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NEW SOURCES OF FINANCE FOR DEVELOPMENT

As the squeeze on national aid budgets tightens, there is renewed interest in new sources of finance for development. This Briefing Paper reviews the range of proposals currently being discussed and assessed their technical feasibility and political acceptability.

Conventional bilateral aid flows now seem set on a downward trend. The latest OECD/DAC figures confirm a fall of 6.4% in real terms from 1991 to 1994, and this appears likely to continue. Multilateral flows are severely threatened by the likely cuts in the US contribution to the International Development Association (IDA). At the same time, a series of new demands has emerged. The new countries in transition are now applicants for aid, and there are other new requirements: for financing UN peacekeeping operations, disaster relief, support for refugees, combatting AIDS, and an enlarged environmental agenda. So the search is now on again for new ways of financing 'global public goods'. The object is to give the international community an automatic, dedicated source of revenue, which, once established, would be independent of political debate and budgetary pressure in the donor countries. (One analogy is the European Union's early search for its 'own resources' in VAT and customs duties).

Ever since the Brandt Report in 1980 the list of suggestions for 'global finance' has been lengthened (see Box 2 for the 20 principal schemes). Two of them involve genuine 'new money' from existing arrangements: a new issue of SDRs, and sale of part of the IMF's gold (see Box 3). The remaining proposals all involve a new tax or charge, and fall into three overlapping groups:

- Those which piggyback on a proposed tax or charge introduced for other reasons (e.g. the Tobin Tax; pollution charges).
- Those which seek to exploit a hitherto-untapped resource, over which no existing state has sovereignty (part of the so-called 'global commons'), e.g. deep sea minerals.
- Those which involve dedicating some part of the national tax base, either voluntarily or by binding treaty.

Box 1: Global Taxation: History of an Idea

The Brandt Report in 1980 devoted a brief section to the need for 'automatic revenue', which alluded to most of the ideas discussed in this Paper. In 1984 the Development Committee Task Force on Concessional Flows listed 16 possible sources but left it to the Committee to decide how to follow them up. No action followed.

In the mid-90s the subject has come back into the international debate. In particular, the UNDP has pressed (for example in the 1994 *Human Development Report*) for more work on global taxes. UNDP organised a meeting of experts in October 1995, the results of which will be published shortly. The independent Commission on Global Governance, which reported in late 1994, argued that 'the time could be right for a fresh look and a breakthrough in this area'. In 1995, the independent Commission on Population and Quality of Life published a much more detailed study in order 'to contribute to purposeful, lively and action-oriented deliberations', but again without making firm proposals. The study suggests that 'the revenue for financing internationally agreed policy objectives and programmes should be raised through international means by tapping activities in the global markets'.

None of these ideas has been taken up by any individual member state of the United Nations. Apart from general statements of principle (for example in the Rio Declaration) and occasional ministerial speeches, there has been no sustained discussion of any of these ideas at intergovernmental level since Brandt. .

Box 2: Twenty Recent Suggestions for Global Revenue

The following list includes most of the proposals canvassed in recent publications:

(a) A tax on all or some international financial transactions (the 'Tobin Tax'). Variants include a tax on bond turnover, or on derivatives.
(b) A general surcharge on international trade.
(c) Taxes on specified traded commodities like fuel.
(d) A tax on the international arms trade.
(e) Surcharges on post and telecommunications revenues.
(f) An international lottery.
(g) A surcharge on domestic taxation (usually expressed as a progressive share of income tax).
(h) Dedication of some part of national or local taxes, eg on luxuries (or surcharges on them).
(i) Parking charges for satellites placed in geostationary orbit.
(j) Royalties on minerals mined in international waters.
(k) Charges for exploration in or exploitation of Antarctica.
(l) Charges for fishing in international waters.
(m) Charges for use of the electromagnetic spectrum.
(n) A tax or charge on international flights (or alternatively, on flights in congested sectors). A variant is a tax on aviation kerosene.
(o) A tax or charge on international shipping.
(p) Pollution charges (e.g. for dumping at sea).
(q) A tax on traded pollution permits.
(r) A voluntary local tax paid to a central global agency.
(s) A new issue of SDRs, distributed to the poorer developing countries (or used for peacekeeping or other global public goods).
(t) Sale of part of the IMF gold stock.

Basic Principles

There are some basic principles of taxation which are usually applied in looking at any new proposal for a tax. It should not distort the free operation of normal economic incentives, unless this is necessary to correct market imperfections ('externalities'). It should be easy and cheap to collect and difficult to evade. Its distributive effects should be neutral, or deliberately slanted to benefit a particular group.

The mechanics and the politics of any tax proposal are also important. How would agreement be reached and implemented? In looking at global taxes, it is particularly important to ask: What special interest groups might object, and how powerful are they? Which states might lose out, and would they block any such proposal? Are there any existing international treaties which might bar the proposed tax, and how might they be amended? Are any new international agreements or instruments needed?

If the new tax proves both feasible and desirable, then what is the possible yield? And what other objectives or organisations might lay claim to the revenue? Finally, since this problem will arise in all the cases under study, how is the tax to be determined; who will administer it; what institutions are to receive the revenue, and how is their use of it to be determined and controlled by the international community?

Not all these questions can be answered in full for each proposal; indeed, some of the ideas to be examined are still very tentative. More work has been done on the Tobin proposal than on any other, so this makes a useful test case. The checklist above forms a framework for an analysis of the rest.

The Tobin Tax

The Tobin Tax (sometimes called a Foreign Exchange Transactions Levy) was first put forward by Nobel Laureate Professor James Tobin in 1972 as a way of discouraging speculation in short-term foreign-exchange dealings, and thus minimising shocks from large currency movements. Although Tobin himself disputes this, many critics argue that the tax would make markets less efficient, and thus inherently less stable, by distorting price signals. It might inhibit certain types of operation and encourage others, which would make the market as a whole shallower. This, in turn, could make it harder for developing countries to raise money on international markets.

More recently, Tobin has suggested that such a tax might also prove a useful revenue earner, with the proceeds devoted to international development. This puts it into the 'piggyback' group of global taxation ideas. To illustrate the potential scale, a tax levied at only 0.01% of turnover, which would add about 20% to the costs of trading in currencies (a significant deterrent), might yield between $12 and $24 billion a year, based on a global turnover in these markets of around $900-1,000 billion a day. If this very tentative figure were really within grasp, it would be a major contribution to development resources: at maximum, it would be as much as half the present level of bilateral aid flows. It is the biggest resource discussed in this Paper. But there are a good many problems.

With the abolition of exchange controls in most major industrial countries, there is no longer a comprehensive reporting system for such transactions. It might therefore be necessary to create a new global system of co-ordination as a basis for the tax. In a largely electronic market, this may prove to be technically possible, but the administrative cost would be high. Alternatively, the tax might be based upon self-assessment, backed up by audit. The small number of financial institutions engaged in the market would ease the administrative problem. It would be necessary to establish the legal residence and thus the tax liability of each player in the market – both financial institutions and, more difficult, multinational corporations (which move large volumes of money around as part of their regular treasury operation, and with whom the problem of tax residence is already a major headache).

Supposing an effective system could be designed, revenue could be collected quickly through a Pay As You Trade system. The administration would probably have to be carried out by an existing revenue department rather than a central bank, because of the potential conflict of interest with the regulatory function. But central bank expertise would be important during the design phase.

Evasion would remain a problem. The more complicated the tax became (with more exemptions or differential bands), the more scope there would be for argument, depending on the original design and the coverage of the tax. If the burden of the tax became too great, it would pay many players to shift the 'booking' of their transactions offshore to financial centres which did not impose the tax. It would then be more difficult to tax the deal in the country where it was negotiated or originated. Similarly, operators might find it profitable to shift into new types of instrument not covered by the tax. This, in turn, risks further distorting the market. Efficient collection of the tax would (most commentators argue) require full coverage of markets and instruments, and full co-operation by all governments.

One variant of the Tobin proposal has recently been proposed, in which a central clearing house for foreign-exchange transactions would be established by international agreement. This could be built upon existing private networks. It is argued that a clearing house would reduce the volume and cost of transactions, and at the same time enable a transaction tax to be collected centrally and cheaply. However, such a proposal would require a lot of capital; not all the technical problems have been solved; it would compete with existing private facilities; and, according to its sponsors, it would need to be a public service requiring international agreement.

The Tobin Tax would certainly be progressive, because there would be a shift of resources from the players in financial markets, mainly situated in industrial countries, towards the developing countries. Bankers and other financial institutions who make their living in the foreign-exchange markets would object; but if there were sufficient political will at international level, this pressure would probably not be sufficient to deter action. However, exemptions would be needed to exclude small personal transactions and, for example, purchases of currency for tourism, etc., or political objections would soon multiply.

At national level, the losers would be the larger industrial countries, especially the G-7. Even if they were to support the proposal because of its currency stabilisation, they would no doubt prefer to hold on to the revenue themselves. For this reason, the developing countries could not enforce such a measure (e.g. through a majority vote in a UN body) against the wishes of the industrial countries. Some small offshore financial centres might also protest. However, there are no obvious international claimants to the proceeds of a tax, apart from the international financial institutions and the UNDP.

Opinions differ about the need for a general agreement. Some critics argue that provided sufficient major trading nations agree, the costs of evasive action are high enough to make universality unnecessary. Others believe that evasion could be made fairly cheap, so that the tax would have to be enforced by all countries. If the latter are right, then a completely new international agreement would probably be required: no manipulation of existing instruments (such as the Articles of the IMF) could deliver the required action, and concerted voluntary action in such a complex area seems impracticable. There would also need to be some standing international mechanism to set and adjust the level of the tax, and oversee its collection from national agencies and its transfer to the receiving institutions. Experience of such international negotiations (e.g. the Law of the Sea Convention described below) suggests that setting up all this would take a long time.

Using the tentative yield figures mentioned above, a tax of 0.01% on all international transactions would yield around $24 billion; allowing for the intended deterrent effect of the tax, this might come down to about $12 billion. These figures illustrate the potential conflict inherent in the double objectives of the scheme. Either the tax is set high, in order to deter speculation, and therefore has a low yield, or it is set low to maximise revenue, thus failing in its original purpose.

For this reason, the yield of the tax is likely to be fairly unpredictable, making it dangerous to rely on any given level of revenue as a firm basis for planning future aid policies.

This brief analysis of the Tobin Tax reveals many of the practical problems of 'global taxation'. The other proposals are not so fully worked out, but some general comments are possible.

Other Taxes on Markets

In the same group of ideas as the Tobin Tax are the proposals for a tax on securities and bond markets trading, or on derivatives (which partly overlaps with the Tobin Tax itself). In each case, the motivation is primarily revenue-raising, rather than market regulation. But many of the same evasion, administration and control difficulties would arise.

Environmental Charges

All of these schemes (items (n) to (q) in Box 2) involve applying the 'polluter pays' principle to 'public bads' and making the proceeds available to the international community. In that sense, they are user charges rather than new taxes. Most proposals assume that the proceeds would be used in the environmental area. For example, they might be used to help poorer developing countries to instal pollution-reducing equipment or to forgo ecologically damaging activities like felling rain forests. (These are precisely the reasons why the Global Environmental Facility (GEF) was set up in 1993, using donor money, some of which may in practice have been diverted from more traditional aid.)

One of the front runners is the idea of 'tradeable pollution permits', which are already being considered at national level in some countries. Eventually it is possible that a genuine international market in such permits will evolve. It would then be feasible to levy a small percentage charge on their transfer. But evasion could quickly reduce the yield. Administratively, the present GEF might be adapted to serve the purpose, but this would require an amendment to its current charter.

The Global Commons

At first sight, this seems a more promising area, because far fewer existing vested interests are at issue. At one time it seemed that mining of the ocean bed would provide a large and secure source of royalty revenue which might be reserved for international use. However, the prospects of large-scale exploitation have receded because of the fall in most mineral prices, and some remaining technical problems. Most research and development has been postponed, and substantial activity seems to be some 15–20 years away. Meanwhile, the negotiations over the UN Law of the Sea Convention (UNLOSC) show the difficulties of gaining international approval even of this fairly uncontroversial proposal.

The United States, which initially proposed the Convention in 1976, drew back from the idea of international control and taxation, under pressure from its own mining companies, and because of its reluctance to put additional resources in the hands of a UN system which it distrusted and could not control. The modified version, which eventually came into force in 1994, assigns much larger territorial waters to coastal states than before. A slimmed-down International Seabed Enterprise will exploit the remaining international seabed. It must work through private-sector consortia, and is entitled to only a small share of the revenue. It will be controlled by an international Authority, with limited powers to distribute its revenue to states (such as existing producers) adversely affected by its operations. The Authority and the Enterprise remain largely inactive until mining becomes a practical possibility. Negotiations continue over procedural questions such as voting powers and structure, with persistent tension between developing and industrial countries on many issues. Given this history, it would be difficult to re-open the question of substantial additional development revenue in the near future. However, it remains one of the more promising ideas for re-examination in the longer term, if the political will returns. By contrast, revenue extraction from Antarctica has been postponed well into the next century, if then.

In another corner of the global commons is the idea of imposing 'parking charges' on satellites in geostationary orbit. At present there is no form of international control over such launches. One estimate puts the potential yield as high as $14 billion a year, but this seems to imply retrospective taxation on satellites already in orbit. A tax on new launches would grow only slowly and erratically (because the number of launches varies annually). Although difficult to evade, there would be classification problems (would military or intelligence satellites be exempt?) The interests of the three major launching powers (the USA, France and Russia) might conflict with the aspirations of other nations.

Other ideas of the same general class include charging for the use of the radiomagnetic spectrum (at present allocated by the International Telecommunication Union (ITU) to national governments). Surcharges on international aviation and shipping (in effect paying for the use of neutral airspace and the international shipping lanes) are further examples of taxing the 'global commons', but these areas also have environmental benefits, and any revenue might be better allocated to anti-pollution activities than to development. These charges would be fairly easy to administer and collect, however, since many nations already apply airport departure taxes, and all airports and seaports have their own charging systems. Evasion would be difficult unless the host country colluded. Such taxes would initially fall most heavily on the richer countries but, like almost all these proposals, would ultimately be passed through to the consumer, including many in developing countries.

Nevertheless, a small global surcharge on airport fees seems one of the simpler and potentially more acceptable instruments to be pursued if an international consensus begins to emerge. Yet when the Secretary-General recently suggested that such

Box 3: New Money: SDRs and Sale of the IMF Gold

These two proposals are different in kind from the others, since they involve respectively the creation of new international liquidity and the one-off sale of a currently unused communal asset. In that sense they are costless.

SDRs are now equivalent to a far smaller proportion of the volume of world trade than they did when they were introduced in 1973. There is thus a case for some catching-up, followed by a small and continuous new issue in line with the future growth of trade, which could be redistributed to the poorer countries. But such proposals have been talked about for many years. Even for the modified version put forward by the Managing Director of the IMF in 1994 (involving a small issue of SDRs specially reserved for new members), there is not, so far, a majority among the shareholders. The old fear of stoking up world inflation, together with worries about putting too much power in the hands of the IMF, seems to have prevented action, which requires an 85% vote of IMF members. It would be even harder to gather sufficient support for a larger SDR issue, or for one aimed at financing some part of the UN activities like peacekeeping (as recently proposed).

Sale of part of the IMF's large gold holdings is another matter; there seems to be a larger vote available for this, but still not enough (it needs support from 80% of the shareholders). However, the proceeds are already spoken for: either to help reduce the level of debt owed to the international organisations by poorer countries, or to finance the continuation of the IMF's Enhanced Structural Adjustment Facility or subsidise its interest charges. And, in any case, gold is a finite resource.

revenue might be assigned to the UN, the idea was severely criticised in the US Congress. With the profits of most shipping companies under pressure, a tax on sea freight seems less attainable.

Levies and Voluntary Taxes

Some of the proposals, in practice involving a surcharge on commodities and services in international trade, shade into the third group of voluntary levies. One proposal concerns aviation kerosene which contributes to excessive carbon dioxide in the atmosphere; another, all hydrocarbon fuels or all fuels. These taxes would have to be collected through national tax authorities, all of which tax these products at present. The history of the European Commission's plans for a Carbon Tax suggests that any of them would be difficult to negotiate. Variants in this general family include a tax on international postage or telecommunications; the common factor is that the international machinery already exists, in the ITU and the Universal Postal Union. A similar idea involves a levy on international arms trading (worth $22 billion in 1991), perhaps building on the UN Register of arms sales. This is a dual-purpose proposal, designed to discourage the trade as well as to yield revenue for peacekeeping or similar UN operations. It might also have the perverse effect of encouraging exporters to evade registration.

More radically, a surcharge on all international trade has been suggested, to be collected through national customs authorities. The tax base would be enormous: total world trade was worth about $37,500 billion in 1993. But such a tax runs contrary to the general worldwide trend towards liberalisation of trade, and conflicts with the GATT obligations. Unless new collection machinery were created, it would also completely miss trade which enters duty-free within the single European market and comparable free trade areas.

Another group of proposals involves a general levy on national taxation, expressed either as a percentage of GDP or of GDP per capita, or as a percentage of the total tax yield. These ideas continue the search for an automatic source of revenue but they require a level of international agreement which seems un-negotiable in present conditions. For both budgetary and ideological reasons, it is unlikely that legislatures in the USA, the UK or France (to name only three obvious examples) would be prepared to pass the necessary measures.

A variant of this idea is designed to capture the 'peace dividend', by requiring states to divert some part of their savings on military budgets to national or multilateral aid. There are severe data problems involved here (the IMF has great difficulty in identifying military budgets accurately). But the main objections are fiscal; most countries achieving such savings since the end of the Cold War have already diverted them to the reduction of budget deficits or to their own social programmes.

An international lottery might seem slightly more acceptable, since it could in principle be made voluntary. But it would run in competition with national lotteries where they exist, many of which (like the UK) are regulated monopolies.

One final proposal in this group concerns a purely voluntary tax at sub-national (i.e. state or municipal) level. This presupposes that there would be sufficient public support in some communities for a local tax (or surcharge on local taxes) at a level to be determined locally (although indicative targets might be suggested internationally). The proceeds would be handed over to an appropriate international body. However, the current anti-taxation ethos in many countries would probably operate at local just as much as at national level; it is not clear that even the most enlightened communities would volunteer to pay such a surcharge. And in most countries, including the UK, such a scheme would also require enabling legislation at national level to permit subordinate tiers of government to take part.

Central Administration and Allocation

All these proposals, to differing degrees, involve supranational institution-building. These include the initial international agreement to impose the charge and a forum for negotiating the coverage of the scheme, including penalties for evasion, and for amending its parameters as necessary in the light of experience. For most of the proposals, machinery for collecting the proceeds from national agencies and distributing them to international bodies would rely heavily on the co-operation of national authorities. In a few of the 'global commons' cases, new collection machinery would be needed at supranational level. Above all, who would receive the revenue and allocate its disbursement? The UNLOSC story suggests resistance in some industrial countries to a handover of revenue to any UN agency subject to majority voting. It is possible that there would be less objection to the IDA, which is more tightly controlled by the G-7 countries through votes in the World Bank.

Conclusions

There is little to show so far for fifteen years of debate. But this is not surprising. The states which would find themselves contributing most (at least at the point of collection) are precisely those whose conventional aid programmes are under greatest political pressure. They are also the countries where vested interests would be most adversely affected. In many of them, such as the United States, distrust of public-sector and multilateral intervention is widespread. The potential beneficiaries, for various reasons, have not progressed far beyond rhetoric. As a result, despite much activity by international secretariats and outside experts, no nation or group of nations has made concrete proposals for action, in an appropriate forum with power to carry the action forward. Without such an initiative, none of these ideas can take off. The one exception so far is the Law of the Sea Convention, but substantial negotiating difficulties remain and technological progress has been slow. The present agreement would need substantial changes before this could become a source of revenue for development; that too would require a fresh political initiative.

Among the remaining candidates, the airport tax surcharge seems the simplest and least controversial idea, if political pressure for global revenue were to develop. The Tobin Tax remains the scheme on which most work has been done, and many of the technical problems addressed if not solved. But there is little political pressure to translate it into action (and some experts still think it wrong in principle). None of the other proposals examined here seems likely to fare any better, at least for the next few years.

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