions and zero-ratings, which effectively put the rural population outside VAT's scope (with some exemptions discussed in the Zambia Case Study Report). Recent years have witnessed a substantial degree of erosion of the real value of the income tax brackets, because the government had chosen not to index the tax credit and tax brackets, so the penetration of the tax to households significantly below the poverty line has increased. The project has been active in supporting improved compliance of the business sector in the application of the Pay-As-You-Earn (PAYE) system and this too has had the effect of bringing poor families into the tax net.

31. *Uganda:* as in Zambia the overall incidence of the tax system is critically affected by the limitations on the effective scope of the main tax instruments, notably the exclusion of almost all agricultural activities and commodities from direct tax and VAT, and the effective exclusion of the informal sector, which occupies a large part of the economy. The strengthening of the tax instruments managed by the Uganda Revenue Authority has permitted a shift in the structure of taxation away from export-based taxation, even though trade taxes as a whole continue to have an important role. The improvement in compliance achieved on Customs has permitted a significant reduction in external tariffs without a reduction in the absolute level of revenue.

32. There is a widespread perception, especially in the business community, that the Uganda Revenue Authority has concentrated unduly on known corporate tax-payers and on improved compliance in this sector, which has created a distortion relative to the smaller and informal sector operators, who tend to

go untaxed. However, it must be recognised that the absolute levels of direct tax and VAT are not high by international standards and that part of the problem is that both corporate and individual direct tax-payers had long ago become used to not paying their taxes. As in Zambia, differential improvements in compliance between the formal and informal sectors may be creating an inequity and this could have important implications for the registration and conduct of businesses. However, the evaluation team found no direct evidence of informalisation.

33. *Ghana*: the Ghana Reintroduction of VAT project has introduced a new tax instrument to the revenue structure. When considering the implications of VAT incidence we need to make a comparison with the instruments it is replacing – the former sales tax, the cocoa tax and other trade taxes. The VAT has tended to broaden the tax base and to make the system more nearly proportional. Factors that contribute to these outcomes include: the contribution of VAT to permitting the removal of the most distortionary higher levels of trade taxation (notably taxes on cocoa exports but also the higher import tariffs); the broadening of the base to include services, which largely affects higher income tax-payers; the widespread exemption of goods and services that constitute an important share of the budgets of poorer households (agricultural raw products, urban transport, medicine, etc.); and the lowering of the base rate (10 per cent) in comparison with the previous sales tax.

34. *Pakistan:* DFID's support for the development of VAT-like characteristics in the sales tax has not had a major impact on tax incidence. The sales tax continues to be characterised by extensive exemptions for key commodities such as unprocessed food and medicine. Major shortcomings in the overall structure of the tax system, which effectively excludes the agricultural sectors from input and output taxes, have not been touched by the project.

35. With respect to direct taxation, the assessment of DFID's activity on the impact of incidence hinges especially closely on changes in compliance that result from improved administration, since the rate structure of direct taxation has been broadly stable (at least compared to indirect taxation) in the selected case study countries.

36. An aspect of tax incidence which arose in all the case studies, was the perception that the tax authorities' improved administrative efficiency concentrates too much on the existing pool of registered tax-payers, and that improvements in compliance have largely occurred within this group. This perception was strong in both Zambia and Uganda, where the industry and trade organisations complain vociferously that the tax authorities are concentrating on the few known larger tax-payers to the exclusion of the broad mass of non-compliant individuals and smaller businesses.

3.2.1 OVERALL INCIDENCE OF THE TAX SYSTEM

37. This evaluation has concentrated on those tax instruments implemented by the organisations that are supported by DFID, typically income tax, Customs and Excise, and the major national indirect taxes

(sales tax and VAT). However, a systematic review of tax incidence would also need to incorporate two other major types of taxation: locally generated revenues and service user charges. Locally raised revenues are not usually important in terms of their share of total government revenue. They do, however, involve the separation of certain tax bases. In many cases locally raised taxes are using archaic instruments and are very poorly administered; this leads to inequity and low revenues. This is the case in Uganda and Zambia.

38. Charges to users form an important part of the overall fiscal incidence because they typically apply to essential services (including primary education and health). It is clear that the introduction of user charges in these sectors in the 1980s had a substantial impact on fiscal incidence, equivalent to a major increase in the taxation of the poorest groups. These charges are, for many poor households, a more important component of fiscal incidence than the impact of the formal tax instruments themselves.

3.3 LINKS BETWEEN REVENUE – CURRENT EXPENDITURE AND POVERTY

3.3.1 HYPOTHESISED LINKAGE

39. The second hypothesised mechanism by which DFID's support for revenue projects can affect poverty is through the expenditure side of the government budget. This mechanism is cited in the project rationale for all the case study projects, that is that support for revenue administration should increase the resources available to government to finance spending on poverty-reducing services and interventions. This mechanism depends on several conditions being fulfilled: DFID's support must indeed increase revenue (at least in relation to a counterfactual situation without the project); increased revenue must become available for current spending (that is, it must not to be used, for example, to increase debt service of other non-discretionary spending); the government must be committed to using incremental resources on poverty-reducing outlays; and finally, the systems for managing the budget and expenditure must be able to translate budgetary allocations into effective delivery of services to the poor. It will be immediately apparent that these are demanding conditions and it should not be presumed that recipient countries can meet them. The evaluation team has, accordingly, attempted to assess how far these conditions are met in the case study countries.

3.3.2 HAS DFID'S SUPPORT INCREASED REVENUE?

40. As argued above, the DFID projects examined have been successful in increasing government revenue, even where actual revenue may have stagnated or fallen as a proportion of GDP. The appropriate benchmark for assessing the impact of DFID's support is a counterfactual situation based on what revenue would have been collected in the absence of DFID support. However, this revenue-raising influence was naturally rather modest in the case of the project in Ghana, which aimed at neutrality of revenue collection.

3.3.3 DOES INCREASED REVENUE LEAD TO INCREASED CURRENT EXPENDITURE?

41. The evaluation team has sought to understand the relation between increased revenue and the level of government expenditure on current services. The case study countries in Africa are all operating (or have recently operated) cash budgeting systems as a mechanism for increasing control over the expenditure side of the budget. While the cash budget system varies somewhat in its details between countries, the basic system is the same. Expenditure ceilings are set in relation to the resources expected to be available, especially from domestic revenue. The expenditure ceiling set is not necessarily equal to total revenue, but relates to a maximum permissible residual financing for the budget from the central bank. Revenues and expenditures are monitored and if there is a significant shortfall in the mobilisation of resources, allocations for expenditure are reduced to maintain the underlying monetary target, usually on a quarterly basis. Cash budgeting is accompanied by a distinction between non-discretionary (statutory and other unavoidable items) and discretionary expenditures. In the event of a revenue shortfall, the adjustment must fall disproportionately on the discretionary expenditures, which include the major services that are considered to be pro-poor, such as health and education.

42. The effect of changes in revenue collection are therefore dependent on the budgetary performance in relation to the cash budget controls and there is no simple relationship between revenue and expenditure on services. If there is a shortfall on cash budget targets, incremental revenues are allocated to ensure that non-discretionary expenditures are met.

3.3.4 IS INCREMENTAL EXPENDITURE PRO-POOR?

43. To ask whether incremental expenditure is pro-poor is to presume that we know what constitutes pro-poor spending. In fact the definition is not at all obvious because many forms of expenditure impact on poverty with varying linkage mechanisms and differing time profiles. Faced with these difficulties the donor community has tended to equate pro-poor spending with a limited number of ostensibly poverty-reducing lines of expenditure, the so-called "sexy six" budgetary sub-heads: primary education, primary health care, rural feeder roads, rural electrification, poverty-focused expenditure in agriculture, and some social welfare expenditure. These priorities have been institutionalised in the commitments and conditions attached to specific budget line allocations by the IMF and the World Bank in all three African countries reviewed, as well as in Pakistan.

44. However, once it is recognised that a much wider range of spending also impacts on poverty, attention moves to the formulation of the budget. In a situation where government budgetary planning was firmly based on the poverty-reduction agenda, and where the requirements of this agenda permeated the process of allocating resources, the budgetary outcome would be expected to have an equal poverty-reduction impact at the margin for all budget heads and sub-heads. In other words, it would not be possible to improve the poverty-reduction impact of the budget by reallocation of resources between

heads or sub-heads. Allocations to domestic debt reduction would be as efficacious as increased primary health care, albeit with a different time profile for impact on poverty.

45. Clearly this happy situation of perfect poverty-oriented budgetary planning does not prevail in the case study countries today. Systems for allocating expenditure are characterised by rather gross imperfections:

- the inherited budgetary structures have a historically built-in regressiveness in expenditure that reflects the interests of ruling elites. This is most apparent in education and health, with the predominance of expenditures at the tertiary level that benefit the urban and better-off disproportionately, as demonstrated by the World Bank's Expenditure Incidence Study in Ghana (Demery et al, 1995).

- the continued risk of fungibility in the use of incremental revenues and associated diversion to military and other applications.

3.3.5 ARE BUDGETARY SYSTEMS ADEQUATE TO ENSURE THAT INCREASED ALLOCATIONS ARE REFLECTED IN IMPROVED SERVICES?

46. A problem found in all the case studies was the poor quality of the systems for monitoring and tracking expenditure, which meant that few guarantees could be given that funds, even when allocated to agreed priority budget heads, would actually be applied to those purposes. Reasons include: the continued problem of creation of unauthorised budgetary arrears for uncommitted expenditure; the diversion of budgetary resources from front-line services to administrative support services; the undermining of final service delivery through inappropriately small allocations to essential operational budgetary lines; a simple lack of monitoring mechanisms that mean actual final expenditures remain unknown until long after the expenditure in question.

47. In the way the linkage between incremental revenue and incremental pro-poor spending functions, the case study countries can be ranged on a spectrum. At one extreme is Zambia, where in spite of the government's attempts to conform to the social (pro-poor) spending priorities agreed with the World Bank, continued macroeconomic instability and inadequate or non-existent systems for budgetary management allow little or no relation between revenue and pro-poor spending under present conditions. Uganda, at the other extreme, has made substantial progress within a stabilised economy to place poverty-reduction at the centre of its planning process. It is also taking active steps to upgrade the monitoring and tracking systems necessary to control the actual use of spending.

48. Revenue collection is justified by the expenditure it permits. In economic terms incremental revenue is justified if the social value of resulting expenditure exceeds the social cost of collection (which is

primarily the social valuation of the private loss of income to the tax-payer, plus collection costs). **Under present conditions it is difficult to justify revenue raising efforts on the basis of their contribution to incremental pro-poor service provision**, though this is becoming possible in the countries closest to best practice (for example Uganda). For DFID revenue projects the implication is that the social profitability of these projects can be enhanced by taking measures to improve public budgetary and expenditure management, and to incorporate poverty objectives in the planning process more firmly. Also it must be remembered that most revenue projects make their impact over a longer period than the current year. Increased trend revenues will be reflected in expenditure if a longer period is adopted and the short-term implications of cash budget management are put in the medium-term context.

3.3.6 FISCAL INCIDENCE

49. Earlier sections of this chapter have reviewed the question of incidence on the tax and expenditure sides of the budget. For the purpose of defining appropriate DFID interventions for poverty reduction it is, however, necessary to look at the combined impact, or what has been called fiscal incidence, which incorporates both tax and expenditure analysis. The trend towards broad proportionality in tax systems (driven by the quest for economic efficiency) prompts the question: which side of the public sector budget should provide the cutting edge for redistribution? There is clearly much scope for increasing the poverty orientation of the expenditure side of the budget, and DFID's support for such budgetary reorientation may be an effective way of improving the overall impact of fiscal incidence on revenue-side interventions.

3.4 LINKS BETWEEN REVENUE AND GROWTH

50. The third hypothesised linkage between revenue and poverty works through the effect of increased revenue in easing constraints on growth, especially at the macroeconomic level. Experience from East Asia in recent decades has demonstrated the potential for rapid economic growth to accelerate poverty reduction when opportunities for the poor to participate in employment and economic advancement improve. This suggests that in economies where continuing macroeconomic instability associated with structural deficits in the public sector finances act as a constraint on investment and growth, the development of revenue capacity and collection may play a pivotal role in removing the constraints on resumed growth.

51. The evaluation findings confirmed the importance of this mechanism in all three of the African economies, though in each case the finding is a matter of interpretation and judgement rather than of proof.

52. In Uganda the early achievements of the revenue authority in building up the revenue base from 5.7 per cent of GDP to 11 per cent constituted a major element in the successful macrostabilisation

programme effected during the early 1990s, an achievement that was heavily dependent on the DFID-supported first phase of the project.

53. In Zambia the strong revenue performance has reduced the negative impact on the budget of adverse macroeconomic developments, and has given the government more leeway than it would otherwise have had in managing the successive fiscal crises. Given the persistent failure to achieve fiscal sustainability, however, the hypothetical benefits on growth and resulting poverty reduction have yet to be achieved. The alternative scenario, in the absence of support for revenue collection, would doubtless have been an even more adverse cycle of inflation and falling real incomes.

54. In Ghana full macrostabilisation has yet to be achieved. In particular the very high levels of domestic debt that are a result of recent counter-inflationary monetary measures have crowded out other categories of expenditure in the government budget. With little room for further reduction in expenditure there is a critical role for increased revenue to resolve the persisting fiscal unsustainability. The successful launch of the VAT (at the second attempt) has now given the Ghana government an instrument for increasing its revenue/GDP ratio in the coming years. This will make a major contribution to creating the basic economic conditions for sustained growth by reducing public sector domestic debt with the subsequent reduction in real interest rates.

3.5 SOCIAL DEVELOPMENT ASPECTS OF REVENUE PROJECTS

55. The evaluation team reviewed the revenue systems in the case study countries in the context of three relevant social development issues. These were: gender bias, the openness of the formulation of the budget, and whether poverty-oriented civil society organisations (CSOs) could influence budgetary outcomes.

3.5.1 TAXATION AND GENDER

56. The evaluation team reviewed the tax instruments in the case study projects to find out whether they affected men and women differently, and if so whether this had any poverty implications. Progress in this area was hampered by the difficulty of obtaining information on direct tax collection broken down by sex and income group – a problem that will be resolved when the revenue authorities move towards direct tax computerisation.

57. As countries tackle the taxation of the informal sector more systematically it will be important to keep the question of impact on gender under close review. A large proportion of participants in the informal sector at the lower end of the income scale are women. Furthermore, women are usually responsible for caring for AIDS orphans, and find that the flexibility of the informal sector helps them to do this. These issues need further analysis before major inroads are made into the taxation of the informal sector.

58. The requirement for compliant tax-payers to be literate has increased sharply with the introduction of VAT, and in some countries this has a gender dimension. A particular issue is whether smaller scale traders are discouraged from registration for VAT by the bureaucratic requirements. The evaluation team reviewed this question in Ghana (Cape Province) where it was not considered to be an issue, but it may be elsewhere.

3.5.2 THE INVOLVEMENT OF STAKEHOLDERS IN THE FORMULATION OF THE BUDGET

59. One mechanism for making the budgetary process more responsive to the needs of the poor is to give greater voice to advocacy groups with a pro-poor orientation. The current state of the budgetary process was accordingly assessed in each of the case study countries to determine the extent to which pro-poor advocates are able to participate in and influence the budgetary process. This assessment was based on interviews with civil society organisations and budgetary managers in each country.

60. A wide variation was found in the development of budgetary processes that accommodate the views of non-governmental bodies. In Zambia there is a formal consultation process, with a known timetable for pressure groups and lobbies to submit their budgetary recommendations, complemented by a committee structure within the Ministry of Finance that assesses the recommendations received. The major economic interest groups and poverty-related civil society organisations all participate in this process annually. While many express a degree of frustration (not all recommendations can be accepted) the system is widely appreciated. Similar, if less developed, processes are used in Ghana and Uganda.

61. Participation, viewed as a mechanism for giving the poor a voice in the budgetary process, suffers from two principal shortcomings: the civil society organisations and pro-poor lobby groups have rather limited technical capacity to develop their proposals to the point where they will be seriously considered by government. This was true even of the most active organisations, such as the Catholic Commission for Peace and Justice in Zambia, and more so for the smaller less organised organisations. The second problem is that even where they do actively formulate proposals a framework has not evolved within which government can receive and use them in its pro-poor budgeting. An exception is Uganda, where it could be argued that though the government has put poverty on the budgetary agenda, this has made demands on the NGOs that they are unable to meet.

62. There would be scope for DFID to offer resources for future revenue-related projects, or in contemporary projects, to civil society organisations to support their development and articulation of pro-poor fiscal policies.

3.6 TAX POLICY ISSUES

63. DFID-support has tended not to address tax policy because this was assumed to be covered in the negotiations between the ministry of finance and the IMF. However, the evaluation team has observed a number of unresolved tax policy issues that will significantly affect the effectiveness of continued DFID support to the revenue function.

3.6.1 HAS REVENUE REACHED A PLATEAU?

64. Revenue collection in the African case study countries shows an initial strong upward movement in performance (measured by the revenue/GDP ratio) followed by a more recent period of stagnation and, in both Ghana and Zambia, actual declines. With the exception of Ghana, the case study projects have worked within a largely static tax policy framework, and increases in revenue are, to a large degree, attributable to enhanced collection and compliance. The recent trends suggest that extraction of significant revenue increments on this basis may become progressively more difficult.

65. The stagnation of revenue at a comparatively low level as a share of GDP (only 11–12 per cent in Uganda, and 18–19 per cent in Zambia and Ghana) may constrain improvement in the quality and quantity of pro-poor government services. Three principal factors limit the tax yield on the existing direct and indirect tax instruments: the effective failure to tax the agricultural sector; the failure to tax the informal sector (part of which is of course in agriculture); and the extent of exemptions on major household consumer items under the VAT.

66. Countries that face continuing fiscal imbalances can be expected to try and remove these constraints on revenue collection in future. The issue is whether this will be possible to achieve without undermining the present benign characteristics of tax incidence in these countries.

3.6.2 APPROACH TO THE INFORMAL SECTOR

67. In each of the case study countries the question of whether and how to tax the informal sector of the economy is exercising the minds of policy analysts. Structural changes in the composition of GDP, and the fear that tax effort has been concentrated on the formal sector, has increased the recognition that a strategy needs to be defined for taxing the informal sector, and also that a policy framework is needed that avoids differences between the informal and formal sectors that distort the tax regimes. Nevertheless, there are significant obstacles to the establishment of appropriate policies:

- some countries lack the political will to apply the full force of the tax law to informal operators who are perceived to have low incomes and to be electorally important.

- the dispersed nature of the informal sector, with low average turnover and incomes, creates a conflict between the uniform application of the law and the cost-effectiveness of revenue collection. Faced with the imperative of strong conditions set by the IMF on short-term revenue collection, administrators naturally concentrate their inadequate resources on the relatively well known and accessible tax-payers. There is a clear trade-off between equity (which demands equal treatment between sectors) and efficiency (which requires concentration of resources on larger tax-payers).

- the low level of accounting skills and lack of records found in most, if not all, businesses in the informal sector.

- an uncertainty in tax policy as to whether the best approach to the informal sector is by direct or indirect taxation.

- attempts to address the issue of taxation of the informal sector directly, through legislation in the form of presumptive tax, have not yet proved their popularity with revenue administrations (See Box 2).

Box 2: The introduction of presumptive tax in Uganda

Uganda introduced a Presumptive Income Tax (PT) for low turnover informal sector enterprises in 1998, under IMF conditionality. The PT provides for assessment of the income tax liability on a presumptive basis for small-scale enterprises. It is intended to provide a mechanism for tax collection from this sector without the impractical paperwork and accounting requirements of the main Income Tax schedule.

The new instrument, which has yet to be actively espoused by the URA, promises to raise revenue from a part of the economy notoriously difficult to tax. The PT provides for substantially lower rates of taxation than those under the Income Tax schedule. One problem of the PT is that it introduces a discontinuity in the effective rate of tax as businesses progress from the PT to Income Tax (which they are required to do if their turnover increases above the Income Tax threshold), creating a perverse incentive for the subdivision of businesses.

68. The result of these difficulties is that as stronger administration is improving compliance in the formal sector, it is at the cost of widening the gulf between tax-payers and non-tax-payers. In extreme situations, such as in Zambia, this is actually leading some businesses to deregister to avoid tax, and in less extreme situations smaller operators avoid registration in the first place, and so limit their potential for growth and ability to interact with the formal sector of the economy (see Box 3).

69. The issue of whether and how to tax the informal sector is clearly becoming a focal point of concern in Sub-Saharan Africa. In Kenya, the revenue authority has recently submitted its proposals to the

Treasury for taxation of the informal sector based on a differentiated approach for the various sub-sectors. Different approaches are likely to have markedly different implications for the poor, making this an appropriate area of policy for DFID's involvement through project support.

Box 3: Dilemmas in taxing the informal sector – the Zambian experience

Zambia illustrates clearly the dilemmas facing governments in the region in respect of taxation policy towards the informal sector. Macroeconomic decline coupled with trade liberalisation have progressively reduced the scope of the formal mining-led sector of the economy, leading to increased reliance for household incomes on informal market opportunities, often petty trading. However, the informal sector comprises several distinct groups: (i) the relatively formal well-established private trading community (usually referred to as the "Asian Traders"); (ii) small scale operations working in the newly designated market places – the "Vendors"; (iii) small scale business operations operated from the home or other urban premises, but not in the formally designated markets; (iv) larger scale operators, often with political connections, especially on external trade of items such as second hand clothing and vehicle spare parts.

Government policy is to incorporate the informal sector in the tax system so that all perceive themselves as contributing to the budget. ZRA has implemented this policy primarily through efforts to bring the Asian Traders within the tax net, by means of an amnesty on arrears in 1999. In addition proposals have been made to bring in the Vendors through the imposition of a small levy on the market premises collected by the City Council officers in the market place. However, the rate of this tax, which is set at a very low uniform rate to cover all operators means that collection is not cost-effective.

The incidence of direct taxation on the informal sector is perceived to be unfair, with larger operators often evading tax while the very low-income market vendors are caught. Moreover the Vendors represent a political force the government wishes to placate, so that this avenue of taxation does not appear promising.

3.6.3 THE LOCAL GOVERNMENT REVENUE ISSUE

70. Revenue projects supported by DFID characteristically assist central revenue collection institutions. However, there is also an important local government dimension to the revenue function. Several countries are pursuing active policies of decentralisation (notably Uganda among the case study countries) and these policies raise important questions about the allocation of tax instruments to different levels of government and the possible relations between central and local tax authorities.

71. In Uganda a large proportion of the central government budget now passes, in principle, through the local administration structure. However, comparable progress has not been achieved in developing local tax instruments or capacity for local tax collection. The local authorities continue to rely on the outdated graduated tax, which has an inappropriately low ceiling on individual collections. At the same time

significant local taxable capacity, especially from the large farmers and agricultural and livestock holdings, remains untaxed. Collection competence for the local instruments is very poor, as is the lack of transparency in the use of collected revenues.

72. There may be scope for improving efficiency, and extending the effective role of the local authorities, by utilising the skills and offices of the central revenue authorities to strengthen the collection of local taxes for which the central revenue authorities have no responsibility.

3.6.4 MANAGEMENT OF TAX POLICY

73. In each country the evaluation team has assessed the existing capacity for the design and adoption of appropriate tax strategies and policies.

74. The overall finding is that the capacity for tax policy analysis and planning is underdeveloped. There are two elements to this finding. First, there has been a tendency for any existing capacity to analyse tax policy to be undermined by the dominant role played by the IMF in the setting of revenue policies in countries undergoing stabilisation programmes. On several occasions the evaluation team heard it said that there was little point in supporting expensive tax policy units in government if actual directions of revenue policy were determined during brief IMF programme consultations. This would appear to be one explanation for the atrophied tax policy capacity in Zambia and its failure to develop in Pakistan.

75. The second element of the finding was that some countries have failed to distinguish between the levels and types of tax policy analysis appropriate to the government and to the revenue authority. In Uganda, the revenue authority was invested, under the original legislation, with the role of policy adviser to the government. This has since been amended and removed from the authority's mandate. In Zambia there has clearly been a rivalry between the Zambia Revenue Authority and the Ministry of Finance, which is believed to have hindered the evolution of well-defined national revenue policies. In Pakistan there is virtually no capacity within the Ministry of Finance for independent tax policy analysis and the Central Board of Revenue has the main advisory role. In Ghana and Uganda more conventional relationships have been established, with the ministries of finance taking the lead role in formulating tax policy, while the revenue authorities concentrate on collection.

76. These differences prompt the questions: what form and level of capacity to analyse tax policy would be appropriate, and where should it be located within the public sector? A subsidiary question is whether there is a role for DFID in the strengthening of such a capacity. Many people interviewed by the evaluation team believed that tax policy was a technical issue best left to the IMF, and that any attempt by DFID to intervene would send mixed messages and undermine the IMF's efforts.

77. The evaluation team believes, however, that there is indeed a need for the capability to analyse tax policy to be developed in the countries they visited, and that DFID could support this process.

78. In examining requirements for tax policy analysis it is useful to distinguish three levels of activity:

(i) At the **strategic level** there is a wider process of the reform of tax systems and structures, which has been led by the IMF and World Bank in recent decades. This involves the progressive reduction of trade taxes, the broadening of the tax base, the adoption of broad systems of indirect taxation with relatively low and uniform rates, and the reduction of direct tax rates where these are out of line with international norms. Broad tax strategy will continue to be determined by governments in consultation with the Bretton Woods institutions at this level.

(ii) At the **tax instrument level**, however, there is a wide range of decisions and settings to be determined that are of a tax policy nature. The extent to which the direct tax system should be inflation proofed, the schedules of exemptions and zero-rating for indirect taxes, and the regime of investment incentives, are all examples of tax policy issues that call for sound analytical capabilities within the public sector. Because they involve issues of equity and economic efficiency, they cannot be passed over to a purely technical institution for determination. All the countries reviewed need to strengthen this level of analysis, which will typically reside in the ministry of finance or the central bank (or both). Box 4 illustrates the range of tax policy issues at this level in Zambia.

Box 4: Zambia RIZES – priority issues for the tax policy unit (TPU)

Issues which could appropriately be addressed by the Tax Policy Unit in Ministry of Finance, Zambia, were identified as follows:

- Review of the tax structure in relation to poverty alleviation (specific attention to the level and inflation adjustment system for income tax credit and rate brackets).
- Articulating the fiscal policy elements of the GoZ's Poverty Reduction and Growth Strategy in the context of the GoZ's relations with the IMF and other donors.
- Development of a coherent strategy towards the taxation of the informal sector.
- Review of external tariff policy in the light of Zambia's international commitments and the prospects for manufacturing sector investment.
- Analysis of the tax expenditure cost of existing tax exemptions and investment allowances and the formulation of coherent policies for the attraction of inward investment.
- Approaches to the reduction of tax avoidance.
- Formulation of medium and long-term fiscal strategies.

(Extract from RIZES Appraisal, 2000)

In order to strengthen the orientation of analysis towards the reduction of poverty, countries particularly need to develop methodologies for disaggregated analysis of the incidence of proposals for specific tax reform. For indirect taxes, such incidence analysis should combine the rich sources of information on patterns of household expenditure that are now available with the detailed schedules of rates and exemptions for VAT and other instruments to arrive at group specific estimates of tax incidence. For direct taxes, improved accessibility of information (held by the revenue authorities but, typically, not available) on the actual pattern of tax incidence by income group will be needed.

(iii) At the **revenue implementation level** tax collection agencies do increasingly recognise that they need to increase their analytical capacity in order to carry out their mandates efficiently. Cost-effective collection strategies can only be built on sound information and analysis of the economy, and their interactions with actual and potential tax-payers. DFID's support to the Tax Policy Unit in Pakistan has effectively strengthened analytical capacity within the Board of Revenue's Tax Policy Department through support for the construction of models based on inputs and outputs. These models allow the rapid calculation of the expected impact (on revenue and prices) of adjustments to schedules of sales tax rates on specific commodities (See Box 5).

Box 5: Pakistan: DFID support for the Tax Policy Unit (TPU)

Among the case studies, DFID is only supporting tax policy development in the Pakistan project. This has established a new unit within the Tax Policy Department of the Central Board of Revenue. The function of the unit is closely tied to the requirements of the CBR, and especially the Sales Tax Wing, and addresses practical issues relevant to collection strategy and approaches. The initiative for the Tax Policy Unit came originally from the expatriate staff of the DFID project, and the unit enjoyed only partial support from within the CBR.

The establishment of the TPU has not significantly addressed the more basic problem of a lack of tax policy analysis capability within the Ministry of Finance. External donors have pressed for several years for a more comprehensive reform of the tax system with a view to remedying the inequity and loss of tax revenue arising from the blanket failure to tax the agricultural sector.

The formation of the TPU has helped to raise the profile of analytical work as a necessary support service for efficient collection and some progress has been made in establishing workable models to sustain such analysis.

79. In practice there is likely to be an overlap in the appropriate modelling structures for tax policy work at the instrument and implementation level, though the institutions involved are different. This can lead to conflict over the location of analytical capacity (such conflict has threatened to emerge in Zambia). Alternatively it can be viewed as the basis for a collaborative and co-operative approach to development of analysis capability within the public sector with appropriate capacity being developed in more than one institution. DFID can potentially facilitate this positive approach in recipient countries.

4. INSTITUTIONAL DEVELOPMENT IN THE REVENUE SERVICE

4.1 THE UNIVERSITY OF BIRMINGHAM STUDY OF REVENUE ADMINISTRATION PROJECTS

80. In 1997/98 the University of Birmingham undertook a detailed study (University of Birmingham, 1998) of DFID's experience of reforming revenue administration, concentrating on projects in Africa. Given this recent detailed review, the present evaluation concentrates on other areas and it was agreed at the Inception Report stage that the coverage of issues of institutional development would be relatively brief. Nevertheless, the countries studied for this evaluation provide a basis for further comment on the findings and conclusions of the Birmingham study. In this chapter, accordingly, the major findings of the Birmingham study are reviewed in the light of the evaluation case studies.

4.2 IS THERE A TRADE-OFF BETWEEN TAX COLLECTION AND CAPACITY BUILDING?

81. The evaluation team encountered several indications that DFID revenue projects face a difficulty in balancing their activities between support for the achievement of short-term targets for revenue collection on the one hand, and the pursuit of longer-term objectives for institutional capacity-building on the other. This dilemma is institutionalised in some revenue authorities by a total concentration on getting the revenue in during the second half of the month to the exclusion of, for example, staff training.

82. However, the team also found many examples of approaches to enhanced collection that are based on and embodied in improved and innovative systems and methods, where raising current collections and developing the base for the future go hand-in-hand. The implication is that careful and detailed design of the project may be able to minimise this trade-off.

4.3 THE EFFECTIVENESS OF THE REVENUE AUTHORITY MODEL

83. The robustness of the revenue authority model is evidently the most important institutional issue facing revenue projects, and the Birmingham study provided an overview of the strengths and weaknesses of this framework. The present evaluation was not designed to make a definitive assessment of this issue. All the African case study countries have established revenue authorities, so that the evaluation does not provide a basis for comparison between countries with and without a revenue authority. Furthermore in each case the study was confined to a limited number of revenue departments. The evaluation nevertheless provides some observations on the extent to which the strengths and weaknesses are manifest in the case study countries. These include:

- the *de facto* degree of adoption of the revenue authority framework varies from country to country. Even where adopted at a legal level, as in Ghana, the benefits may be invalidated by poor co-ordination between the various revenue services. This is reflected in poor adoption of cross-department efficiency measures such as the implementation of Tax Identification Numbers (TIN), linked computer systems and common approaches to common services.

- in Uganda and Zambia the revenue authority framework has, for several years, provided the basis for maintaining more competitive salaries and retaining staff, though some erosion of initial pay differentials has occurred. In Ghana the adoption of the revenue authority concept has not led to independent pay scales, and there are serious problems with staff recruitment.

- the implementation of the revenue authority structure has led to more internal flexibility in the allocation of revenue authority budgets but has not brought independence from the state budget. It is notable that, in spite of assurances they gave to donors who fund revenue projects, none of the countries has actually adopted a system of appropriation-in-aid for the revenue services, and these services remain dependent on the tribulations of budgetary allocations – appropriation-in-aid is discussed in more detail in Section 4.8. This has removed the potential to use appropriation-in-aid as an incentive to improved collection and has led to poorer than expected performance in extending administrative improvements, especially in the geographically outlying services, which tend to remain under-resourced.

- generally, the revenue authority framework has not yet led to a significant easing of the problems of enforcement. Several authorities still need to work through the government attorney-general's office.

4.4 THE LARGE TAX-PAYER UNIT: THE UGANDAN EXPERIENCE

84. The establishment of large tax-payer units provides a method of focusing scarce resources on the limited number of large clients who pay most of the revenue collected. This concept is favoured by the IMF, which sees the benefit of concentrating all activities concerning one business client in a single department: it avoids the multiple inspections by unco-ordinated departments that typically lead to corruption, and reduces the tax-payer’s costs of compliance. Uganda provides the clearest example of the establishment of a Large Tax-payer Department (LTD) (actually an LTD of the Uganda Revenue Authority). The accounts of the largest 100 companies (including a further 112 subsidiaries) are handled by the unit for all tax instruments collected by the revenue authority. Initially the unit’s staff was assembled by "poaching" from the existing collecting departments, which generally lost their best inspectors and assessors and became demoralised as a result. Latterly, however, the establishment of the LTD has permitted the other departments to concentrate their attentions on the larger of their remaining customers, creating a significant initiative for their middle size customers. It is still too soon to judge the impact on revenue of the Large Tax-payer Department in Uganda, but so far this appears to have been limited.

4.5 IMBALANCES IN DEPARTMENTAL DEVELOPMENT WITHIN REVENUE AUTHORITIES

85. The evaluation team noted a tendency towards an uneven rate of modernisation in the various revenue departments. The support of DFID has often, understandably, been concentrated on new areas of revenue collection, especially VAT (all the Africa case studies), where the implementation of a new revenue instrument has been the opportunity to establish from the outset dedicated computerised information and tracking systems. By contrast, the direct taxation departments typically run long-standing manual systems and have fallen behind in the modernisation process. Whilst initially this pattern of unbalanced development did not pose a significant threat to enhancing capacity of the revenue departments, it is now constraining various initiatives that cut across the traditional instrument-based departmental boundaries. This is reflected by a spate of requests for DFID to finance modernisation programmes for the direct tax system (Zambia, Ghana and Uganda). Unless this imbalance is addressed, the benefits that will be realised by DFID investments within the progressing departments will be limited.

4.6 MERGER OF VAT AND DIRECT TAXATION

86. The trend towards reorganisation of the revenue authorities from an instrument-based organisation to a functional one is evident. It is visible in three trends: moves to create common services across existing departments (audit or investigation for example); the creation of large tax-payer departments or units, which carry out the functions of several collecting departments in respect of the larger clients; and the move towards common computer systems across revenue instruments.

87. The evaluation team notes that the IMF and World Bank are now pressing several countries to move towards full integration of the VAT and direct taxation departments, which they justify on the grounds of a common client base, and the advantages of harmonising the direct and indirect taxation of corporate clients on the basis of audited accounts. Given the important continuing differences in corporate culture in the direct taxation and VAT departments in most countries, this issue needs to be approached with sensitivity if key stakeholders in the revenue authorities are to take ownership of the merger option. It is important, however, for the design of the new round of direct taxation computerisation projects, that longer-range plans for merger (or alternative forms of co-operation) are made explicit at an early stage.

4.7 INFORMATION TECHNOLOGY AND COMPUTERISATION

88. Computerisation and the development of information technology (IT) systems have played an important role in DFID's support for revenue projects, often including computerisation of Customs through the introduction of ASYCUDA software and the installation of VAT computer and software systems. It is, however, outside the scope of this evaluation to review this aspect closely. It is merely noted that in several countries there were difficulties introducing IT systems on time and within budget, and

that bedding down problems were the norm rather than the exception. An example is the difficulty caused by the introduction of the VIPS computer software for VAT management in Ghana. However, computerisation has a critical role in the overall development of the capacity of revenue authorities to deliver an efficient and effective service as well as in the reduction of compliance costs, especially for corporate tax-payers.

4.8 FUNDING: THE FAILURE TO IMPLEMENT APPROPRIATION-IN-AID

89. The evaluation team noted the unwillingness of government budgetary authorities to adopt methods of giving the revenue authorities direct access to their administrative and operational budgets by retaining a proportion of the revenue collected. Such appropriation-in-aid schemes have been advocated widely as an incentive to the revenue authority to exceed its set revenue targets and as a way of protecting the critical revenue services from the vagaries of budgetary releases that undermine other departments. It appears that the principal objection of budgetary authorities to appropriation-in-aid is that such schemes weaken the overall budgetary control exercised from the centre, combined with an element of rivalry noted in some countries between the ministry of finance and the revenue authority, whereby the autonomy of the latter is resented by the former.

90. It is clear that, for all the African case study projects, the level of budgetary funding to the revenue authority acts as a constraint, especially in respect of the expansion of the tax base geographically and downwards to smaller scale operators. In the Ghana VAT Service, for example, this deficiency is reflected in unfilled staff positions, especially in the inspectorate for rural areas. However, it is less clear what an appropriate rule for budgetary authorities to follow would be in determining an appropriate level of current financing by the revenue authority. On the one hand, revenue authorities claim that within the budgetary year, increased financing can more than offset increases of revenue that result from higher levels of inspection. On the other hand, ministries of finance are keen to avoid the perception that the revenue authority receives special treatment in the budgetary process.

91. Progress in accessing adequate operating budgets is unlikely to be achieved until revenue authorities are able to demonstrate much more credibly and directly that incremental budgets will in fact be translated into increased revenues. This in turn will depend on sound internal departmental systems of cost-accounting and monitoring, which can show clearly the input–output relationship. The evaluation team noted that progress was being made in introducing such systems in several of the case study revenue authorities. In the meantime, the lesson for DFID when appraising a project is that paper commitments to budgetary support from government cannot be relied upon. A key element of proper accounting systems would be the introduction of the distinction between the revenue authority's developmental and current expenditures.

4.9 CORRUPTION AND GOVERNANCE ISSUES

92. Tax authorities in countries assisted by DFID almost universally face a problem in controlling corruption within their ranks, and projects have often inherited situations where revenue corruption was formerly a way of life (literally). This corruption takes several forms, and the three most common are probably: turning a blind eye to duty-free importation of dutiable goods for a consideration (either on a petty scale at the borders, or on a large scale that involves complete industrial consignments); the "negotiation" of tax settlements by tax inspectors with both corporate and individual tax-payers; and the large scale tax-evaders with political connections who are untouchable by the revenue officials.

93. The evaluation team recognise that it is difficult for them to make an accurate assessment of the extent of corruption, especially during a short visit to the country. Nevertheless, it is clear that fighting corruption remains a major task for all the case study projects. In Uganda the failure of the revenue authority to systematically collect duties on imports has become a hot political issue, because local manufacturers claim that a significant proportion of imported manufactured goods are entering the country without bearing the legally mandated duties. Estimates prepared by the Uganda Manufacturers Association (UMA) based on their members' knowledge of individual product markets, suggest that up to 10 per cent of the legally mandated duties on imports are not being collected. The concentration of the figure on a limited number of key products with domestic production competitors points to more than casual laxity at the border posts. The Association points to goods on offer in the informal markets at prices close to ex-factory prices in Kenya. The perception that the revenue authority is failing to collect adequately on Customs has led to calls for the services to be fully contracted out and the Mozambique experience (supported by DFID) has been cited as a model.

94. Officials of the Uganda Revenue Authority point to the difficulty of policing Uganda's long land and lake borders, the smugglers' flexibility in switching between routes and modes of transport, and the increasing use of sophisticated computer-based fraud. The extension of the URA project aims to strengthen the authority's ability to combat these threats, and the arrests of high-profile URA officers in late 1999 pointed to the government's commitment to take the matter seriously.

95. More generally it must be asked whether DFID-assisted revenue projects are in a position to combat corruption effectively. The four principal instruments include: the creation of attractive salary scales to reduce the temptations of office; close management of the inspectorate and the limitation of the powers of assessment of any one officer or team, coupled with frequent rotation of teams across clients; a shift to increased reliance on documented and audited accounts as the basis for assessment; strengthening linkages between tax instruments, to reduce the possibility of out-of-line assessments on any one instrument; and the establishment of adequate penalties and a sufficiently rapid legal response to impropriety.

96. However, even though there is a wide range of instruments for reducing corruption, it is clear that there are limits to what is achievable within projects supported by DFID if there is not a wider framework for sound governance in place. In particular, efforts to reduce corruption in the revenue authority may fail if there are such shortcomings in the governance framework as:

- the appointment of a chief executive who is too close to the political ruling elite
- the revenue authority is not given enough freedom to pursue high-profile tax-evaders. This creates an environment of unwillingness to pay tax.
- the wider framework to combat corruption in government and in business is weak or non-existent.

97. All these shortcomings were found in the selected African case studies, and they had reduced the effectiveness of DFID's support to the project.

4.10 MANAGEMENT OF THE INTRODUCTION OF A NEW REVENUE INSTRUMENT

98. The evaluation team encountered important examples where DFID was supporting the introduction of new tax instruments. In Ghana, in particular, the involvement of DFID in two successive projects provides a rich source of lessons in the "dos and don'ts" of introducing the VAT (See Box 6).

Box 6: Lessons from the reintroduction of VAT in Ghana

Ghana first attempted to introduce VAT in March 1996, with a supporting project financed by DFID. The attempt failed as the government lost political support in the face of large price increases in the retail sector and the legislation was withdrawn in June 1996.

VAT was reintroduced in December 1997, again with support from DFID, this time through the GRVAT project.

Some key lessons in the experience were:

- The need for an adequate period between enacting and implementing VAT legislation.
- The importance of broad political support for introduction of potentially unpopular tax legislation.
- The importance of public awareness campaigning in preparing the public and professional bodies and the business community for VAT introduction.
- The value of involving key stakeholders in the introduction process. For example, in 1997 the VAT Service contracted the Ghana Union of Traders' Associations (GUTA), (who had vociferously opposed VAT in 1996) to undertake independent price monitoring during the period before and after VAT introduction.
- The decisive importance of the rate at which the new instrument is initially set. In Ghana it was set at 10 per cent compared to an average former sales tax rate of 12 per cent.
- The scope for use of exemptions and zero-rating to mitigate potential adverse effects on poorer consumers and politically sensitive groups (the urban poor).

These lessons were effectively learnt in Ghana and the second attempt was managed very smoothly. This is the main reason for the difference in performance in DFID's two projects in support of Ghana VAT.

4.11 ISSUES OF SUSTAINABILITY IN INSTITUTIONAL DEVELOPMENT

99. All the case study projects are seeking to achieve sustainable increases in revenue-collection capacity in their recipient institutions. It is necessary to ask whether this is being achieved. As the projects are still running, we cannot yet say whether the impact on institutional capacity can be sustained: one of the critical tests of sustainability is whether innovations introduced during a project survive after it has been completed. However, it is possible to point to elements of the projects that can be expected to promote the sustainability of institutional improvements, and also to any risks to sustainability encountered during the evaluation.

100. Four broad types of innovation that promote sustainability have been supported by the projects:

- support for institutional reforms that promote operational efficiency.

- support for new systems and working methods that are fully adopted by the revenue authority and embedded in practice.

- innovations captured in the skill level of the work force, and, equally important, in the capacity of the organisation to renew the skill levels of its staff in the face of staff turnover and technological developments.

- legislative reforms that enhance taxability or the framework for enforcing tax compliance, or both.

101. Two case study projects (Zambia and Uganda) were characterised initially by the large number of technical co-operation officers (TCOs) appointed to fill line management positions in their respective revenue authorities. But in both countries the degree of such support has been progressively reduced, so that by the middle of the year 2000, there was only a single such position in each country.

102. While the initiatives mentioned above tend to give confidence that the projects will have a sustainable impact on the development of capacity, there are a number of factors that could undermine that sustainability. These include:

- the weakening of the arm's length relationship of the revenue authority to the line ministries denotes an erosion of the quality of governance. The evaluation team noted a tendency, in countries that initially took a strong line to create relatively independent revenue agencies, for this to be undermined over time, especially if the revenue and fiscal position of the government becomes less precarious.

- the erosion of commitment to the eradication of corruption as a result either of staffing changes within the revenue authority or in the context of the wider national efforts to control corruption. This is clearly a threat that accompanies the withdrawal of expatriate line managers from senior management posts, as it is more difficult for local incumbents who have links to the local political system to impose effective anti-corruption measures.

- the erosion of human capital, built up by DFID projects, through rapid staff turnover. The two main factors that push up turnover are the erosion of pay differentials (though this has not gone very far in Zambia and Uganda, where there are separate pay scales for the revenue authority and the public service), and the impact of the HIV/AIDS pandemic. Rapid staff turnover reduces the return on staff training (at the level of the business) and this has obviously affected the efforts of the Zambia project.

- inflexible management, which does not adapt systems and procedures to meet changing circumstances. In all the case study countries the nature of the economy and the way people do business are changing rapidly, and also call for rapid change in methods of tax collection.

5. PROJECT CYCLE ISSUES: APPRAISAL TO EVALUATION

103. The case study projects are all relatively large, multi-phase projects that extend over several years. They constitute a rich source of information on how effectively the cycle of a DFID project is managed. All the case study projects have encountered major crises that have shaped their subsequent development. The original Ghana project (GRVAT), implemented in 1995/96, had to be discontinued when the first attempt to introduce the VAT was legally rescinded (see Box 6). The Zambia project (ZRACP) was essentially redesigned after the damning report produced after the Governance Adviser's visit in November 1997 (DFID, 1997a). This pointed to a wide range of problems in the design and implementation of the project (see Box 7). Its subsequent restart on a stronger basis with a dedicated project manager provides an object lesson in the design of process-based projects. In Uganda the initially promising support to the revenue authority was subsequently scaled back as DFID was still unconvinced that governance issues were being adequately addressed.

5.1 APPRAISAL ISSUES

104. Several problems in the design of projects, and with associated methods of evaluation, were encountered in the course of the evaluation.

5.1.1 THE REDUCTION OF POVERTY AS A SUPERGOAL

105. The projects under review were all prepared before the issue of the White Paper in November 1997, and so reflected the previous thinking of the United Kingdom Government. Specifically, poverty objectives and implications were not prominently documented in the appraisal of any of the case study projects. The need for DFID to justify all projects in relation to the poverty reduction targets places a new onus on the officers who prepare projects to specify clearly what impact on poverty they expect the new revenue projects to have. As will be clear from the discussion in previous chapters, the causal mechanisms are in many cases likely to be both manifold and subject to a range of risks.

5.1.2 THE REVENUE TO COST-OF-COLLECTION RATIO AS AN OBJECTIVELY VERIFIABLE INDICATOR OF MORE EFFICIENT ADMINISTRATION

106. The projects reviewed make extensive use of the cost/revenue ratio as the principal objectively verifiable indicator (OVI) for more efficient management. This is subject to a range of problems:

- suitable benchmarks for use as reference points of absolute efficiency have not been established for the conditions prevailing in the Africa region (they are available for developed economies from a range of tax authority internet websites).
- when changes in managerial efficiency are assessed, it is necessary to take into account the need

to pay more attention to collecting tax from smaller tax-payers from whom it costs more to collect, to avoid the tendency towards segmentation of these economies into taxed and untaxed sectors. The implication is that a desirable shift towards extending the tax base into the unregistered sector of the economy will tend to raise the cost/revenue ratio.

Box 7: Zambia 1997 project review conclusions

In September 1997, a DFID Governance Adviser, undertook a review of the ZRACP. The report (DFID, 1997a) was a key turning point in the implementation of this project and was referred to extensively in subsequent project documentation. The main problems identified were:

Lack of strategy and vision: ZRA's corporate plan no longer reflected the situation facing the Authority and where vision existed it was individualistic, personalised and isolated to senior management.

Lack of political commitment and local ownership: there were different views as to the level of political commitment demonstrated towards ZRA and specifically ZRACP. However, the lack of local ownership was indisputable. The latter had been a central concern of DFID yet few steps had been taken to foster it since the February project launch. In September 1997, the Governance Adviser determined that the majority of staff were not even aware of the project's existence.

Lack of communication and information: there was a very limited concept of the need for information sharing about the project and operational matters within the culture of ZRA. This generated suspicion and distrust amongst ZRA staff.

Poor project design and planning: the absence of up-to-date project action plans or Gantt charts for the various components of ZRACP.

Poor project focus: the project had become too input focused with attention paid to consultants' contractual constraints, disagreements with consulting firms, and personality clashes, at the cost of focusing on what ZRA was trying to achieve and how best it could do so.

Inappropriate project pace and sequencing: project design and planning problems were exacerbated by the speed of implementation envisaged for ZRA.

Poor project management and co-ordination: there was ambiguity over who was responsible for managing ZRACP and non-DFID funded project activities.

Failure to take account of institutional and absorptive capacity: The Adviser identified the danger that the scope and ambition of ZRACP exceeded the organisation's staff's absorptive capacity.

Poorly defined organisation and staffing structure: the diagnostic reports concluded that management and staff in key operational divisions did not fully understand the functions, responsibilities, accountabilities and delegated authorities of their own and other related units. Management control was also reported to be weak.

5.2 COUNTRY STRATEGY PROCESS

107. Revenue projects are typically large enough to be a significant component in the respective DFID Country Strategy. Furthermore, as we have argued in previous chapters, revenue projects raise a number of issues that go beyond the limits of the project. It is, accordingly, appropriate to review the way they fit into the wider programme.

5.2.1 POLICY DIALOGUE WITH GOVERNMENT AND THE MULTILATERAL DONORS

108. The revenue projects were all intended to contribute substantially to wider macroeconomic stabilisation and consolidation by strengthening the government's budget. In practice, however, DFID's involvement in the dialogue on macroeconomic stabilisation policy is rather limited. More specifically, DFID has not been closely involved in dialogues on taxation policy, which has usually been treated as the preserve of the IMF in conjunction with the national authorities. Usually DFID has provided technical support for the institutional capacity-building that is necessary to implement decisions on tax policy that have already been taken, and DFID's project staff tend to emphasise the technical nature of their mandate. There are some exceptions, such as the involvement of the British High Commission and DFID in policy discussions in Pakistan on the evolution of the sales tax. Furthermore, DFID was actively involved in the original discussions leading to the formation of revenue authorities, for example in Uganda and Zambia.

109. DFID's support for revenue projects has, typically, not carried tax policy conditionality (or pre-start-up conditions relating to tax policy). An exception is the Pakistan project, where successive rounds of support to the Central Board of Revenue were given on condition that the government made progress in addressing the broader issue of taxation of the agricultural sector. This condition was consistently ignored by the Pakistan government without any project-level sanctions, and this undermined the credibility of attempts to influence tax policy.

110. This limited involvement raises two questions: first, whether a closer involvement in dialogue on policy would lead to a more focused DFID country programme, and second, whether DFID financing for projects that address issues regarded by governments as being of strategic fiscal importance increases the scope for DFID's influence in other areas of policy, such as in a government's poverty strategy. Clearly, as one of several bilateral donors, DFID cannot expect to have a dominant role in round table involvement in economic policy dialogue. However, there appears to be scope for a stronger DFID voice in macro-level policy dialogue in some countries. In Uganda the IMF's continuing heavy emphasis on short-run revenue targets does not rest easily with the current level of donor funding for the budget, and a shift towards greater emphasis on longer-run development of the tax base would be in order. Appropriate indicators of progress in broadening the tax base could be developed fairly easily, and incorporated in macro-conditionality along with the conventional indicators. A closer involvement of

DFID in the specific area of taxation, in which DFID has been so heavily concerned as a financier of technical assistance, would be beneficial. It would, of course, depend on there being appropriately qualified DFID staff in the country or at least the Africa region.

5.2.2 LINKAGES WITHIN THE COUNTRY STRATEGY

111. Given the conclusion of this review that the impact of revenue projects on pro-poor spending in the short term is tenuous or non-existent, the rationale for revenue projects rests heavily on the benefits of longer term capacity-building and the concomitant strengthening of expenditure management systems. This conclusion raises several issues for the identification and appraisal of projects and for the management of revenue projects whose benefits are linked to other initiatives outside the scope of the revenue project itself.

112. A key issue in respect of identification and appraisal is the need to note any weaknesses and risks related to expenditure management systems. If these are weak and not being strengthened the revenue project is unlikely to achieve its goal. The obvious solution to this problem rests at the country strategy level, and the adoption of a holistic approach to the planning of DFID interventions in such specific sub-sectors as revenue. This approach has already been effective in Ghana and Uganda. In these countries DFID is making revenue interventions in the context of a broader master plan for the improvement of public sector management led by the World Bank. However, while the oversight of the various interventions has been linked, the linkage has not been translated into the effective tracking and monitoring systems that are needed to clarify the progress and impact of linked revenue projects supported by DFID.

113. This observation, in turn, raises the important question as to who should undertake cross-project tracking and monitoring activities, in both DFID and government. Revenue officials (and their technical assistance counterparts) tend to be perplexed when questioned on issues of expenditure management. These are understandably seen as falling outside their own responsibility and competence. DFID monitoring, such as the Output-to-Purpose Reviews, were observed by the evaluation team to focus closely on achievement at the output level and the risks to purpose level fulfilment and neglected assessment of progress towards goals.

5.2.3 IS THERE A GAP IN DFID'S STRUCTURE FOR MANAGEMENT OF THE COUNTRY STRATEGY?

114. The need for initial appraisal and subsequent tracking and monitoring of linkages with other projects and areas of budgetary management raises a question about DFID's field structures in relation to the tasks to be completed. Revenue projects typically address a broad macroeconomic problem with strong linkages to expenditure side and poverty reduction activities, but the preparation, supervision and

management of revenue projects have remained largely the preserve of governance advisers within DFID. While the compartmentalisation of DFID has contributed to the development of strong, institutionally-oriented revenue projects, it has also weakened the economic and poverty-reduction aspects of these projects .

115. The solution appears to lie in strengthening DFID's capacity to formulate strategy, identify projects, and track programmes at the country level.

6. CONCLUSIONS AND LESSONS FOR THE FUTURE

116. This chapter is a review of the evaluation team's main conclusions, and the lessons to be learned by the main players – recipient governments, DFID and other stakeholders.

6.1 CONCLUSIONS

6.1.1 THE EFFECTIVENESS OF REVENUE PROJECTS

117. The revenue projects in this study have all broadly achieved their goals and purposes, especially when viewed over the full period of DFID's support (that is, including earlier phases of project activity). In Zambia and Uganda, DFID's support in the early stages of the establishment of the revenue authorities made a critical contribution to the initial sharp increases in revenue/GDP ratios. The quality of technical assistance has generally been high, and DFID is respected as a leading provider of support to revenue administration. However, with hindsight it is clear that major errors were made in the early stages of the Zambia and Ghana projects: the initial management framework for ZRACP was inadequate and basically collapsed in 1996, and the conditions for the introduction of the VAT in Ghana were not in place at the time of the first project. In Pakistan a messy process of appraisal and design has led to continuing support of the project within a very weak policy environment.

118. An important contribution has also been made to building capacity for sustainable collection of revenue through the wide range of specific interventions that DFID has supported in management systems, development of human resources, and organisational changes. This increased capacity is expected to lead to a significant increase in future revenue collection capacity, offsetting to a large degree the lack of short term impact of revenue collection on government expenditures. There are, however, a number of threats to the sustainability of these improvements. These include the possibility of a weakened governance framework; reduced independence of the revenue authorities (in Zambia and Uganda); inadequate budgetary support for operating expenditures; and threats to human resources from reduced incentives and from HIV/AIDS.

6.1.2 REVENUE PROJECTS AND POVERTY

119. The evaluation team has reviewed the linkages between DFID's support for the revenue function and poverty through three hypothesised mechanisms: tax incidence, links between revenue and expenditure, and links between revenue and growth. The main conclusions can be summarised as follows:

- DFID projects do not support regressive tax regimes or regressive new instruments. Instead they contribute to the redesign of tax structures in order to reinforce a broad tax base, to lower maximum rates, and reduce dependence on trade taxes. The relatively benign incidence characteristics observed in each of the three Africa case studies however, stem largely from the widespread exemptions that characterise the emerging indirect tax systems, with many low income budget goods exempted or zero-rated for VAT.

- the link between incremental revenue and pro-poor current public expenditure, often cited to justify DFID's support of revenue projects, is in fact weak and burdened with problems, in most instances. Two reasons for this are: in countries with continuing fiscal unsustainability the link is inherently weak because expenditures have to be directly related to closing the fiscal deficit, and crisis management (especially servicing and retirement of external and domestic debt). With the existing cash budgeting systems the linkage may be completely lacking where targets for macro-indicators are not being met and incremental revenues are allocated to these macro-objectives under IMF conditionality; a weak commitment to pro-poor budgetary allocations and weak budgetary and expenditure management systems (including tracking and control of actual expenditure applications) further erode the plausibility of this mechanism in the case study countries, at least in the short term.

- the four case studies illustrate a wide range of experience of addressing the weaknesses that inhibit the desired relationship between revenue and pro-poor expenditure. At one extreme Zambia has extremely weak systems for managing the budget, which, coupled with continuing fiscal unsustainability, render the revenue–expenditure linkage virtually void. At the other extreme, Uganda has taken a range of steps to strengthen each link in the chain through such measures as the adoption of systematic poverty-reduction based budget planning, and expenditure tracking for key categories of poverty-related expenditure.

- linkages between revenue enhancement and poverty reduction through the establishment of the conditions for economic growth are seen to be important in all the African case studies, even if all the expected benefits have yet to be realised in some cases (for example in Ghana).

6.1.3 HOW REVENUE PROJECTS FIT INTO THE DFID AGENDA ON THE REDUCTION OF POVERTY

120. The central question addressed in this evaluation is whether DFID's revenue projects fit into the DFID agenda as defined by the strong poverty-reduction orientation underlying the 1997 White Paper. The evaluation team has therefore reviewed the impact on poverty of DFID revenue projects in four case studies and undertaken a broader assessment of the effectiveness of those projects.

121. The case for DFID's continued involvement in supporting the revenue function – within the current DFID portfolio – is based on several arguments:

- in the short term DFID's projects have supported the governments of the case study countries to achieve the macroeconomic stabilisation targets that are considered critical for economic normalisation and the resumption of economic growth.

- in creating the capacity for recipient countries to address seriously the reduction of poverty, DFID projects have substantively supported the building of capacity for future revenue collection, either by consolidating the introduction of new broad-based tax instruments (for example the VAT in Ghana), or through the building of supporting capabilities in the revenue authorities (all three African case studies). Viewed within the World Bank's Comprehensive Development Framework, the revenue function should be seen as one of the essential elements of a functioning economy.

- the case for DFID's revenue projects is based on the presumption that they will contribute to expenditure on pro-poor services but this was found to be weak: in the case study countries the chain between increased revenue and increased pro-poor spending has several critical weak links that seriously undermine the argument in support of these projects. However, this must be seen in relation to the time taken to develop revenue capacity and for the expenditure systems to evolve. The building of revenue collection capability requires several years (broadly between five and ten) and the current DFID revenue projects will have a longer lasting positive impact on revenue collection. This delay allows time to strengthen the systems for managing public expenditure.

6.1.4 CONDITIONS REQUIRED FOR THE REVENUE PROJECTS TO BE EFFECTIVE

122. Analysis of the case study projects indicates that several conditions need to be met if revenue projects are to be successful. In-country, the principal conditions are:

- strong political support for the revenue authority and respect for its agreed degree of independence by the line ministries, as statutorily provided.

- broad political support for the specific revenue instruments in which DFID is to be involved. In Ghana the initial project lacked this support, and this was the principal reason for its failure.

- an appropriate framework of governance for the revenue authority, including the appointment of a chief executive who is at an adequate distance from the political ruling elite.

- a high degree of commitment on the part of the government to eradicate corruption. Where this is lacking, any beneficial effect that a revenue project might have is likely to be short lived.

6.2 LESSONS

6.2.1 LESSONS FOR RECIPIENT GOVERNMENTS

123. Many of the findings and conclusions of this evaluation are of interest principally to governments. These face the challenge of increasing revenue performance while pursuing increasingly pro-poor policies. Lessons include:

- the continuing need to provide a governance framework within which revenue authorities can perform their functions effectively without continual compromise.

- the need to ensure that the conditions that will sustain institutional development under DFID projects continue to be met. These include respecting the independence of the revenue authority, permitting the continuation of pay differentials (in relation to the public sector) where these have been necessary to allow the revenue authority to recruit skilled staff, and the provision of regular budgetary allocations for operating budgets.

- the need in some cases to clarify the institutional locus of tax policy analysis in which to create tax policies so that, in the short and the longer term, the requirements of growth and the reduction of poverty can be met, and to develop the ability to analyse the problems and trade-offs necessary in such policy analysis.

- the need to address seriously the taxation of the informal sector and to devise cost-effective strategies that enable revenue growth to be sustained but do not jeopardise poverty reduction objectives.

- the need to address the weaknesses in the systems for budgetary and expenditure management, which currently undermine the potential economic returns on investment in the revenue services.

6.2.2 LESSONS FOR REVENUE AUTHORITIES

124. These include:

- the need to achieve the right balance between tax collection from existing known tax-payers and the use of resources to extend the tax base to include those who are currently evading tax. Some countries have concentrated excessively on the existing tax-payers in order to meet targets set by the IMF and governments.

- the desirability of improving information to management on the cost-effectiveness of different activities. It is at present difficult to recognise that development expenditures aimed at consolidating the future tax base may be inefficient in the short run but can be justified by a longer time horizon; improved information on cost-effectiveness would also facilitate the flow of budgetary funds from government.

- the need to work closely with government on the development of equitable and cost-effective strategies for taxing the informal and agricultural sectors. To the extent that the debate on these topics hinges on tax collectibility, the revenue authorities should be involved in the review of options.

- the need to upgrade systems for direct tax information to the standards that now typically prevail for indirect tax instruments. This can only be achieved with accelerated computerisation.

6.2.3 LESSONS FOR DFID

125. The conclusion of this report is that revenue projects should indeed have a place in DFID's portfolio. For such projects to be effective, however, DFID needs to take several steps to ensure that the design of projects maximises their impact on poverty, and that wider issues of country portfolio management are addressed.

How to sharpen the impact on poverty of DFID's support for revenue projects

126. The four revenue projects evaluated in this study originated in the period before the 1997 White Paper, and their goals centred on objectives within the revenue function – increasing revenue collection and building revenue collection capacity. New projects (and extensions to existing projects such as the Revenue Institutions in Zambia: Enhanced Support (RIZES) project in Zambia, which was approved in November 2000) are being developed that have a clearer view of their contribution to poverty reduction. The findings in this evaluation point to a number of measures that can be taken, when designing and preparing revenue projects, to increase the likely impact on poverty. These include:

a. **being selective in the choice of countries for support to revenue while developing the overall DFID country strategy.** Those countries with most to gain from the strengthening of the revenue service are usually the same countries that are at an early stage in developing expenditure management systems and where guarantees on the effective use of resulting incremental revenues are most problematic. Where expenditure management systems are especially poor or government commitment to the reduction of poverty is weak, such projects may not be appropriate. In this context it is doubtful whether continued support to revenue collection in Pakistan is warranted.

b. during development of the DFID country strategy, **concentrate analytical attention on the question of fiscal incidence,** and not only the narrower questions of tax and expenditure incidence. That is, look at the net incidence of revenue and decisions on the allocation of expected accompanying expenditure. Given that revenues are not normally hypothecated, such forecasts of expenditure incidence can only be based on broad assessments of the progressivity of the expenditure side of the budget.

c. **where there is government support, build tax policy components** into revenue projects with a specific mandate to incorporate poverty-related analysis into the mainstream budget agenda. Lending by the IMF based on the Poverty Reduction Strategy should provide a context in many potential recipient countries for the provision of technical and capability-building support to tax policy.

d. where expenditure management systems are weak or inadequate, **nest DFID revenue projects in country programmes**. This also addresses the expenditure side issues. This may also be achieved in the context of multi-donor country programmes that address all main aspects of the public sector budget management.

e. **use project resources to broaden the scope for pro-poor civil society organisations and other organisations to influence the budgetary process**. There is clearly a role for other stakeholders, such as business organisations, pro-poor NGOs and other civil society organisations, etc. to participate in a more democratised budgetary process. The finding in this evaluation is that these organisations, especially pro-poor CSOs, often lack the analytical capability to provide advice that can be taken seriously by the budgetary authorities. This can be changed through public support, especially in those countries where the principle of an open and democratic budgetary process has already been espoused. DFID could support the strengthening of analytical and representational capacity in some of the latter as a way of giving the poor a voice in the budget, for example by making small or matching grants to CSOs.

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ANNEX A: TERMS OF REFERENCE

INTRODUCTION

A1. DFID's Evaluation Department wishes to appoint a team of consultants to undertake an evaluation of DFID's involvement in revenue-related projects. The main aim of the evaluation will be to improve the effectiveness of support for the development of the revenue function in partner countries through the identification and dissemination of good practice in this area. To this end, the evaluation will analyse experience in a selection of completed and ongoing revenue projects, funded by DFID and by other donors, in a range of countries. It will draw also on relevant academic and other literature, including a study of DFID revenue projects in Africa by the School of Public Policy at the University of Birmingham, which was completed in June 1998.

BACKGROUND

A2. DFID has been involved with partner countries for many years in a variety of projects in the broad revenue field, ranging from the provision of direct assistance with the management of Customs and Excise, to advice on the reform of tax policy and the development of longer term capacity in tax departments and agencies. Support for the establishment of separate revenue authorities has increasingly featured in our programme, particularly in Africa.

A3. The White Paper on International Development defined DFID's aim as the elimination of poverty in poorer countries, and gave a clear message that all of the Department's activities must be justified in terms of their contribution to this aim. This sets the context for the evaluation, for which an underlying theme will be how well DFID's involvement in revenue projects fits with our new agenda. The analysis of this issue will be informed by our increased understanding of the crucial importance for growth and development of good public sector financial management, and specifically, well prioritised and executed public expenditure programmes, and a revenue system which is efficient, effective and equitable.

OBJECTIVES

A4. The evaluation will have the following objectives:

- to assess the appropriateness, efficiency, and effectiveness in meeting their objectives, of Overseas Development Administration (ODA)–DFID projects in support of the revenue function in a range of partner countries since 1990.

- to assess the likely impact of this support in contributing to the achievement of wider economic and social goals in partner countries.

- to identify lessons on good practice in the appraisal, design, implementation, and monitoring and evaluation of revenue projects, which will be of value in increasing the effectiveness and the sustainable economic and social impact of DFID assistance in this area in the future.

ISSUES

A5. An Appendix to this Annex outlines some of the issues which DFID believes are relevant to the evaluation. These issues have been illuminated by the Birmingham study, and by the discussion of its conclusions which took place at a workshop in Zimbabwe in July 1998.

APPROACH

A6. The evaluation will proceed in three broad stages. During the **first stage**, the selected evaluation team will develop a detailed methodology in response to these terms of reference, and will undertake the necessary research and data collection and collation. As part of this process, and in consultation with EvD and DFID regional departments, the team will identify a representative sample of relevant completed DFID projects for evaluation. The scope and coverage of the evaluation of the selected projects will be agreed between the team and EvD. Subject to agreement with regional departments, a range of other relevant DFID material will be identified, including project completion reports (PCRs), output to purpose reviews (OPRs) of ongoing projects, and submissions to management in relation to recently approved and proposed new projects. It is expected that extensive use will be made of evaluation material and other relevant literature from selected bilateral and multilateral donors and from academic institutions. The report produced by the University of Birmingham on DFID support to African revenue authorities should form a particularly key input into the study. An initial stakeholder analysis should be produced at this stage, which would outline the team's view on which groups would need to be consulted during the evaluation, and suggest how this might be done.

A7. The core of the **second stage** will be the evaluation of the selected completed projects, which will necessitate field visits to the partner countries in which the projects were implemented. Analysis of other material identified as relevant will be undertaken at this stage.

A8. The **third stage** will involve drawing together the conclusions of stage two, and the drafting and finalisation of the expected outputs of the study. These outputs are set out below.

OUTPUTS

A9. The evaluation team will produce a report in two volumes. Volume 1 will consist of a synthesis report, which will draw together the findings and lessons of the study. Volume 2 will contain the individual project evaluations, along with other relevant supporting material.

A10. The team will produce a draft of the report for discussion at a DFID seminar, and for circulation to other stakeholders. Subsequently, a final version will be produced, reflecting, as far as is appropriate, comments from DFID staff and other stakeholders, and feedback received at the seminar.

A11. The report will be presented to a meeting of DFID's Projects and Evaluation Committee (PEC), chaired by the Director General (Programmes).[2] The evaluation team leader, accompanied if necessary by other members of the team, will be expected to participate in this meeting, along with the Task Manager and the Head of EvD.

APPENDIX TO TERMS OF REFERENCE

ISSUES FOR THE EVALUATION

It is arguable that a positive relationship between support for revenue systems and poverty elimination hinges largely on the incidence of taxation – who pays – and the incidence of public expenditure – *who benefits*. This prompts a number of fundamental questions, which concern the context within which it is appropriate for DFID to support partner governments' revenue systems. The ideal situation is probably one in which public expenditure clearly supports a sound pro-poor policy framework, and the taxes which we help to collect to fund this expenditure are raised in a way which is fair and non-distortionary (or can be made so). That such ideal conditions do not exist in our partner countries should not prevent us from involvement in support for the revenue function, but does imply a need for rigorous economic and social appraisal, and monitoring and evaluation of revenue projects. The evaluation study should seek to identify good practice in these areas.

The range of issues which the evaluation might examine is extensive. The sample below, presented in no particular order and randomly grouped, is a preliminary attempt at defining some key areas.

Tax Policy : Many revenue projects are implemented in the context of wider programmes of economic reform and transition. On the donor side, the IMF is often considered to lead on tax policy – is this therefore taken as given in many DFID projects? The recent independent evaluation of Enhanced Structural Adjustment Facility (ESAF) questions whether too much emphasis is sometimes placed on increasing revenue, and not enough on the impact on economic growth of higher transfers to the government from the private sector. It is clear also that, when the incidence of certain taxes is on the final consumer, revenue-raising measures may have detrimental effects on poor groups. Are there examples of good practice in the analysis of these key issues? Many donor projects focus on improving revenue performance by changing the way in which the tax system is administered (e.g. through support for the establishment of autonomous revenue authorities). Does this focus lead us to pay insufficient attention to potential synergies between improved administration and reform of the tax system itself which might allow a pro-poor redistribution of the tax burden? How can donors promote "good" tax

[2] The report will now be presented to a meeting of DFID's Portfolio Review Committee.

policies? What are the key elements in tax policy and administration which lead to lower transaction costs? Have DFID supported initiatives contributed to lowering costs in partner countries?

Budgetary Context : In an ideal world taxes would be levied in order to fund an agreed and rigorously prioritised expenditure programme in the least distortionary way. In our non-ideal world, it is crucial to treat revenue as merely one side of the fiscal equation. Have DFID's revenue projects, and the broader programmes within which they operate, taken sufficient account of the need to ensure that expenditure patterns are pro-poor, or are making adequate progress in that direction?

Broader Reform Context : If a partner government's commitment to re-thinking the role of the state is lukewarm, can donor projects designed to increase revenue have the effect of reducing the pressure for reform by easing the budget constraint? Where a government is publicly committed to decentralisation but privately unenthusiastic, might support to central revenue institutions reinforce a centralising tendency? In a number of countries in which we work, the financial sector remains inefficient, and parastatals and favoured private sector operators may have preferential access to credit. In this context, how convincing is the argument that projects which help to increase the revenue take will reduce crowding out? Instead, can they merely have the effect of transferring resources from the efficient parts of the private sector to the less efficient, and to the public sector, via reduced central government borrowing from the banking system? To what extent have revenue projects been integrated with, for example, concurrent efforts to improve budgetary planning and management capacity, or civil service reform programmes? How might practice be improved? Is there any evidence which indicates whether establishing separate revenue authorities promotes or retards reform within the rest of the public service?

Project Design : This is clearly a large sub-group in itself, and many of the issues which will need to be examined are not necessarily sector-specific. A couple which are may be worth consideration. Some of our partner governments have opted for a radical approach to reform of the revenue function by setting up separate autonomous or quasi-autonomous bodies to administer the collection of taxes. Others are considering a move in this direction, or have chosen an alternative reform model somewhere between the radical option and institutional status quo. How might our appraisal of projects to support this reform process move from analysing the financial business case (i.e. the comparison of revenue attributable to the project to direct financial costs) to a more meaningful examination of the costs and benefits of the various options? What lessons can be learned about the design of projects which may have a double-sided purpose – raising revenue in the short term, and building capacity to sustain the revenue effort in the longer term – which may not be immediately compatible? How was "capacity building" defined in DFID revenue projects? What sort of indicators were proposed to measure impact, and how useful were they in practice? Is it possible to identify examples of good practice in monitoring and impact assessment, which might involve a rigorous approach to target setting, but would go beyond measuring performance in simple revenue terms, to include indicators such as cost of collection ratios and tax-payer compliance?

Again, this selection is far from exhaustive, and will need to be developed during stage one of the study to ensure that the scope of the evaluation is as comprehensive as possible.

ANNEX B: THE CASE STUDY PROJECTS

GHANA: REINTRODUCTION OF VAT PROJECT

B1. The Implementation of VAT Project was designed as a three-year project with a total commitment of £1.8 million. The project comprised: assistance to the GoG with the preparation of legislation; institution-building; the establishment of a computer system, and assistance with the planning and implementation of a public education campaign. A new revenue collection service, the VAT Service (VATS) was created, staff were recruited and trained, and a computer based system to administer the tax was developed. VAT was initially introduced in March 1995 and set at a rate of 17.5 per cent. Its introduction provoked civil unrest, leading to its repeal only three months later in July 1995. DFID's project ended prematurely having achieved mixed results in attaining its desired outputs. The main reasons for the failure to introduce VAT effectively were the high introductory rate, delays in passing legislation and an inadequate public information campaign.

B2. Although the introduction of VAT in 1995 failed, the arguments in favour of such a tax were still considered valid. Moreover, the problems experienced in 1995 were considered to relate to the way in which the tax was introduced rather than to any fundamental problem with the tax. Thus in June 1997 DFID agreed to provide £1.2 million to support the reintroduction of VAT. The goal of this project was to improve the GoG's revenue raising capacity and the purpose of the project was to introduce an effective and sustainable VAT system during 1998. The project's outputs were similar to those specified for the earlier project: the establishment of an effective VAT Service; publicity and education campaign for the general public and traders; effective computer based systems for administration of the tax; procedures for administration of the tax developed; and trained staff able to administer the tax effectively. During project design and implementation, the lessons of 1995 were fully taken into account and in December 1998 VAT was re-introduced successfully.

B3. In spite of an observed decline in the revenue/GDP ratio in Ghana in recent years the evaluation team concludes that the project has been successful in achieving its goal, to improve the revenue raising capacity of the GoG. The successful introduction of VAT has expanded the tax base and provided the GoG with a buoyant tax instrument for future revenue collection. The capacity to raise revenue in the future is further enhanced by the institutional capacity which has been created, the low rate of VAT and the widespread exemptions which currently prevail.

B4. The project has also achieved its purpose. During 1999 and 2000 the project has supported the reintroduction of an effective and sustainable VAT system: the institution is well-established; the legislative base is sound; the public have accepted the VAT; the core staff have undergone training; a VIPS information system is fully functioning; and the enforcement base is now being strengthened. There remain, however, a number of weaknesses in the system, including inadequate budgetary provision which does not provide adequate funds for operational expenses necessary to strengthen enforcement and underdeveloped relations with the other revenue departments.

B5. The project was also assessed in terms of its effectiveness in meeting DFID's new poverty objectives. This assessment was based on three mechanisms: tax incidence, revenue-expenditure linkages, and economic growth. The incidence effects of the reintroduction of VAT appear to have been mild and possibly modestly progressive. Poorer consumers have had some benefit from the reduction of the basic rate compared to the sales tax, and this reduction has been offset by the broadening of the tax base to include professional services (which are principally utilised by higher income groups). Furthermore the successful introduction of VAT has, we believe, permitted the GoG to effectively reduce the tax on cocoa farmers, who primarily fall at the lower part of the income distribution. The revenue–expenditure linkage has been strengthened under the MTEF, (supported by DFID) but the quality of public services remains poor and further progress is required in this area. Finally, the successful introduction of VAT is likely to have a positive impact on economic growth by contributing to debt resolution, thereby promoting investment and increasing the scope for financing public services. The evaluation team therefore concludes that the project is consistent with DFID's new poverty objectives.

PAKISTAN: GENERAL SALES TAX (GST) STRENGTHENING PROJECT

B6. The project purpose was to increase the capacity of the Central Board of Revenue (CBR) to reform and administer its tax collection system and the project goal was to increase revenue collection at lower cost and through improved efficiency. The project's outputs related to developing and introducing new VAT-type systems and procedures within the Sales Tax Wing (STW) of the CBR as well as training staff and developing an understanding of the new system among tax-payers, and their responsibilities within it. The primary justification for the project was that it would support IMF and Government of Pakistan (GoP) objectives to mobilise revenue in Pakistan. Enhancing revenue from the GST was considered a key source of potential revenue, particularly given the absence of progress in effectively taxing the agricultural sector. The project was also justified on the grounds that it would support economic reform and good government.

B7. The project had two phases. Phase I commenced in September 1995. It was initially planned to cover a 14-month period with a project budget of £701,900. Following several project extensions, the final commitment for Phase I amounted to £1,160,000, representing an increase of 165 per cent of the initial commitment. In part this increase can be explained by assistance provided in the area of information technology, which was originally outside the scope of the technical assistance, but to a far greater extent the additional funds were sought to achieve existing project outputs.

B8. Phase II commenced in July 1998 and was originally intended to cover an 18-month period. It consisted of a series of short term inputs and a long term adviser at the STW to provide institutional reform and administrative advice. The objectives were similar to Phase I although greater emphasis was given to achieving *sustainable* improvements in GST administration capacity and increases in tax revenues. Furthermore, improved capacity for tax policy formulation was introduced as a project output. For the purpose of project implementation, a waiver of competition was awarded to the incumbent consultants, Coopers & Lybrand. DFID's commitment under this phase of assistance was initially £720,000, increasing to £873,000 after two project extensions in July and September 1999. The project ended one month prematurely in November 1999, following the withdrawal of DFID assistance to the GoP, following a military coup.

B9. To examine the success of the project in terms of its achieving its goal *to increase revenue collection at lower cost and through improved efficiency* it is useful to distinguish between the short and medium term. In the short term (during the first three years of the project) sales tax revenue as a share of GDP was stagnant and then fell. This decline can be attributed to external factors, such as the reduction in the rate of tax and a decline in the large-scale manufacturing sector, and therefore does not reflect a deterioration in the capacity of the CBR to collect GST revenue effectively. Moreover, in spite of the targets set for raising revenue during the first few years of the project, the nature of DFID assistance meant that incremental revenue was unlikely to be realised as a result of the project in the short term. In the medium to long term, however, given the expansion of the tax base and the improved capacity of the CBR, revenue from the GST is likely to increase. The evaluation team therefore concludes that the project goal is likely to be achieved in the medium to long term, but not within the timeframe envisaged at the project's commencement.

B10. When assessing the project's performance against its purpose, *to increase the capacity of the CBR to reform and administer its tax collection system*, the project appears to have performed fairly well. The GST administration has been significantly strengthened and the project has been central to achieving this. However, during both phases, the project has failed to realise *all* the anticipated gains. For example, by the end of Phase I new processes and procedures were not fully in place and improvements in tax-payer compliance during Phase II were limited. These shortfalls were attributed to the difficult environment in which the project was being implemented and the limited timeframe permitted. It was concluded by the evaluation team that the project had made a significant contribution to enhancing the capacity of the CBR to administer the GST and by doing so had partially achieved its purpose as measured against objectively verifiable indicators set out in the logical framework.

B11. The project performs less favourably when assessed against DFID's new poverty objectives. With regard to tax incidence, whilst the incidence of GST does not raise any significant concerns (basic commodities are exempt and the tax rate has been reduced since the project commenced) the overall tax system in Pakistan is highly inequitable because of the failure of government to tax the agricultural sector effectively. Furthermore, whilst some progress has been made to improve the provision of primary services under the Social Action Programme (which is also supported by DFID) there is no guarantee that additional revenue will benefit the poor, particularly given Pakistan's current pattern of government expenditure. Finally, there may be some benefit to the poor in future years as a result of macroeconomic stabilisation, but this depends on continued government commitment to the stabilisation process and it will only benefit the poor in the long term.

UGANDA REVENUE AUTHORITY PROJECT

B12. DFID has supported the URA since 1991 in five principal areas: implementing the initial setting up of the URA; introduction of VAT (June 1996); strengthening revenue administration management systems; providing technical and management training; and improving Customs infrastructure. Initial support was aimed at assessment of the revenue authority concept and the subsequent filling of line management posts in the URA. A major project commenced in 1993 and concentrated on management systems; this was extended in 1997 and included the creation of the post of Deputy Commissioner General Revenue, filled by an expatriate. The total value of assistance under the project (as extended to 2000) was £8.6 million.

B13. DFID support to the URA since 1992 has been a critical factor behind the URA's success in creating a viable institution that has doubled the revenue/GDP ratio from around 6 per cent at the start of the 1990s to around 12 per cent in the late 1990s. However, since 1994/95 the revenue/GDP ratio has stagnated at 11 per cent, which is low by international standards. This stagnation can be attributed to a combination of factors, including the economic downturn (and especially the sharp fall in import volumes and values during 1999); the low buoyancy of the tax system, given the structural orientation of the economy and heavy dependence on agriculture; exhaustion of "easy" sources of revenue increase from improved compliance; and the inability to curb border smuggling and corruption.

B14. DFID's support to the URA has been both important and effective in making the URA a sustainable entity for revenue collection. Initial efforts at establishing basic administrative systems in URA were successful. Subsequently, as a result of DFID assistance, good progress has been made in creating a sound organisational structure; attracting and retaining staff, improving staff motivation and management quality; and developing a sound relationship between the Board and the Executive. The process of institutional capacity building remains incomplete, however, and further progress is required to develop information systems, improve corporate planning, and combat corruption.

B15. The impact of the project on poverty has been central to this evaluation. Our findings on the project's performance in this area are as follows:

- changes in the tax structure have been benign, with the impact of taxation on the poor limited by the extensive exemptions on a commodity-specific basis for the indirect tax instruments and in terms of the limited scope of the income tax system which effectively excludes the bulk of the poor.

- the poverty-reducing impact of raising incremental revenue is enhanced by the substantial progress made in orienting the government budget towards poverty-reduction, although the impact of this is dampened by the poor quality of service provision resulting from a high rate of leakage through local administrative structures and little or no accountability at the local level. The government, however, has recognised this problem and is now instigating measures to improve transparency.

- the additional revenue raised as a result of the project is unlikely to contribute to economic growth and poverty reduction through domestic debt retirement as the benefits of this would be limited due to the poor functioning of the banking sector.

The evaluation team concludes that the project has made an important contribution to poverty reduction in Uganda because of the commitment by GoU to improve social service provision.

ZAMBIA REVENUE AUTHORITY CONSOLIDATION (ZRACP) PROJECT

B16. ZRACP is an institutional-strengthening DFID project designed to ensure and sustain higher compliance with tax laws in Zambia. It builds on earlier assistance provided by ODA. The project goal is to collect a higher proportion of taxes due on a sustainable basis. The purpose of the project is to develop ZRA into an effective, efficient and well-managed organisation with Zambian top management. The project outputs are: an effective Zambian senior management team, established by 1997; strengthened corporate business processes and information systems implemented; the Direct Tax Modernisation Programme, including ASYCUDA, successfully implemented; and VAT, established successfully by December 1995 and ZRA capacity to run VAT without external support, established by 1997. DFID's commitment under the project was £5.7 million with a further £2.5 million approved at a later date.

B17. The project was formally launched in February 1997, following an 18 month delay. In September 1997, a DFID Governance & Institutions Department (GID) Adviser undertook a review of the project which marked a key turning point in project implementation. Her report identified several serious project shortfalls, including: a lack of strategy or vision; lack of political commitment or local ownership; lack of communication and information; poor project design and planning; poor project focus; inappropriate project pace and sequencing; poor project management and co-ordination; failure to take account of institutional and absorptive capacity; and a poorly defined organisation and staffing structure. Project performance was subsequently substantially improved following the uptake of a number of her recommendations, including a corporate planning workshop held at the ZRA and the appointment of a project co-ordinator.

B18. The evaluation team has concluded that the project has been successful in raising revenue in the short term in spite of the observed fall in real revenue collection. Several important factors are currently depressing revenue collection, including negative macroeconomic growth, the effect of the past liberal policy of granting tax exemptions, the negative effect of a large stock of arrears in inflationary conditions, and illiquidity resulting from the near insolvency of the mining sector. When allowance is made for these factors the ZRA is seen to be achieving a very high level of performance and the project is achieving its goal.

B19. The project has also largely achieved its purpose to develop into an effective, efficient and well-managed organisation with Zambian top management. The inadequacies identified in the GID Adviser's Report have been effectively addressed. The project is successfully pursuing organisational and management improvements. Of the four senior management posts previously held by expatriates, three are now filled by Zambians. One expatriate remains in post as Commissioner-General.

B20. The performance of the project in terms of meeting DFID's poverty objectives is thought to be generally positive, although the evaluation team concludes that there is scope for improvement in this area. The overall incidence of the tax structure is believed to be neither strongly progressive nor strongly regressive but there are areas of concern, notably the very low threshold for direct tax. The linkage between revenue and expenditure exists through the cash budgeting system and has been enhanced by MTEF, which DFID had been supporting. The Zambian authorities have shown a determination to shift the overall pattern of budget expenditure in favour of social sector expenditures but the quality of services remains poor, thereby reducing the project's poverty-reduction effect. The project has also contributed to macroeconomic stabilisation by improving ZRA's revenue-raising capacity, and this is likely to result in economic growth and poverty reduction in the long term.

DEPARTMENT FOR INTERNATIONAL DEVELOPMENT

The Department for International Development (DFID) is the UK government department responsible for promoting development and the reduction of poverty. The government first elected in 1997 has increased its commitment to development by strengthening the department and increasing its budget.

The central focus of the Government's policy, set out in the 1997 White Paper on International Development, is a commitment to the internationally agreed target to halve the proportion of people living in extreme poverty by 2015, together with the associated targets including basic health care provision and universal access to primary education by the same date. The second White Paper on International Development, published in December 2000, reaffirmed this commitment, while focusing specifically on how to manage the process of globalisation to benefit poor people.

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