



# IMF POLICY PAPER

## BUILDING FISCAL CAPACITY IN FRAGILE STATE

June 2017

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- A **Press Release** summarizing the views of the Executive Board as expressed during its May 12, 2017 consideration of the report.
- The **Report**, prepared by IMF staff and completed on April 18, 2017 for the Executive Board's consideration on May 12, 2017.

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## **IMF Executive Board Discusses Building Fiscal Capacity in Fragile States**

On May 12, the Executive Board of the International Monetary Fund (IMF) discussed the staff paper “Building Fiscal Capacity in Fragile States (FS),” which analyzes recent country experiences, describes the IMF’s technical assistance (TA) approach for FS, highlights how it differs from non-FS, and derives lessons for future work.

The paper notes the importance of targeting fiscal TA to achieve stability and secure, elastic revenues. Other key lessons include prioritizing reform sequencing, promoting effective donor coordination, implementing formal Medium-Term Revenue Strategies (MTRS) and expenditure reform strategies to help countries exit fragility, as well as considering further integration of TA to FS to better complement IMF lending and surveillance operations.

The number of countries in post-conflict or fragile situations (more commonly referred to as FS) represent slightly more than twenty percent of the IMF’s membership. How best to support these countries build their institutions continues to be a major concern for the IMF. In recent years, the volume of fiscal TA to FS has increased significantly, from approximately seven person years of field delivery in 2006 to nearly 30 person years of field delivery each year during the past five years (2012–2016).

The TA approach to building fiscal capacity in FS differs depending on the stage of fragility. This approach broadly takes into consideration the state of fragility: (1) midst of conflict/disaster; (2) most fragile/post conflict or disaster; and (3) fragile/stable but vulnerable. Countries often do not progress in a linear manner through these stages: they may start off in conflict/disaster, move to post-conflict/post-disaster, and then fall back into conflict or experience additional disasters. The duration of each stage varies widely across countries. The approaches described are not meant to be prescriptive or “one-size-fits-all”, but to provide a sense of the principles that guide interventions in the fiscal area at various stages of fragility.

The first stage, the immediate post-conflict/post-disaster stage, includes a focus on tax revenue collection. In this stage, targeting is on easy-to-collect taxes such as customs duties at the border and selective high-yielding excise taxes, and introducing simple organizational structures and basic processes for tax and customs administration. On the expenditure side the focus is on actions that allow the authorities to gain immediate control over the budget, including preparing an annual budget, introducing basic payment systems and controls for budget execution, and consolidating cash resources for the government to meet its immediate

payment obligations. Once countries become more stable (but still vulnerable), the objective of TA is to modernize fiscal institutions incrementally through medium-term revenue and expenditure strategies. Overall, reforms should be paced and sequenced to take into account country-specific circumstances and conditions, including absorptive capacity and initial conditions.

The synchronization between revenue and expenditure reforms is critical. In general, TA is provided in both areas at the same time. However, their relative magnitude varies depending on the starting conditions, the weaknesses in each area, and the country's absorptive capacity.

IMF TA responds to demands from IMF member countries, and is designed to support the IMF's surveillance and lending activities. In this regard, annual TA programs are planned in collaboration with the authorities and the IMF area department teams, and reflect evolving country priorities. IMF staff also coordinate TA advice and activities with other donors and TA providers. These coordinating efforts are easiest when they are country-led, which underscores the importance of political ownership for the long-term success of reforms.

IMF missions from headquarters (HQ) define overall reform strategies, whose implementation is supported by the ten Regional Technical Assistance Centers (RTACs), long-term advisors, and short-term advisors. All three modalities—missions from HQ, RTACs and advisors—also deliver workshops and other training activities to help develop capacity in FS. The IMF's Institute for Capacity Development (ICD) also offers training on fiscal issues to officials in FS.

### **Executive Board Assessment**

Executive Directors welcomed the staff paper on the review of the Fund's effort to build fiscal capacity in fragile states based on recent country experiences in delivering IMF technical assistance (TA) in the fiscal area. They also welcomed the comprehensive and balanced analysis of how the TA to fragile states differs from that to non-fragile states and the lessons that can be derived for future work in this area so as to better serve this important segment of the membership.

Directors agreed that staff's strategy to building fiscal capacity in fragile states has been broadly appropriate: first, defining and implementing the needed tax and expenditure policies; second, establishing a proper legal and regulatory framework for fiscal policy; and third, establishing an effective central fiscal authority (ministry of finance) and a mechanism for coordinating donor assistance.

Directors acknowledged that the approach taken regarding TA differs between an immediate post-conflict/post-disaster stage, and a second, more stable (but still vulnerable) stage. They agreed on the staged approach, under which the focus in the first stage on the revenue side should be on securing receipts by targeting easy-to-collect taxes, with the concurrent

introduction of simple organizational structures and basic processes to better manage revenue administration. On the expenditure side, they agreed that the focus of TA at this stage should be on actions that will enable the authorities to gain immediate control over the budget. Once a fragile state becomes more stable, they agreed that the second stage is to modernize fiscal institutions incrementally through medium-term revenue and expenditure strategies.

Directors stressed the need for differentiation of revenue and expenditure reforms across countries depending on the starting conditions, the weaknesses in each area, and the country's absorptive capacity, noting that in general, it is appropriate to provide TA in both areas at both stages.

Directors welcomed the increase in IMF fiscal TA to fragile states over the past decade, which was facilitated by rising external funding. They considered the current modalities for TA delivery to be appropriate but emphasized the need for providing training to a wider range of stakeholders to ensure the effectiveness of Fund TA. Directors agreed that ensuring that the overall reform strategies are well defined by missions from headquarters is key to coherence and effectiveness in meeting the longer-term needs of fragile states. Both long-term and short-term advisors then have a framework to guide implementation of the reform strategies. Directors appreciated the supportive role played by the regional TA centers (RTACs) in the AFR, APD, MCD and WHD regions. Ensuring good coordination with other TA providers and donors, including the World Bank, is critical. Directors emphasized that TA should be demand driven and structured flexibly to support the country's specific needs. They considered strong country ownership to be key for the long-term success of reforms. The importance of workshops and seminars, as well as other training and peer-to-peer activities, to develop capacity was also noted.

Directors recognized the considerable efforts involved in building capacity in fragile states and commended staff involved in delivering TA in often difficult and sometimes dangerous circumstances, where progress is slow. As part of future capacity development strategies, they generally agreed that increasing the intensity and duration of TA can be supported by greater use of communications technology and of short-term and long-term experts, including resident advisors, which are crucial for implementation of fiscal reforms. Directors were also of the view that increased visits by experienced staff to countries are needed to gain in-depth knowledge and provide appropriate, tailor-made support. Directors acknowledged the inherent difficulties in measuring the impact of TA on reform outcomes, both on the revenue and expenditure sides, and positively viewed staff's efforts to gauge the possible impact of TA based on the application of standardized tools such as Public Expenditure and Financial Accountability and Tax Administration Diagnostic Assessment Tool. Directors concurred that there is further scope for integrating fiscal TA to fragile states into Fund surveillance operations. Some Directors also called for similar reviews of TA provided to fragile states by other functional departments.



## BUILDING FISCAL CAPACITY IN FRAGILE STATES

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### EXECUTIVE SUMMARY

**The paper draws on recent country experience to describe the approach to designing and implementing fiscal reforms in fragile states (FS) taken in the IMF's technical assistance (TA).** In doing so, it highlights how the TA that the IMF provides to FS differs from that of non-FS, describes the trends in and modalities of TA delivery, and draws on recent experiences to derive lessons for future work.

**The approach taken differs between the immediate post-conflict/post-disaster stage, and a second, more stable (but still vulnerable) stage.** The first stage includes a focus on tax revenue collection. In this stage targeting is on easy-to-collect taxes such as customs duties at the border and selective high-yielding excise taxes, and introducing simple organizational structures and basic processes for tax and customs administration. On the expenditure side the focus is on actions that allow the authorities to gain immediate control over the budget, including preparing an annual budget, introducing basic payment systems and controls for budget execution, and consolidating cash resources for the government to meet its immediate payment obligations. Once countries become more stable the objective of TA is to modernize fiscal institutions incrementally through medium-term revenue and expenditure strategies.

**The synchronization between revenue and expenditure reforms varies across FS.** In general, TA was provided in both areas at the same time. However, their relative magnitude varied depending on the starting conditions, the weaknesses in each area, and the country's absorptive capacity.

**Missions from headquarters (HQ) define overall reform strategies, whose implementation is supported by the ten Regional Technical Assistance Centers (RTACs), long-term advisors, and short-term advisors.** All three modalities—missions from HQ, RTACs and advisors—also deliver workshops and other training activities to help develop capacity in FS.

**FAD TA provision to FS points to some key lessons, highlighting the importance of:** targeting fiscal TA to achieve fiscal stability and secure, stable and elastic revenues; setting priorities and paying attention to reform sequencing; promoting effective donor coordination; designing and implementing formal Medium-Term Revenue Strategies (MTRS) and medium-term expenditure reform strategies to help countries exit fragility; considering a more extensive TA presence and more flexible TA delivery modes; and, further integrating TA to FS into IMF lending and surveillance operations.

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## Glossary

AFR	African Department
ATI	Addis Tax Initiative
APD	Asia Pacific Department
ATAF	African Tax Administration Forum
BEPS	Base Erosion and Profit Shifting
CBF	Capacity Building Framework
CD	Capacity Development
CEMAC	Central African Economic and Monetary Community
CIT	Corporate Income Tax
CPIA	Country Policy and Institutional Assessment
CREDAF	Centre de rencontre et de recherche des dirigeants des administrations fiscales
DGD	Direction Générale des Douanes (Mali)
DIT	Dual Income Tax
DRC	Democratic Republic of Congo
ECOWAS	Economic Cooperation of West African States
EI	Extractive Industries
EME	Emerging Markets Economy
EITI	Extractive Industries Transparency Initiative
ERAP	Economic Recovery Assistance Program
EUR	European Department
FAD	Fiscal Affairs Department
FS	Fragile States
G20	Group of Twenty
GDP	Gross Domestic Product
HIPC	Highly Indebted and Poor Country
HRL	High Risk Location
HQ	Headquarters
ICD	Institute of Capacity Development
IDA	International Development Association (World Bank)
IDB	Inter-American Development Bank
IFMIS	Integrated Financial Management System
IMF	International Monetary Fund
IT	Information Technology
IPSAS	International Public Sector Accounting Standards
LEG	Legal Department
LG	Local Government
LIC	Low Income Country
LMIC	Lower Middle Income Country
LRA	Liberia Revenue Authority
LTX	Long Term Expert
LTO	Large Taxpayer Office
LTU	Large Taxpayer Unit
MCD	Middle East and Central Asia Department



MDRI	Multilateral Debt Relief Initiative
MENA	Middle East and North Africa
MIC	Middle Income Country
MNRW-TF	Managing Natural Resource Wealth-Trust Fund
MoFEP	South Sudan's Ministry of Finance and Economic Planning
MTO	Medium Taxpayer Office
MTRS	Medium Term Revenue Strategy
ODA	Official Development Assistance
ODI	Overseas Development Institute
OECD	Organization of Economic Cooperation and Development
OTA	Office of Technical Assistance (US Treasury Department)
PCT	Platform for Collaboration on Tax
PEFA	Public Expenditure and Financial Accountability
PFM	Public Financial Management
PIT	Personal Income Tax
PWT	Penn World Table
RA-FIT	Revenue Administration Fiscal Information Tool
RCF	Rapid Credit Facility
RBM	Results Based Management
RM-TF	Revenue Mobilization Trust Fund
RTAC	Regional Technical Assistance Center
SDG	Sustainable Development Goals
SEEs	Myanmar's State Economic Enterprises
SOE	State Owned Enterprise
SPR	Strategy Policy and Review Department
SSA	Sub-Saharan Africa
STX	Short Term Expert
TA	Technical Assistance
TADAT	Tax Administration Diagnostic Assessment Tool
TPA-TTF	Tax Policy and Administration Tropical Trust Fund
TSA	Treasury Single Account
UMIC	Upper Middle Income Country
UN	United Nations
VAT	Value Added Tax
WAEMU	West African Economic and Monetary Union
WB	World Bank
WCO	World Customs Organization
WDI	World Bank World Development Indicators
WEO	World Economic Outlook
WHD	Western Hemisphere Department
WoRLD	World Revenue Longitudinal Database

## INTRODUCTION

**1. During the past decade, conflict in the Middle East and Africa has intensified,<sup>1</sup> small island states in the Caribbean and the South Pacific have been ravaged by earthquakes and other major natural disasters, and several West African countries have (only recently) emerged from their worst public health crises in recent years.<sup>2</sup>** While the total number of IMF member countries that are in post-conflict or fragile situations (more commonly referred to as FS) has remained relatively stable between 2006 and 2016, how best to support them continues to be a major challenge for the IMF. FS represent slightly more than twenty percent of the IMF's membership.<sup>3</sup>

**2. Building, or re-building, FS' fiscal institutions and strengthening their fiscal capacity is of particular concern, given their key role in the functioning of the state and the economy.**

There is a rich literature (Acemoglu and Robinson 2012; Besley and Persson (2011, 2013, 2014a, 2014b), Collier (2007); Fukuyama (2004, 2011, 2014, etc.) arguing that robust and inclusive fiscal institutions are essential for state-building and economic growth.

**3. At the same time, the international context has undergone significant changes that will affect many FS for years to come:** the 2008–2009 global financial crisis has brought about a reduction in aid flows to more than a few FS (although aid to some has increased).<sup>4</sup> On the revenue side, this has been accompanied by a call from the international community for developing countries, especially those with the weakest revenue performance, to strengthen their revenue-raising capacity based on better designed tax systems and stronger revenue institutions. "Aid for trade" has become "aid for taxes paid," as reflected by the commitment of the signatories to the 2015 Addis Tax Initiative (ATI)<sup>5</sup> to double, by 2020, their assistance to developing countries to strengthen their tax systems and their administration. The vulnerability of many FS to volatile international commodity price cycles is another important reason for them to strengthen their capacity to raise non-resource revenues.

**4. On the expenditure side, developing countries, including FS, are facing greater demands to demonstrate transparency and accountability in their use of public funds—**especially countries that receive significant grant aid or that are resource rich.<sup>6</sup>

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<sup>1</sup> Melander (2015).

<sup>2</sup> World Health Organization Ebola Response Team (2016).

<sup>3</sup> Appendix I includes the list of Fragile States, non-Fragile States, and Other (High-income countries) considered in this paper. There are 39 FS and 98 non-FS, the latter low and middle income countries, for a total of 137. Appendix I also lists as "other" 54 high-income countries that are excluded from analysis in this paper.

<sup>4</sup> OECD (2013).

<sup>5</sup> The Addis Tax Initiative (2015) <http://www.un.org/esa/ffd/ffd3/commitments/commitment/addis-tax-initiative.html>.

<sup>6</sup> OECD Development Assistance Committee (2005), Extractive Industries Transparency Initiative (EITI) (2016).

**5. The last review of the IMF’s efforts to build fiscal capacity in post-conflict countries was more than a decade ago.**<sup>7</sup> That paper found that the IMF’s advice was in many ways similar to that provided to countries without conflicts, but with important nuances to reflect the realities of the post-conflict environment.<sup>8</sup> In recent years, the volume of fiscal TA to FS has increased significantly, from approximately seven person years of field delivery in 2006 to nearly 30 person years of field delivery each year during the past five years (2012–2016).

**6. The purpose of this paper is to analyze more recent country experiences, highlighting how the IMF’s TA to FS differs from that to non-FS, and derive lessons for future work.** It draws on the IMF’s extensive experience providing TA to FS in the revenue and expenditure areas. In addition to FAD advice, the IMF’s Legal Department (LEG) also provides assistance to FS in drafting laws and reforming the legal framework relating to revenue and expenditure policies, processes, and institutions. The analysis in this paper is supported by eight case studies covering five IMF regions (Africa (AFR), Asia Pacific (APD), Europe (EUR), Middle East and Central Asia (MCD), and Western Hemisphere (WHD)).

**7. This paper is organized as follows:** The next section sets the scene by describing some characteristics of FS. It then highlights revenue and expenditure trends in FS, and proceeds to describe FAD’s approach to designing and implementing fiscal reforms in FS. The main trends in FAD’s TA to FS are assessed, followed by a preliminary assessment of outcomes and lessons learned. There are six appendices clarifying specific issues discussed throughout the paper. The eight country case studies can be found in the companion piece to this paper: Building Fiscal Capacity in Fragile States—Case Studies.

## CHARACTERISTICS OF FRAGILE STATES

**8. This paper follows the same definition of FS as in previous IMF work in the area.**<sup>9</sup> This defines FS as having either weak institutional capacity as measured by the World Bank’s Country Policy and Institutional Assessment (CPIA) score (average of 3.2 or lower) and/or experience of conflict (signaled by presence of a peace-keeping or peace-building operation in the most recent three-year period).<sup>10</sup> Box 1 describes the methodology for calculating the World Bank’s CPIA score.

<sup>7</sup> Gupta et al. (2005). At that time, the term ‘countries in fragile situations’ had not been adopted by the IMF.

<sup>8</sup> In recent years, the IMF has issued several papers and a guidance note on its engagement with FS. These are summarized in Appendix II.

<sup>9</sup> IMF (2011a); IMF (2012); IMF (2015); and Gelbard et al. (2015).

<sup>10</sup> Appendix III shows the details of the CPIA sub-scores for the ‘efficiency of revenue mobilization’ and ‘budget and financial management’ aspects of the overall CPIA score for the eight case study countries. These are highlighted because they are part of the ‘public sector management and institutions’ cluster of the CPIA score, and are most closely related to the topics discussed in this paper.

### Box 1. Fragile States: Definition

**Macroeconomic administrative capacity.** This is measured using the World Bank's CPIA score against 16 criteria grouped in four clusters: economic management, structural policies, policies for social inclusion and equity, and public sector management and institutions. Countries eligible for assistance under IDA<sup>1</sup> are classified as fragile when they have a rating of 3.2 or less. The maximum score is 6.0.

**Ability to deliver security.** This is assessed using World Bank data on the presence, within the most recent three-year period, of United Nations or regional peacekeeping or peacebuilding operations. This measure of fragility spans all countries beyond those that are IDA-eligible.

**The definition of FS** used in IMF work is based on the World Bank's definition. But the IMF uses a three-year average, rather than the World Bank's annual CPIA score, to reduce the risk of countries being excluded or included in the fragile list due to temporary shifts in CPIA ratings.<sup>2</sup>

Sources: World Bank, CPIA Criteria, 2015

<sup>1</sup> IDA refers to the International Development Association, which offers concessional loans and grants to the world's poorest developing countries.

<sup>2</sup> Appendix I includes the list of the 39 countries the IMF currently considered as being FS.

## 9. At end-2016 there were 39 FS, more than half of them in Sub-Saharan Africa (SSA).<sup>11</sup>

As mentioned earlier, this paper follows the definition of FS in previous IMF work in this area. Between 2006 and 2016, 53 IMF member countries, nearly 30 percent of the total IMF membership, were classified as 'fragile' at some point. Nineteen countries have remained 'fragile' throughout the period, suggesting that it is difficult to 'exit' fragility. That said, a large number of countries—18—did manage to do so during this period. Given the heterogeneous nature of the FS, there are many different reasons why countries may have done so. An analysis of CPIA sub-scores suggests that for countries that have left fragility between 2005 and 2015 the budget and financial management component of CPIA improved significantly (e.g., a three-fold increase), suggesting that investing in improvements in budget and financial management capacity accompany the process of exiting fragility (Appendix IV). On the revenue side, an analysis of the CPIA sub-score for "efficiency of revenue mobilization" suggests that a capacity to mobilize revenues more efficiently is also associated with the process of exiting fragility. Seven of the 13 countries that exited fragility between 2005-2015 had "efficiency of revenue mobilization" sub-scores that remained above 3.2 during this period. Four countries in the 'exiting' group that started the period with scores below 3.2 improved them by an average of 40 percent by 2014-2015. Only two of the countries that exited fragility still showed "revenue mobilization" fragility in 2015, with scores below 3.2.

**10. FS are heterogeneous in their economic structure, sources and degree of fragility, and macroeconomic performance.** In addition to exhibiting macroeconomic and institutional weaknesses, countries are also designated as 'fragile' because they are in a conflict situation, under a military regime following a coup, or in a post-conflict situation where the requirements for reconstruction are significant. Other FS face natural disasters requiring large investments and

<sup>11</sup> By the same token, nearly half of the SSA countries are FS.

reconstruction budgets. Institutional weaknesses are a key element of fragility. Analyzing FS as a unified group is challenging given the country specific nature of fragility.

**11. Many FS, though not all, have low levels of economic development and are characterized by large macroeconomic imbalances (Table 1).**<sup>12</sup> In 2015, around half a billion, or approximately 7.3 percent of the world population lived in FS, which accounted for about 1.5 percent of global gross domestic product (GDP). This large gap between population and their share of global GDP points to a low level of economic development: average GDP per capita is less than half that in non-FS countries.<sup>13</sup> FS tend to have lower economic growth rates compared to non-FS, higher inflation, larger general government debt,<sup>14</sup> large current account imbalances, and high dependence on official development assistance (ODA).<sup>15 16</sup>

**12. FS are distributed across the five regions considered in IMF work but more than half are in SSA (Figure 1).** Their notable features—some of which may also pertain to non-FS, suggesting that there is not always a clear line between the two groups in terms of advice—are as follows:

**13. Many are affected by external or internal wars.** Conflicts destroy infrastructure and institutions, and result in a dramatic depletion of human capital.<sup>17</sup> The Global Peace Index produced by the Institute for Economics and Peace estimated that the cost of global conflicts in 2014 was USD817 billion (0.8 percent of global GDP). This figure is relevant for the group of FS because they accounted for 44 percent of the countries that are ranked in the lowest quintile (meaning their ‘state of peace’ is at the lowest levels) of the 163 countries included in this Index. High security risks make it difficult for donors and international agencies to assist these countries.

<sup>12</sup> The tables and figures throughout the paper do not always present data for the full 2006–2016 period, given that some data are not available for the full sample all FS, or non-FS, for the entire period.

<sup>13</sup> The non-FS group includes 98 non-fragile low- and middle-income countries.

<sup>14</sup> FS started with very high debt-to-GDP ratios during the period 2006–2007, which subsequently went down in 2014–2015. Debt-to-GDP ratios decreased in 25 of the 39 FS during the period 2006/2007–2014/2015. By contrast, debt-to-GDP ratios increased in 68 of the 98 non-FS, especially some SSA countries (Cameroon, Cape Verde, Gambia, Mozambique), some Middle East and North Africa (MENA) countries (Egypt, Jordan, Lebanon) and some Eastern European countries (Serbia, Ukraine). Public debt (in percent of GDP) in many FS declined significantly between 2006 and 2015 owing to multiple factors. Several FS (e.g., Burundi, Democratic Republic of Congo, Guinea-Bissau, Liberia, and Sao Tome and Principe), received significant debt relief under Highly Indebted and Poor Country (HIPC) and Multilateral Debt Relief Initiative (MDRI) programs. Myanmar also received debt relief during this period. Other countries (Afghanistan, DRC, Iraq, Myanmar) have graduated from immediate post-conflict situations, leading to significant base effects (with massive increases in nominal GDP). In other cases, extracting natural resources has contributed to the base effect for GDP (Eritrea, Sierra Leone).

<sup>15</sup> Note that all these differences are statistically significant at 1 percent level.

<sup>16</sup> This last characteristic may point to a strong correlation between aid and weak revenue mobilization, an issue that has been studied extensively in the empirical literature on aid and revenue mobilization. See Benedek et al. (2014).

<sup>17</sup> Institute for Economics and Peace (2014).

**Table 1. Basic Economic Trends: Fragile and Non-Fragile States, 2006–2015**

	2006–2007		2014–2015	
	FS	Non-FS	FS	Non-FS
GDP per capita (US\$) (1)	1,549.25	3,660.67	1,474.83	4,428.59
Real GDP per capita growth (%)	3.1	5.2	-0.9	2.5
Real GDP growth (%)	4.6	6.6	1.9	3.8
Inflation (%)	8.3	6.3	6.1	4.1
Debt (% GDP) (2)	78.4	41.9	44.9	49.9
Current Account Balance (% GDP)	-1.3	-3.8	-5.4	-6.6
Current Account Balance (% Exports) (3)	15.5	-14.8	-0.2	-23.0
Fiscal Deficit (% GDP)	-2.4	-0.2	2.7	3.7
Reserve Assets (% GDP)	15.2	19.8	18.5	21.0
ODA (% GNI) (4)	16.3	4.6	14.0	3.3
Grants (% GDP) (5)	9.2	1.9	4.7	2.1
No. of Countries (6)	38	93	38	93

Source: IMF World Economic Outlook (WEO) Database, IMF World Revenue Longitudinal Database (WoRLD), World Bank World Development Indicators (WDI) Database.

(1) Per capita GDP is in terms of 2010 USD.

(2) Refers to General Government Gross Debt.

(3) Excluding Timor-Leste, the average Current Account Balance (% Exports) for Fragile States would instead be equal to -28.6 percent in 2006–2007 and -22.1 percent in 2014–2015.

(4) Only 2014 values considered, due to lack of data for 2015.

(5) 2012–2013 averages instead of 2014–2015 averages, due to lack of available grant data for 2014 and 2015.

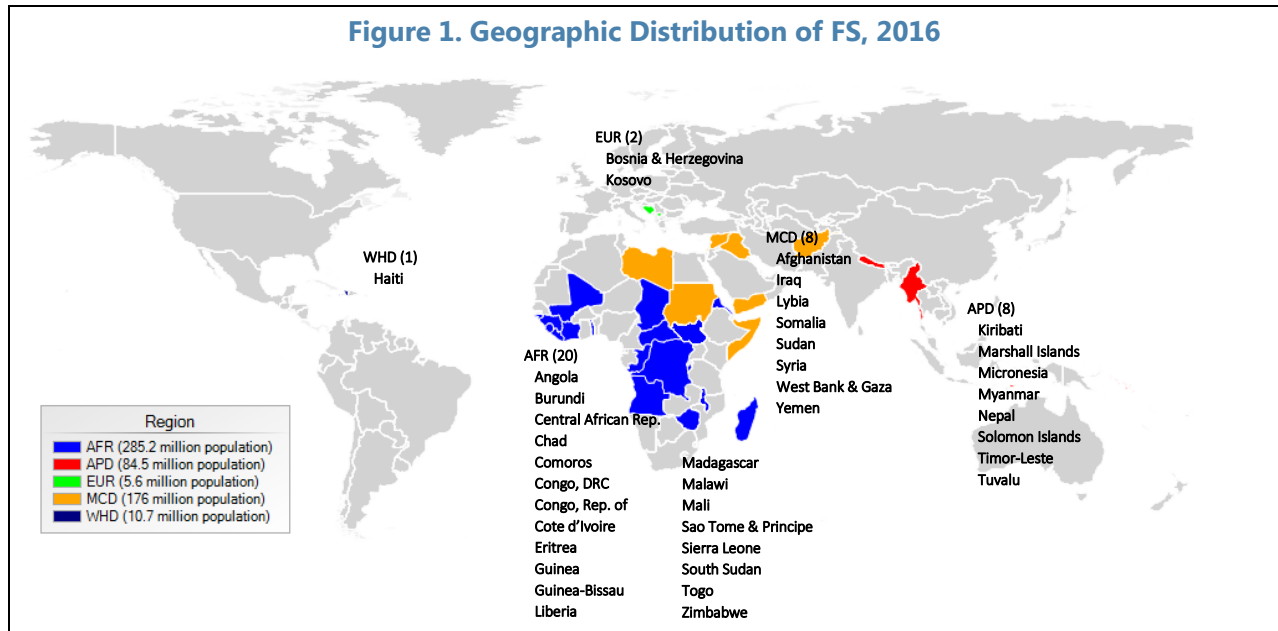
(6) Observations not available for all countries in all years, given the variables in question.

**14. A significant proportion of FS (20 percent) are particularly vulnerable to natural disasters.**<sup>18</sup> This is the case for small island FS in the Pacific, and for Haiti. The annual cost of disasters for small states is nearly two percent of GDP—more than four times that for larger countries.<sup>19</sup> This reflects a higher frequency of disasters, adjusted for land area, as well as greater vulnerability to severe disasters. About nine percent of disasters in small states (compared to less than one percent for larger states) involve damage of more than 30 percent of GDP. Greater

<sup>18</sup> Although it is the case that there are non-FS that are also vulnerable to natural disasters, suggesting that it is the combination and the intensity of the characteristics highlighted here that give rise to fragility.

<sup>19</sup> IMF (2016).

exposure to disasters has important macroeconomic effects on small states, resulting in lower investment, lower GDP per capita, higher poverty, and a more volatile revenue base.



**15. The level of corruption tends to be higher than in other countries.** One indication of this is that the 2015 CPIA scores for the following sub-clusters: “Property Rights and Rules-Based Governance” and “Transparency, Accountability, and Corruption in the Public Sector” are lower—around 2.0—for the FS that were fragile throughout the 2006–2016 period, compared to average scores of 3.0 for the FS that were not. In 2015 two thirds of the FS were among the countries with the highest corruption levels in the world, as measured by the Transparency International corruption perception index.<sup>20</sup> 23 out of the 39 FS were ranked in the bottom third of the 168 countries and territories for which these calculations were made.

**16. Poor governance and weak institutions are endemic to those FS that were fragile throughout 2006-2016.** Acemoglu and Robinson (2012) argue that the most common reason why nations fail is that they have extractive political and economic institutions, in the sense that they extract resources and hamper economic activity rather than being inclusive and providing economic incentives. Collier (2007) points to a set of traps that ensnare these countries, including civil war, being landlocked with ‘bad neighbors’,<sup>21</sup> a dependence on the extraction and export of natural resources, and bad governance. Collier argues that especially for smaller, landlocked countries, dependent on aid-flows or natural resource revenues, governance is critical. Fukuyama (2004) highlights the importance of well-functioning public institutions for state-building, and the “need to focus more closely on those dimensions of stateness that can be manipulated and built.”

<sup>20</sup> Transparency International (2015).

<sup>21</sup> Twenty percent of the 39 FS are landlocked.

**17. There is a high incidence of IMF programs among FS.** This in part reflects their weak macroeconomic performance. A comparison of FS and non-FS based on the Penn World Table (PWT) database shows that, for the period 1990–2014, real per capita GDP growth is more volatile in FS, growth is lower for FS relative to non-FS, and on average, the intensity of recessions in FS is twice that of recessions in non-FS. Twenty-five of the 39 FS (at end-2016) had an IMF program during the period under analysis (2006–2016).<sup>22</sup> This compares with 54 of the 98 non-FS (at end-2016) that had an IMF program during this same period. Nearly all of the FS IMF programs aim at protecting vulnerable households by setting a social spending floor. Many programs also contain structural reforms to improve expenditure efficiency and transparency, and include benchmarks in the areas of public financial and investment management.

## REVENUE AND EXPENDITURE TRENDS

### A. Revenue Trends

**18. The average tax revenue-to-GDP ratio in FS was below 15 percent during 2005–2014 (1 percent in Iraq and 1.4 percent in Libya) compared to 19 percent in non-FS** (Figure 2). The low average tax ratio for FS excludes extractive industry (EI) royalties and other similar non-tax revenue. In this regard, studies (Gaspar et. al., 2016) have found evidence of a ‘tipping point’: once tax-to-GDP level reach around 13 percent, there is a marked tendency for real GDP per capita to increase sharply and in a sustained manner over the following several years. This finding lends credence to the notion that tax revenue plausibly matters more than non-tax revenue to creating state capacity; EI and similar non-tax revenues are more ‘extractive’ than ‘contributive’. Recent studies also note that, ideally, countries should aim to be safely above this threshold—e.g., above 15 percent of GDP—to provide adequate and sustainable resources for growth and development. While there have been long-term increases in revenue ratios these have been modest, suggesting that FS face challenges in expanding tax revenue as a percentage of GDP, and that gains are difficult to sustain (IMF, 2012). Nevertheless, some FS have made considerable gains in expanding their tax revenues. For example, tax revenue in Liberia grew from 11.4 percent of GDP in 2004 to 19 percent of GDP in 2014, and in Mozambique from 10.2 percent of GDP in 2004 to 23.8 percent of GDP in 2014.<sup>23</sup>

**19. Sources of tax revenue are less diversified than in non-FS.** In terms of revenue structure, FS rely more on trade taxes than non-FS countries, and much less on taxes on goods and services (Figure 3).<sup>24</sup> Over time, there are stark differences in the evolution of the composition of tax revenue

<sup>22</sup> Appendix V lists the FS that have had IMF-supported programs since 2006, and the type of program.

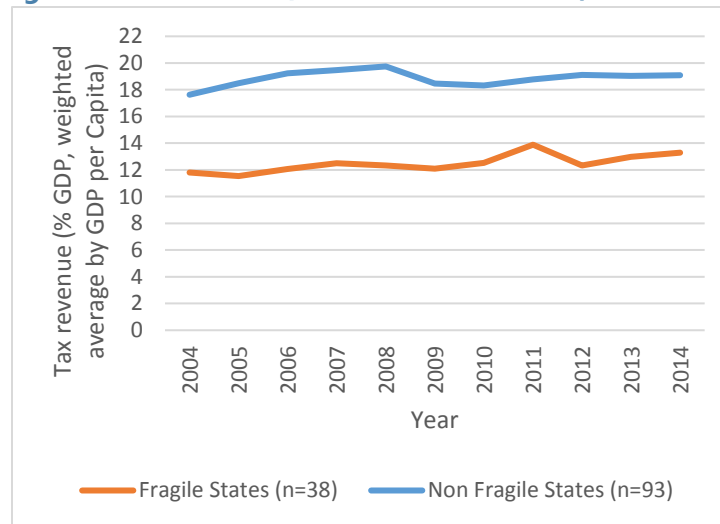
<sup>23</sup> Tax revenues from the EI sector played an important role in this increase—more so in Mozambique, where these accounted for 22.6 percent of total tax revenues in 2014, than in Liberia, where they accounted for 11.3 percent of total tax revenues in 2014.

<sup>24</sup> Figure 3 includes FS for which data for the major tax categories are available. Lack of detailed data (breakdown of tax revenues by major tax categories are missing for between half and three quarters of the fragile states sample) makes it difficult to develop a comprehensive understanding of tax revenue structures for all FS, undertake careful



between the two groups. In non-FS, tax shares have remained relatively stable over the sample period, with the exception of the decline in the share of trade taxes—compensated by an increase in indirect tax revenues, and to a lesser extent, income taxes. In FS, the share of trade taxes also declined, much more significantly, but the losses were made up primarily through income taxes, with the largest increase from the corporate income tax; taxes on goods and services seem to have played no role. This is somewhat of a puzzle: expectations are that FS would rely more on easier tax handles such as taxes on goods and services, and excises, given that they exhibit a high concentration at their collection points—in particular, customs border posts, and large companies. The data presented here suggests that the potential to do this remains untapped. Further examination of the data shows that this is particularly the case in resource-rich countries, where reliance on income taxes, and especially the corporate income tax (CIT), is much higher than in non-resource FS. Finally, the high level of external grants in FS may have contributed indirectly to this lack of diversity in FS tax revenue structures through its negative impact on total revenue.<sup>25</sup>

**Figure 2. Tax Revenue/GDP in FS vs. Non-FS, 2004–2014<sup>1</sup>**

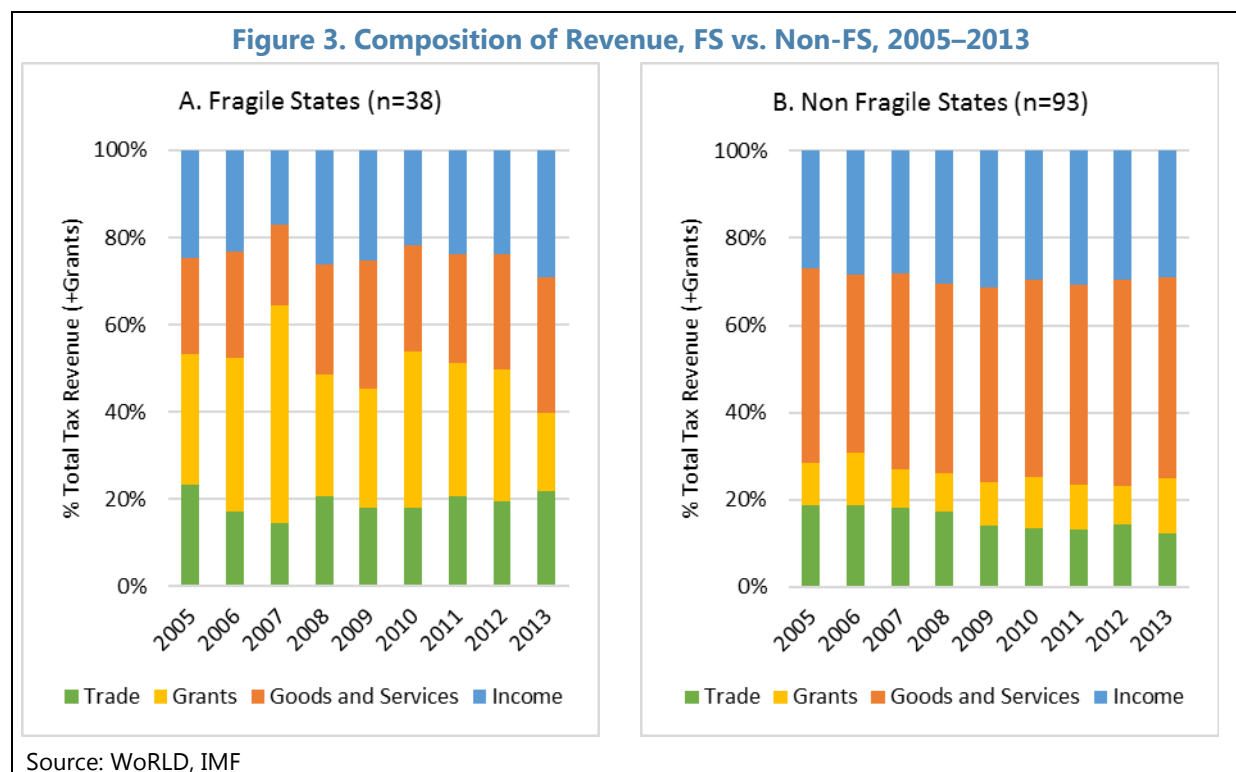


Source: WoRLD, IMF

<sup>1</sup> Tax/GDP ratios were calculated for the period 2004–2014 for the group of countries that were considered fragile at the end of the period, 2014. If one were to consider those countries that exited fragility during this period, the tax/GDP ratio for the FS group would be 1.2 percent of GDP higher.

analysis into the sources and drivers of changing composition of the revenues, and examine potential revenue impact of alternative tax instruments.

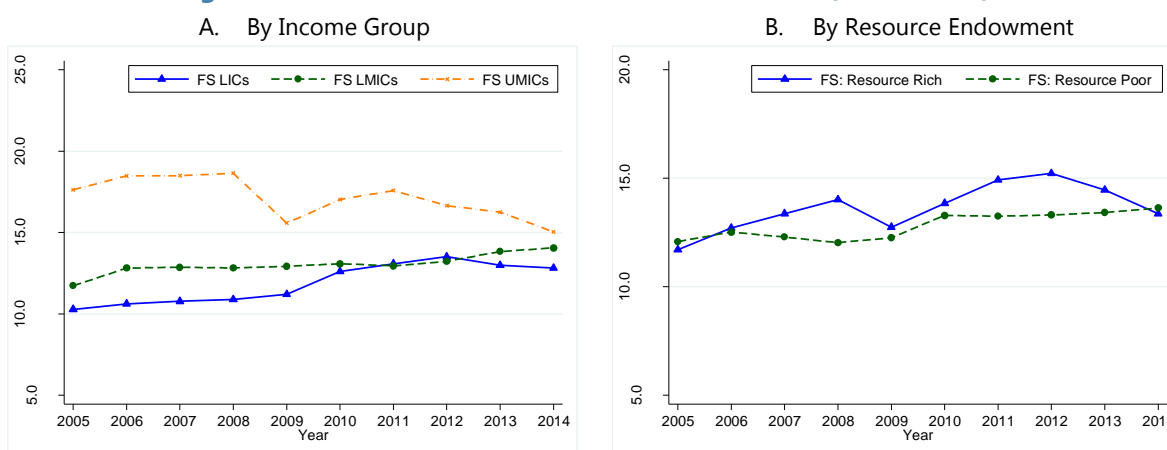
<sup>25</sup> On average, grants accounted for 48.5 percent of tax revenue for FS as opposed to 11.6 percent for non-FS during the period 2005–2013 (Figure3). While there is some support in the empirical literature that grants may provide a disincentive for countries to mobilize their own tax revenue, much less is known about how (or even if) they may affect tax revenue structures.

**Figure 3. Composition of Revenue, FS vs. Non-FS, 2005–2013**


**20. Despite some common features, the evolution of FS over the past decade shows stark heterogeneities of several kinds.** Two of these should be stressed given their likely impact on revenue mobilization going forward (Figure 4). First, of the sample of countries that are studied in this paper, FS tend to remain low-income countries for long periods—20 in the sample studied were in this position starting in 2006 through 2014. FS that graduated to middle-income status are either very small island economies or rich in natural resources.<sup>26</sup> Second, 11 FS are resource-rich countries,<sup>27</sup> with a higher level of economic development compared to their non-resource rich counterparts. However, they face the challenge of more volatile revenue, due to volatility in commodity prices. There is evidence that countries rich in natural resources tend to substitute revenue from such resources for non-resource domestic tax revenue (Crivelli and Gupta, 2014; Brun, Mansour, and Chambas, 2015).

<sup>26</sup> Low Middle Income Country (LMIC) FS include: Republic of Congo, Côte d'Ivoire, Kiribati, Kosovo, Myanmar, Micronesia, São Tomé and Príncipe, Solomon Islands, Sudan, Syria, Timor-Leste, and Yemen. Upper Middle Income Country (UMIC) FS include: Angola, Bosnia and Herzegovina, Iraq, Libya, Marshall Islands, and Tuvalu.

<sup>27</sup> "Resource-rich fragile states" here refers to Low Income Countries (LICs) and Low Middle Income Countries (LMICs) whose revenue from exhaustible natural resources comprised at least 20 percent of GDP, based on a 2005-14 average. The resource-rich FS include Angola, Burundi, Chad, Dem. Rep. of Congo, Republic of Congo, Guinea, Iraq, Liberia, Libya, Nigeria, Solomon Islands and Timor-Leste.

**Figure 4. Economic Conditions and Tax Revenues (2005–2014) <sup>1</sup>**


<sup>1</sup> Tax/GDP ratios were calculated for the period 2005–2014 for the group of countries that were considered fragile at the end of the period, 2014.

Source: WORLD and IMF Staff calculation

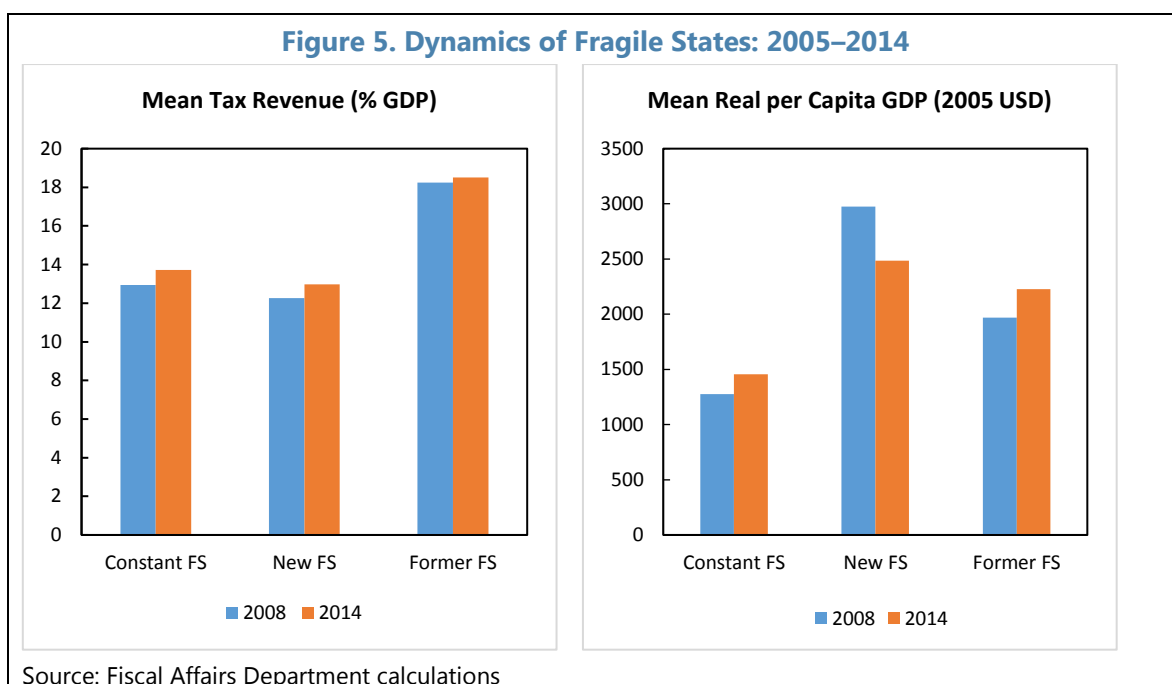
**21. Heterogeneity in FS is reflected in the duration of fragility, and the resulting economic and revenue performance.** Three types of FS can be distinguished in the sample: countries that remained fragile (Constant FS), countries that became fragile (New FS), and countries that were fragile in 2008 but left fragility (Former FS). New FS, which have a higher per capita GDP levels compared to former and constant FS (especially in 2008), have nonetheless witnessed a drastic decline in their levels of GDP per capita since 2010 (Figure 5), due to political shocks and wars.<sup>28</sup> A substantially higher tax-to-GDP ratio, despite lower income levels, seems to be associated with exiting fragility.<sup>29</sup> It is noteworthy that those states that remained fragile the whole period (“Constant FS” in the left-hand-side graph in Figure 5) performed better than new FS (“New FS” in the left-hand-side graph of Figure 5) despite having a lower per capita GDP (“Constant FS” in right-hand-side graph of Figure 5 vs. “New FS” in right-hand-side graph of Figure 5).

## B. Expenditure Trends

**22. Public expenditure levels are lower than in non-FS, especially for social spending.** Total public expenditure in FS is somewhat lower than in non-FS—29 percent of GDP compared to around 32 percent of GDP. The principal reason for this is that tax revenue levels are lower. Many of the low-income FS lack access to financial markets, and donors tend to fund a large proportion of their total expenditure.

<sup>28</sup> The sharp drop in 2011 is driven by the outbreak of civil war in Libya.

<sup>29</sup> This is consistent with the argument of Gaspar et al. (2016) above.



**23. The composition of public expenditure is different in FS, with more spending on wages and less on social benefits** (Figure 6). In many FS, expenditure on wages is much higher than in non-FS. In conflict FS, this could reflect the need to absorb combatants previously involved in armed conflicts into the military. In most FS, however, this could reflect the fact that the public sector is the major employer. This reduces the government's ability to spend on goods and services to ensure adequate provision of social services. FAD TA<sup>30</sup> has focused on effective management of the wage bill spending to ensure that the desired public services are delivered in a cost-effective and fiscally sustainable manner. It has also focused on strengthening institutions for effective and sustainable wage bill management. FS spend considerably less than non-FS on social benefits such as social assistance and pensions. Interest payments tend to be lower than non-FS countries as FS rely more heavily on concessional or grant financing.

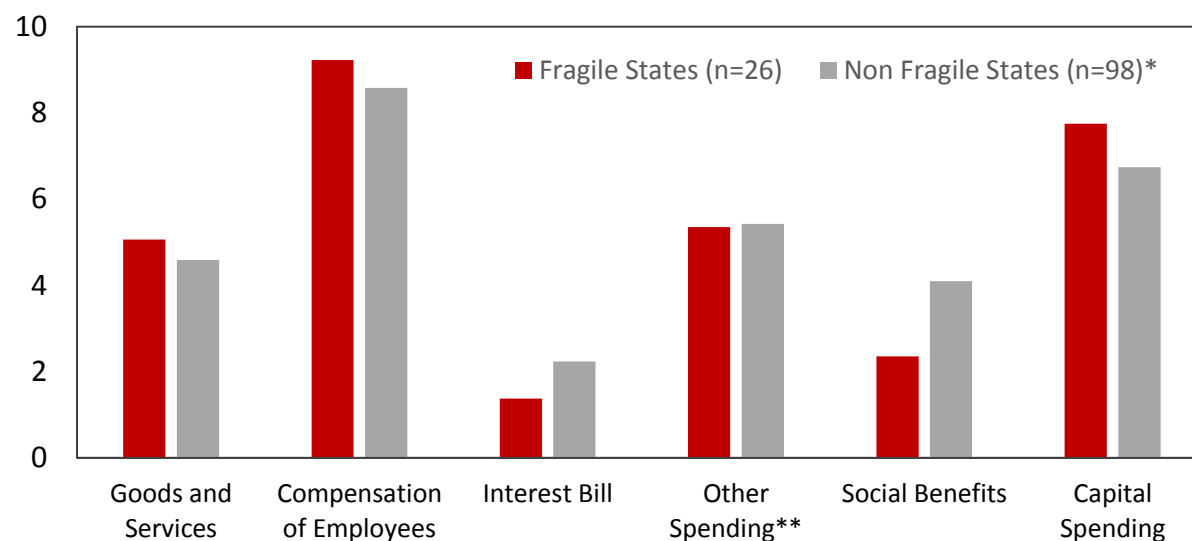
**24. Capital expenditure is higher than in non-fragile LICs, reflecting the need to rebuild damaged infrastructure, and lack of basic public services such as water, electricity, and transportation.** Capital expenditure is the second largest expenditure category, representing nearly 30 percent of total expenditure. Capital expenditure is an area of particular attention for donor support.

**25. The size and structure of public expenditure in FS is constrained by the quality of public institutions.** Beyond public resources, skilled staff and stable institutions are necessary preconditions for developing a well targeted social safety net. Only a few FS, such as Kosovo, have

<sup>30</sup> IMF (2016b)

had a social safety net in place, in this case inherited from the pre-conflict period, that could form the basis for developing a system appropriate for the new country's economic circumstances.

**Figure 6. Public Expenditure Composition in FS vs. Non-FS, 2015**  
(as a percent of GDP)



Source: WEO, Expenditure Analysis Tool.

\*Non-FS include Emerging Markets Economies (EMEs) and LICs

\*\* Other Spending might include, for some countries, capital spending and social benefits

**26. Recovery from conflict poses extreme difficulties.** In most country case studies, during the period of conflict many skilled staff overseeing budget management left because work conditions had deteriorated, the budget was no longer used as a formal instrument to regulate the use of public resources, and public funds were dispersed outside the control of the ministry of finance (Mali after the 2012 coup, and Haiti, between 2010 and 2015, are examples). In the aftermath of the conflict/disaster, public expenditure systems had to be rebuilt from scratch in an environment resistant to fiscal discipline, with widespread corruption, and without the legal framework to empower the fiscal authorities. At the same time, there is great competition for the few skilled staff from other strategic areas in the government or from donors to manage their in-country projects.

## APPROACH TO DESIGNING AND IMPLEMENTING FISCAL REFORMS IN FRAGILE STATES

**27. IMF TA responds to demands from IMF member countries, and is designed to support the IMF's surveillance and lending activities.** Annual TA programs are planned in collaboration with area department teams, and reflect evolving country priorities. TA missions often overlap with area department missions (including Article IV) in the field and provide input into their work, both during and after the mission. On occasion, FAD staff join area department missions as technical

experts to provide direct input on specific revenue and expenditure issues. Area department teams receive advice from TA staff on program benchmarks (when mobilizing revenue and ensuring effective cash management are key short-term objectives) and to identify key surveillance issues (where improving the quality of revenue collection and budget design and execution over the medium term are often crucial for macroeconomic stability and growth). Box 2 illustrates how FAD and IMF area department teams interacted in the case of Myanmar.

### **Box 2. Collaboration Between FAD and the IMF Country Team in Myanmar**

Myanmar had been isolated for 50 years and all fiscal institutions needed modernizing to complement the political and economic reforms underway. An IMF Article IV mission in January 2012 helped the authorities assess the economic issues that needed to be addressed.

**Revenue reforms.** In taxation, it noted that tax and non-tax revenue collection, at about 4½ percent of GDP in 2012, was among the lowest in the world. The bulk of government spending was financed by receipts and transfers from State Economic Enterprises (SEEs) which amounted to 16.5 percent of GDP, with most of this concentrated in the extractive industry sector. Broadening the tax base and raising non-resource revenues was thus a priority of the government. The findings of that mission were discussed with FAD and formed the basis for subsequent missions on tax policy and tax administration that took place in October 2012. The missions reviewed the fundamentals of the tax system, considered options to simplify the existing tax structure and identified measures to improve the effectiveness of tax administration. The FAD missions agreed with the authorities on the outline of a plan for sequencing reforms. This formed the basis for discussions with the IMF country team, as well as for the reform and technical assistance plans that were executed during 2013–2016 under the Tax Policy and Administration Topical Trust Fund (TPA-TTF) program. Since 2012 revenues from the major taxes (commercial tax, income tax) have increased on average over 20 percent year-on-year, and the tax-to-GDP ratio is projected to reach 8 percent in 2017–2018.

**Expenditure reforms.** The January 2012 Article IV mission also underscored the need to stop the automatic monetization of budget deficit by the central bank. This was considered critical to contain inflation. The mission also highlighted the risks to fiscal discipline stemming from the planned fiscal decentralization given Myanmar's weak public financial management. These aspects were explored in greater detail by a July 2012 FAD technical assistance mission that carried out a broader assessment of the strengths and weaknesses of Myanmar's PFM system and identified immediate reform priorities. This mission's findings fed into the authorities' medium-term reform strategy, which focused on building core PFM capabilities. A key element of this strategy was developing a treasury management capacity within the ministry of finance with a view to moving towards a more transparent, market-oriented cash and debt management system.

Source: FAD

**28. The design and delivery of TA in the fiscal area is consistent with the recent Board endorsed initiative to provide dedicated support to FS through a Capacity Building Framework (CBF).** The CBF establishes goals for institution building, identifies immediate and planned TA and training from the IMF and other development partners, and allows for fine tuning of support, where needed, based on the evolving needs of FS. A number of pilot countries (up to six in the Sub-Saharan Africa region, of which 5 are FS) will be part of this initiative starting 2017.<sup>31</sup>

<sup>31</sup> SSA countries for which CBFs have been prepared include the Central African Republic, the Democratic Republic of Congo, Liberia, Mali, and Sierra Leone.

**29. The overall approach to building fiscal capacity in FS consists of a three-pronged strategy:** (i) defining and implementing the needed tax and expenditure policies, along with basic arrangements for administering revenues and managing public finances using scarce human resources and leveraging donor assistance; (ii) establishing a proper legal and regulatory framework for fiscal policy; and (iii) establishing an effective central fiscal authority (ministry of finance) and a mechanism for coordinating donor assistance.

**30. The target areas for TA are identified by IMF HQ staff through ‘diagnostic’ or ‘strategy defining’ missions.** Revenue and expenditure missions can take place concurrently, as was the case recently in South Sudan.<sup>32</sup> LEG staff often join such missions, or undertake separate visits to work with legal teams in the ministry of finance, tax and budget departments.

**31. The strategy adopted reflects the country’s degree of fragility.** Figure 7 highlights the main characteristics of the approach to designing fiscal strategies. This approach broadly takes into consideration the state of fragility: (i) midst of conflict/disaster; (ii) most fragile/post conflict or disaster; and (iii) fragile/stable but vulnerable. Countries often do not progress in a linear manner through these stages: they may start off in conflict/disaster, move to post-conflict/post-disaster, and then fall back into conflict or experience additional disasters. The duration of each stage varies widely across countries. The approaches described are not meant to be prescriptive or “one-size-fits-all”, but to provide a sense of the principles that guide interventions in the fiscal area at various stages of fragility.

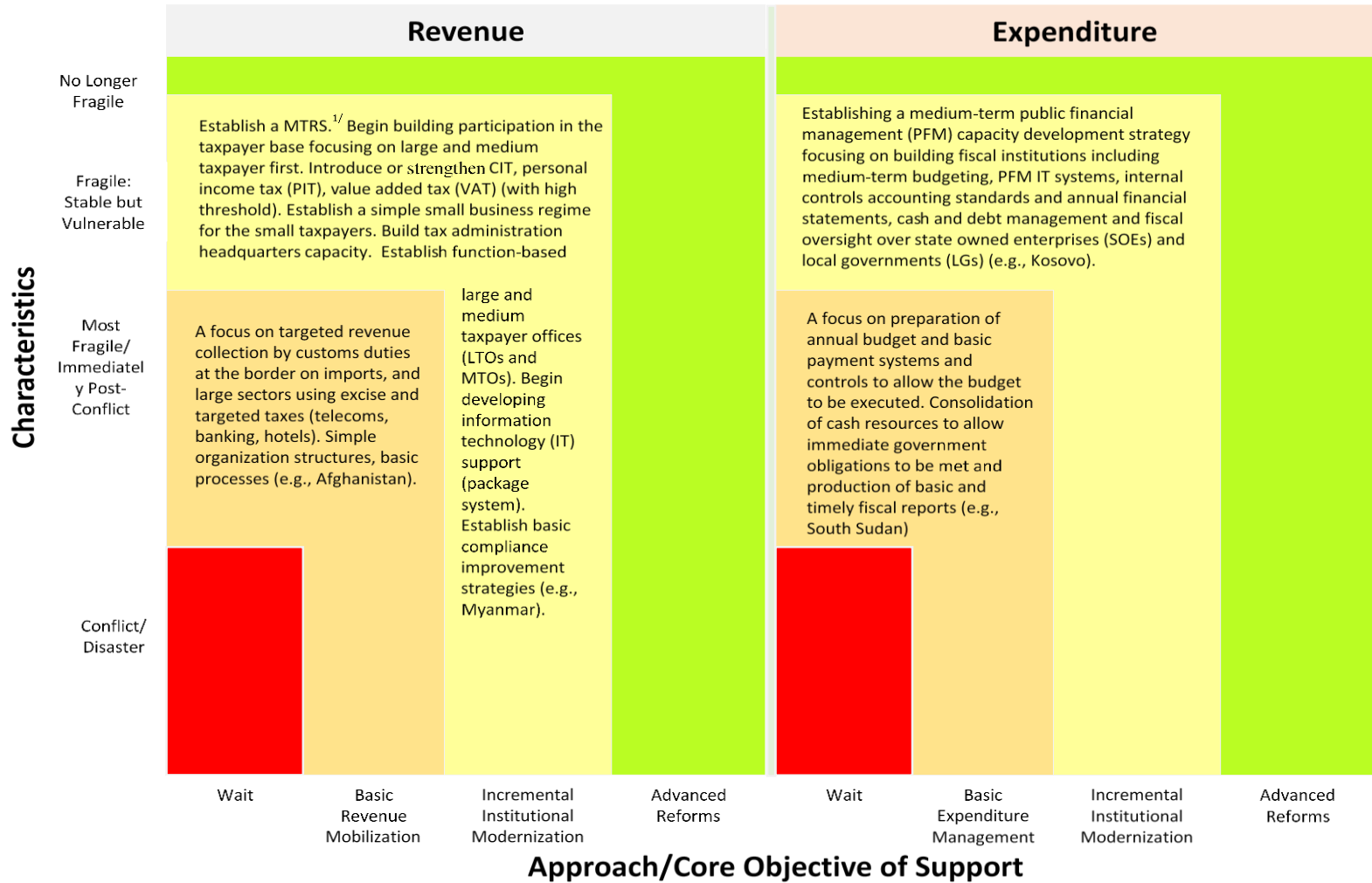
## A. Conflict, Disaster

**32. For countries that are experiencing major insecurity or political instability** (e.g., in conflict), and for which TA provision is not possible (except remotely) because of security concerns or inaccessibility after a major natural disaster or public health crisis, the approach is to ‘wait’ (red quadrant) until conditions allow for a direct engagement. Waiting need not mean inactivity, however. The IMF seeks ways to support the FS at this stage through the use of alternative TA modalities such as video conferencing and off-site missions, as in the case of Afghanistan, Guinea, Liberia, Mali, and Yemen. In Liberia, against all odds, the Liberia Revenue Authority (LRA) was launched on July 1, 2014, at the height of the Ebola crisis. Travel restrictions during this time meant that IMF staff had to find innovative ways to continue delivering technical assistance, including by video-conference, telephone, e-mail, and off-site meetings.

**33. Security risks impose significant constraints on TA delivery in countries that the UN has assessed as ‘high risk locations’ (HRLs).** The tragic death in 2014 of the IMF’s Resident Representative in Afghanistan makes such risks very real. Box 3 describes some of the implications for TA missions of security-related risks, what can be improved, and some of the limits of remote TA delivery.

<sup>32</sup> The timing of TA missions responds to the authorities’ requests and depends on the availability of the appropriate experts; an effort is made not to overburden the authorities with multiple missions.

**Figure 7. FAD’s Main Policy Responses for Fragile States at Different Levels of Fragility, Revenue and Expenditure**



<sup>1</sup> MTRS refers to a Medium-Term Revenue Strategy, which is discussed in greater detail later in this section.

The discussion that follows focuses on countries at the three different stages of fragility, as indicated in Figure 7.



### Box 3. Dealing with Security Risks and Delivering TA Remotely

Key constraints for TA delivery:

- Additional cost of security: consultants, armored vehicles, and ‘secure’ hotels.
- Uncertainty regarding the actual conditions on the ground, including identifying the safest hotels from a security standpoint.
- Difficulty recruiting short-term experts for missions to HRLs, especially if travel is required inside the country or to remote areas to visit tax and customs offices.
- Difficulty recruiting long-term experts; once they are in a country, resumption of conflict means that they cannot remain on site, and cannot be easily reassigned or retained indefinitely.

What can improve: <sup>1</sup>

- Once on the ground, missions could receive more up-to-date and practical security briefings from locally-based security consultants or local UN personnel if the mission security consultant accompanying the mission is not from the mission location.
- Travel services could be more proactive in informing mission members who are in the field about airport security issues, and alternative routing, should air travel routes be affected.
- Mission travelers and overseas-based consultants should ensure that their contact information is accurate so that in an emergency they can be easily contacted to ascertain their well-being.

Remote TA delivery can ensure continued contact with country authorities, but has limits:

- Video-conferencing, telephone, and e-mail contact are not as effective as face-to-face interactions with officials.
- IMF staff cannot review actual operations or ‘real time’ procedures, especially key for some tax and customs operations (for example, review of cargo clearance procedures) and management of budget execution.

<sup>1</sup> A recent major improvement has been the addition of an intensive off-site course that is designed to prepare staff on how to handle potential security risks in HRLs.

## B. First Stage Reforms

### Revenue Design

**34. A fundamental revenue-side question for policymakers in FS is how tax policy can help countries manage or end fragility.** This raises the important issue of taxation and state-building, which has received increased attention in the literature in recent years (Brautigam et al. 2008; Everest-Phillips 2010). This literature emphasizes the importance of political engagement<sup>33</sup> and inclusiveness, accountability and transparency, and equitable and simple tax systems.

**35. The IMF’s extensive TA experience, as discussed in the case studies, suggests that the trade-off among these objectives is difficult.** In practice, simplicity and neutrality should be the overriding principles in the design of revenue systems in FS, especially in the early stages of fragility—such as in post-conflict countries, and after significant natural disasters. At these stages, achieving equity in fiscal policy is best left primarily to expenditure policies; lack of tax administration capacity, and income levels, make it difficult and very costly to pursue income

<sup>33</sup> Political engagement comes out as a key factor in fiscal reforms in nearly all case studies.

redistribution objectives from progressive tax rates on individuals' incomes, or wealth taxes.<sup>34</sup> It is noteworthy, however, that these are not detached from some of the other revenue policy principles. For example, there are linkages between neutrality and horizontal equity, and simple taxes are more transparent than complex ones. Where a simple tax is believed to be generally distortionary (such as import duties or taxes on gross transaction values), its cost may be minor relative to the potential benefits of state-building and ending fragility. Moreover, the distortions caused by taxes depend on market conditions: a highly-regulated market that generates locational rent may justify the use of certain taxes (such as specific taxes on telecommunication companies), which may not be desirable or possible under competitive market conditions.

**36. In a first stage, the primary focus of revenue policy and administration is on the design of simple taxes that require low administrative capacity.** These (simple taxes) have a number of desirable features that make their collection relatively easy, while preserving neutrality. First, their base is large, highly concentrated in a small number of companies, and relatively inelastic. Second, simple taxes are less prone to evasion, through base erosion schemes. This means a preference for taxes based on "gross values", such as turnover or import values. Customs tariffs are natural candidates, and so are turnover taxes on companies in general, such as ad-valorem royalties in the resource sector,<sup>35</sup> and minimum turnover taxes which can act as back-stop to profit taxes (e.g., Mali).<sup>36</sup> These can provide the basis, in a later stage, for adoption of an effective VAT. Simple tax legislation also reduces the likelihood of tax disputes in FS that lack the judicial capacity to handle such cases. Finally, for domestic taxes, the economic activities generating the tax base should be within the reach of the authority of the state. This reduces the difficulties for the tax authorities to reach out to remote areas, especially in large countries, where security issues or weak state authority make tax collection risky and costly (e.g., Afghanistan).

**37. In addition to these characteristics, a simple tax is one that does not require complex legislation.** This means that the tax administration should be able to rely on simple regulations or application rules, short tax forms, minimum information requirements from taxpayers, and minimize the scope for disputes that might be escalated to the general court system. The latter is particularly important in FS, where the judicial system is weak, and may be prone to political manipulation. Taxpayers often go to court to delay paying taxes, a tactic which is not different from that in many non-FS but that can be particularly costly in FS that urgently need to collect tax revenue.

**38. The case studies show that countries in extreme fragility (mostly post-conflict) have relied extensively on simple taxes.** For example, Afghanistan has a sales tax that allows some deductibility of tax on input (mainly imported intermediate goods). South Sudan implemented a simple single-stage tax, at the manufacturing level and on imports. Whether or not to progress from

<sup>34</sup> However, some limited form of real property taxes may be possible, and is advisable, especially as a financing source for local governments.

<sup>35</sup> Mansour and Swistak (2017) provides evidence that resource-rich LICs (a broader group than FS) have favored the use of resource royalties (and not the CIT or rent taxes) to increase their revenue take from this sector.

<sup>36</sup> An example of a minimum tax is the minimum tax of 1.1 percent of turnover in Cameroon. This is independent of any VAT that taxpayers may be liable for.

a sales tax to a VAT in FS has been a matter of debate, given that the VAT has minimum administrative requirements that several FS lack; at the same time, working towards adopting a VAT can be a way to prepare for meeting such requirements.

**39. Setting up basic administrative procedures for the tax and customs administrations that can have the highest revenue impact in a short time is crucial.** This entails establishing basic administrative processes such as registration, filing, and payment for the major taxpayers and taxes. This approach was followed in South Sudan, for example, where the focus of advice before the recent resumption of conflict was on establishing the basic rules and processes in the key compliance areas (registration, filing, and payment of taxes); strengthening the large taxpayer office (LTO) and customs operations at the largest port to secure the greatest proportion of tax revenue; and, implementing simple procedures and automated systems.<sup>37</sup> In Myanmar, the tax administration reform strategy focused initially on larger taxpayers, in order to secure a large percentage of tax revenue and to lay the foundations for progressive strengthening of the tax administration.

**40. Ensuring the continuity of basic operations in the face of crisis and uncertainty can protect against revenue collapses.** In Mali, the 2012–2014 crisis had only a minor impact on revenue collection largely because of the resilience of the tax and customs departments. The March 2012 coup resulted in the pillaging of the customs administration, Direction Générale des Douanes (DGD), and numerous customs offices, including information technology (IT) systems and vehicles. Imports declined by 16 percent in 2012 because of the Economic Commission of West African States (ECOWAS) embargo and the conflict in the north of the country, which forced the administration to move staff to the south. In this critical context, the DGD acted to ensure continuity of operations and the collection of taxes and duties; it opened temporary offices, required use of procedural manuals, and installed a back-up server.

**41. Setting up a basic organizational structure for the tax and customs administration is key.** In South Sudan, this process started with transferring the customs administration from the Ministry of the Interior to the Ministry of Finance and Economic Planning.<sup>38</sup> In Liberia, reforms in revenue administration that started in 2006 included the re-design of the organizational structure of the tax administration, which laid the basis for the establishment of the LRA in 2014.

**42. An early focus on obtaining accurate information on the taxpayer base is the foundation for sound tax administration.** In Myanmar, while the reform strategy focused initially on larger taxpayers, it aimed to broaden the tax base, by both increasing the number of registered taxpayers and improving compliance with tax obligations, while minimizing the cost of complying with these obligations.

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<sup>37</sup> The authorities of South Sudan collected a mere 1.1 percent of GDP in nonoil revenue in 2011–2012 (at independence). This subsequently increased to 2.4 percent of GDP in 2012–2013, but dropped to 1.8 percent in 2013–2014, during the civil conflict. Nonoil revenue increased again to 3.1 percent of GDP in 2014–2015 and is estimated to have reached 6.1 percent of GDP in 2015–2016. This increase could have been greater if peace had prevailed.

<sup>38</sup> In practice this transfer has not fully occurred, in part due to lack of commitment and a plan for dealing with former combatants who make up majority of customs staff.

## Expenditure Design

**43. On the expenditure side, the focus of reform strategies during the early stages is on easy-to-implement measures which do not overburden the limited capacity available.** Quick wins are important to show what is possible at this critical stage; they can help increase the authorities' confidence and encourage further reforms. The strategy includes:

- Consolidating cash resources in an account controlled by the treasury at the central bank to pay for priority expenditures.
- Putting in place capacity to prepare a comprehensive cash-based annual budget covering all entities of the central government. This is then accompanied by restoring basic fiscal controls through cash-based expenditure management, equipping the ministry of finance with the legal powers to define how the expenditure chain will operate and provide operational guidance to line ministries and other government agencies.
- Developing capacity to produce basic fiscal reports on the execution of budget, to ensure accountability to the public and donors and to help fight corruption, as this reduces the opportunities to divert resources from where they are intended and most needed. In South Sudan, for instance, TA focused on budget execution control, accounting and reporting systems, including monitoring and reporting on accumulation of payment arrears, development of macro-fiscal analysis capacity, and putting in place the necessary institutional framework for a comprehensive budget planning and preparation process to be established.
- In the short to medium-term, drafting and adopting appropriate legislation to support the reforms. In the case of post-conflict situations, in the initial stages partial amendments to existing PFM legislation could be adopted by eliminating war-time exemptions from financial regulations and piloting and rolling-out prioritized reform measures. An annual budget law could also be used for this purpose.

## C. Second Stage Reforms

**44. For countries that have moved out of immediate fragility, the objective of TA is to modernize fiscal institutions incrementally through medium-term revenue and expenditure strategies.** TA is often delivered through medium term projects supported by long-term or peripatetic experts. For countries in this category the TA approach may be similar to that adopted for low-income countries, with close attention paid to the sequencing of reforms to reflect low, but gradually improving, administrative capacity.

## Revenue Design

**45. The IMF has been devoting increasing attention to the value for developing countries, including FS, of adopting more explicit MTRS to modernize their tax systems and their administration and increase revenues significantly.**<sup>39</sup> This approach, which is still at an initial stage and in the process of being developed more fully, is more holistic, in the sense that it includes legal, policy, and administrative reforms. A key element, perhaps the most challenging in some FS, is securing country authorities' strong, public, and medium-term commitment (five to ten years) to the announced strategy. Such a strategy would also help coordinate donor activities in an increasingly active field. The main elements of an MTRS are highlighted in Box 4 below.<sup>40</sup> This approach is consistent with the focus of, and commitments made, during the 2015 UN Financing for Development Conference and the Addis Tax Initiative, with the revenue-related commitments being as follows: participating providers of international support will collectively double their technical cooperation in the area of domestic revenue mobilization and taxation by 2020, and partner countries restate their commitment to step up domestic resource mobilization as a key means of implementation for attaining the UN's Sustainable Development Goals (SDGs) and inclusive development. Subsequently, the Platform for Collaboration on Tax (PCT) was established as a joint initiative between the IMF, the OECD, the UN and the World Bank, in April 2016 to enhance collaboration between international organizations working on tax matters, including on capacity development (CD) issues.<sup>41</sup>

**46. As countries reduce fragility, by improving institutions and the role of the state in society, tax design can move to slightly more complex stages, and address equity issues more directly.** The main policy tool for promoting equity is the personal income tax, a revenue source that has increased in recent years in FS. Kosovo, for example, expanded the use of income taxes in recent years. However, in most LICs, it remains largely confined to withholding on wages at the level of employers, and primarily from public service employment. Investment income is largely untaxed, partly because of low savings rate, but also because high-income individuals can effectively hide their wealth, often in foreign countries with bank secrecy laws and low tax rates.<sup>42</sup>

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<sup>39</sup> It is worth pointing out that the MTRS approach is not just for FS.

<sup>40</sup> There are currently a few FS that can be described as having the elements of an MTRS. For example, in the case of Myanmar, work is ongoing on a medium-term strategy to reform the tax system and engage with TA providers and donors under the umbrella of this reform strategy. FAD has been in the lead of supporting the government to formulate and support implementation of this strategy, in close partnership with other TA providers (notably the WB and the US Treasury Office of Technical Assistance (OTA)).

<sup>41</sup> Platform for Collaboration on Tax: Concept Note, April 2016.

<sup>42</sup> A forthcoming FAD Technical Note: Revenue Administration: Implementing a High-Wealth Individual Compliance Program, discusses the administration of high-net wealth individuals in greater detail.

#### Box 4. Core Elements of an MTRS

- A broad consensus on the level of revenue mobilization effort for the medium-term (5–10 years) with due consideration to the poverty and distributional implications of the associated measures.
- A comprehensive reform plan for the tax system, reflecting country circumstances and the state of institutional capacity:
  - A redesign of the policy setting to meet the revenue goal.
  - A reform of the revenue agencies to properly administer the policy setting and to achieve a high level of taxpayers' compliance to meet the revenue goal.
  - A strengthening of the legal framework to enable the policy redesign and administration reform, including by balancing revenue agencies' powers and taxpayers' rights.
- A country's commitment to a steady and sustained implementation, notably by securing political support and resourcing.
- Secured financing for the CD effort (technical assistance and training) to support the country in overcoming domestic constraints to formulate and implement an MTRS effectively.
- Agreement among TA providers on the respective roles they will play.

#### 47. Two recent developments may alleviate these constraints, and allow some FS to improve the taxation of individuals.

- The 'dual income tax (DIT)', which has been adopted in a number of advanced countries, provides a coherent approach to the taxation of personal income in lower capacity countries (Bird and Zolt, 2010). Under a DIT, wage income is taxed at a progressive rate, and capital income is taxed at a single rate, usually at the lowest marginal rate on wage income. This is often how, *de facto*, the PIT works in lower income countries, though with a patchwork of treatment for different forms of capital income: the DIT offers a way to systematize and more effectively enforce this approach. Furthermore, both the wage tax and most capital income taxes (other than the corporate tax) can be collected through final withholding, provided that the tax base has a simple design. For example, a wage tax that allows for a general deduction, and no itemized deductions, can be withheld at the level of the employer, thus requiring less administrative efforts than if the wage earners had to file a tax return.<sup>43</sup>
- Developments in international taxation can prove valuable for FS and low- income economies. One strand is the international push for relaxing bank secrecy laws around the world, and strengthening exchange of information (automatically, in due course, for developing countries that are not financial centers); this can provide a strong handle to address evasion by the wealthiest. Another strand in the Group of Twenty (G20)/Organization of Economic Cooperation and Development (OECD) Base Erosion and Profit Shifting (BEPS) project, aimed at curtailing tax

<sup>43</sup> This is already the case in many African countries, for instance, where wage earners do not have to file a tax return provided they have no other sources of income, such as multiple wages and income from a business.

avoidance by multinationals.<sup>44</sup> Country-by-country reporting, for instance, can provide valuable insights into the tax affairs of multinationals operating locally, though subject to strong conditions required to provide such information. Taking advantage of these important developments requires, of course, capacity that may exceed that yet available to many FS.<sup>45</sup>

**48. Another key component of a more equitable tax system in FS is the taxation of small and micro-enterprises.** Their tax treatment should be geared towards easing their transition into the ‘standard’ tax system, and creating a sense of “fairness” by having all citizens contribute to financing government activities. This can involve simple levies on turnover, at a rate high enough to encourage transition into the tax system, but not so high as to encourage concealment—a difficult balance. FS should resist the (unfortunate but frequent) policy and administrative practices of extending complex tax rules to small and micro-enterprises on the ground that they operate primarily in the informal economy—income concealed in the formal sector often tends to be more significant than the total income that would be subject to tax in the informal sector.<sup>46</sup>

**49. Other noteworthy reforms in the second stage includes the introduction, or strengthening, of broad-base consumption taxes, notably the VATs.** With proper design, VATs can work well in FS that are relatively stable—e.g., Kosovo and Mali. In terms of efficiency, their design may depart, however, from that recommended for VATs in high-income countries. For example, the IMF has typically advised a relatively high registration threshold, and the use of tax exemptions in limited cases as opposed to lower rates—e.g., Liberia. While many countries have followed advice on the threshold, experience with VAT exemptions is mixed, and multiple VAT rates are less uncommon today than they were in the early 2000s. Moreover, there are cases where the transition from extreme fragility to less extreme fragility can take a long time, during which advice on whether countries should introduce VAT, and its key design features, should be reconsidered. For example, IMF advice in Afghanistan and Haiti on VAT design evolved over the years, when it became clear that changes in political and security conditions were very slow, and affected their administrative capacity to operate a VAT in the domestic economy.

**50. A key challenge is to start building the capacity for the headquarters offices of the tax and customs administrations to define basic strategies, plan and monitor core operations, and oversee support functions such as IT and human resources.** In the aftermath of the devastating 2010 earthquake in Haiti, IMF advice (starting 2012) has focused on clearly delineating the tax administration’s headquarters and operational functions, ensuring that the headquarters units are focused on the main tax administration functions, and that the operational offices are organized by taxpayer segments. However, the function-based organizational structure has not been approved or

<sup>44</sup> For more information on the OECD BEPS project: <http://www.oecd.org/tax/beps-about.htm>

<sup>45</sup> It also requires a legal framework (such as tax treaties) for exchange of information, as well as the ability to safeguard the confidentiality of information.

<sup>46</sup> Keen (2015) provides a good overview of the measurement, trends, and drivers of different types of tax compliance.

implemented, reflecting weak strategic management and high turnover of the tax administration's senior management—recently three tax administration directors were appointed in one year.<sup>47</sup> Starting in 2012, Liberia demonstrated its commitment to institutional reform by approving legislation to establish a revenue authority, and a transition team was formed under strong leadership. An area in which advice and training has been provided is strengthening the capacity of headquarters staff and defining the organization's strategies. Liberia is also a good example of the importance of sequencing reforms. The authorities have expressed an interest in introducing a VAT as a way of modernizing their tax system. FAD advice has been to instead begin by strengthening fundamental tax and customs operations, which is challenging in itself during a period in which considerable attention has been placed on establishing the new revenue authority (in the midst of the Ebola crisis), before introducing the VAT.

**51. Establishing function-based Large Taxpayer Offices (LTOs) and Medium-sized Taxpayer Offices (MTOs) is another important consideration.** These offices often serve as pilots for introducing basic core procedures such as taxpayer registration, filing and payment monitoring—and help ensure that the bulk of tax revenues are monitored closely. Once established, they can be rolled out to other tax offices and other taxpayer segments. In Liberia, reflecting IMF advice in the decade after the conflict, the LRA has established an LTO, along with departments that focus on monitoring the compliance of medium, small, and micro taxpayers. Starting 2015, a long-term expert (LTX) has been providing hands-on support to strengthen the operations of the LTO, with an emphasis on improving the tax audit function, including auditing complex sectors such as telecoms and banking.

**52. The design and implementation of an IT system to support the core processes described above is an essential next step** to ensure core procedures are known and standardized across the organization, and to allow the tax administration to begin producing periodic operational and management reports. In most of the case study countries—certainly Haiti, Liberia, Mali, Myanmar, and South Sudan, IT systems require expansion and upgrades or need to be implemented from scratch (South Sudan).<sup>48</sup>

**53. Establishing basic compliance improvement strategies** for individual taxes and/or different taxpayer segments, is critical. Technical support to the tax administration in Kosovo focused on strengthening core tax administration functions (debt collection, audit), managing large taxpayers, and tailoring administrative activities to specific tax risks (synonymous with designing compliance improvement strategies). Building trust and cooperation with taxpayers became a priority of the new compliance improvement approach. These reforms have helped improve revenue

<sup>47</sup> The 2015 IMF Board Paper: Current Challenges in Revenue Mobilization: Improving Tax Compliance, identifies high turnover of senior staff, weak HQs, inadequate and unstable financing, and unwieldy office networks as obstacles to effective revenue administration performance in many countries.

<sup>48</sup>The IMF has recently issued three Technical Notes (IMF 2017a, 2017b, 2017c) which provide practical guidance to country authorities on IT issues relevant to tax administrations. These notes are primarily for tax administrations that have no technology to manage their core tax processes, or their technology is limited and outdated.



yields and achieve a cost-effective use of resources. Indeed, tax compliance management by the Kosovo Tax Administration is now considered as regional best practice.

## Expenditure design

**54. On the expenditure side, the focus is on establishing a medium-term strategy to build fiscal institutions.** Usually the strategy is defined with the help of an HQ diagnostic mission, which assesses the current situation and prepares an action plan for the next three to five years. On many occasions the diagnostic mission is in the form of a Public Expenditure and Financial Accountability (PEFA) assessment. The strategy's main components include:

- *Establishing a medium-term budget framework that takes into account the impact of policies over the longer-term.* The objective is to ensure that budget appropriations in future years are consistent with meeting the government's medium-term fiscal objectives given the expected level of available resources.
- *Implementing PFM-related IT systems that support the budget both in terms of planning and implementation.* This can be the first step in introducing an integrated financial management information system (IFMIS), considering country implementation capacity. Too frequently, complex, resource intensive solutions have been implemented with inadequate planning or oversight and a lack of political commitment—all pre-requisites for successful implementation. Well-designed solutions that consider capacity constraints have the best chances of success (e.g. Kosovo, Afghanistan).
- *Ensuring the creation of an internal control framework to manage the budget execution and reporting process.* Building capacity to reduce budget overruns and unauthorized expenditures is a core element of second stage reforms. Payment arrears are a common feature of FS caused, to a certain extent, by the absence of a robust internal control framework.<sup>49</sup> Introduction of commitment controls to regulate the pre-cash stages of the expenditure process is a crucial element of efforts to prevent the accumulation of payment arrears, to be accompanied by efforts to improve the accountability of budget institutions for execution of the budgets under their control.<sup>50</sup>
- *Developing accounting and reporting standards in accordance with international practice.* Once a basic fiscal reporting system has been established, the next phase is to introduce a reporting framework that complies with international standards in terms of coverage, and comprehensiveness. Preparation and implementation of a chart of accounts that meets these standards is a key element of second-stage reforms. The reporting framework should

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<sup>49</sup> The absence of a credible budget also contributes to the accumulation of arrears.

<sup>50</sup> IMF (2014).

adequately cover all levels of government and state-owned enterprises to ensure that a full picture of the public finances is available.<sup>51</sup>

- *Strengthening cash and debt management arrangements.* This includes the gradual establishment of a treasury single account (TSA), a comprehensive electronic government payment system, developing cash planning capacity, introducing a debt recording and reporting system, and developing an integrated cash and debt management capabilities.<sup>52</sup>

**55. Kosovo is an example of the second stage of PFM reforms.** Following the country's independence in 2008, the government produced a comprehensive and integrated PFM reform plan for which the IMF provided specific support in a diverse range of areas such as cash management, expenditure arrears management, and the design and implementation of a credible fiscal rule.

**56. Once PFM reforms make progress, a new overarching PFM law could be introduced to cement the results of the reform and move to more advanced PFM practices.** A comprehensive PFM law typically includes provisions that regulate: the roles and responsibilities of the various actors in the budget process; the process and timeline surrounding the development of the fiscal framework and the preparation and approval of the budget; budget execution procedures, management of debt and cash; accounting and fiscal reporting; and ex-post control and audit functions.<sup>53</sup> More recently, overarching PFM legislation typically includes provisions that require governments to be fiscally responsible and manage fiscal risks. However, a legislative framework at this level of comprehensiveness requires a high level of capacity for even partial implementation.

**57. Unfortunately, it is not uncommon for country authorities to want to skip the first stage and jump directly to adopting a comprehensive PFM law based on advanced country experiences.** The problem with this approach is that a fragile country will have great difficulty implementing a sophisticated PFM law with demanding fiscal responsibility and transparency provisions. The inability to implement legislation fully can undermine its credibility. Therefore, in the case of FS, it is better to keep legislation concise, focusing on those areas that can be implemented in the short to medium-term, and introduce detailed secondary regulations that can be activated as capacity increases and processes and procedures evolve.

**58. The IMF has been active in advising FS on subsidy reform, but more generally expenditure policy support has tended to be provided when basic systems and institutions are in place.** Energy subsidy reform has often been complemented by technical assistance to reform social safety nets and fiscal decentralization. For example, in Haiti and Mali the target was to reduce the pressure on the budget from fuel subsidies, establish an automatic price mechanism, and put in place a better targeted subsidy scheme. In Kosovo, the emphasis was on reforming social pensions

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<sup>51</sup> IMF (2011b)

<sup>52</sup> IMF (2011c)

<sup>53</sup> IMF (2010)

and benefits through an overarching reform program. Advice was provided on fiscal decentralization with a view to devolving revenue and expenditure decisions to the local level.

## D. The Synchronization Between Revenue and Expenditure Reforms

**59. The synchronization between revenue and expenditure reforms varies across FS (Figure 8).** TA advice has favored a coordinated approach between these reforms. For example, establishing a centralized Treasury account is key for ensuring the accurate accounting and reporting of tax revenue flows to the Treasury, and enabling the tax administration to reconcile tax liabilities with payments. This was the case in Haiti, Liberia, South Sudan, Timor-Leste, and several other case study countries. In all countries except one (Kosovo) TA was provided in both areas. However, their relative magnitude varied depending on the starting conditions (or the weaknesses in each area) and the country's absorptive capacity. For example, in South Sudan, relatively more TA was provided on the revenue side, reflecting the very low tax to GDP ratio at independence and the uncertainty regarding EI revenue flows. In Liberia, the balance tipped in favor of revenue TA after the LRA was established, reflecting the authorities' focus on recovering from the post-Ebola revenue decrease (subsequently, these reforms have been supported further by the assignment of a resident advisor whose work has focused on improving large taxpayers' compliance). In Timor-Leste, the early focus was on establishing the Timor-Leste Revenue Service. Once the tax administration was up and running (2001–2002), the emphasis shifted to the effective management of the country's substantial oil and gas wealth. In Haiti, more TA was provided in treasury management, in particular, to establish a TSA, reflecting the authorities' urgent need to manage reconstruction resources efficiently following the 2010 earthquake and subsequent shocks, including recent hurricanes. In all cases, how much revenue and expenditure TA is provided depends importantly on a country's absorptive capacity: the lack of a basic infrastructure, IT systems, qualified staff and management teams, all mean that TA may need to start slowly and ramp up as counterpart teams develop and are able to absorb advice.

## E. Using Tools to Identify TA Needs

**60. Tools such as the PEFA and the TADAT<sup>54</sup> can help identify common TA needs.** The PEFA and TADAT scores for the FS are lower compared to those for low-income and emerging market countries (Figure 9).<sup>55</sup>

<sup>54</sup> The standardized PFM assessment tool is called the Public Expenditure Framework Assessment, or PEFA. For more, see: <https://pefa.org>. On the revenue side the tool is the Tax Administration Diagnostic Assessment Tool, or TADAT. More detail can be found at: <http://www.tadat.org>. The PEFA framework has been in place since 2001, while the TADAT framework is much newer—with the first pilots undertaken in 2013/2014.

<sup>55</sup> In the case of TADAT, care should be taken in interpreting the results as the sample size for FS is still small.

**Figure 8. Mix Between Expenditure and Revenue TA, 2000–2017**



Source: FAD

**61. The PEFA assessments (of which there are many more compared to TADATs) confirm that the areas in which TA is being provided are the right ones.** For example, the spider graph on the top of Figure 9 side shows that the lowest scores for the FS relate to budget credibility (which reflects the effectiveness of budget execution), management of arrears, and budget accounting and reporting. These are areas in which the IMF is providing TA to the FS—as discussed in more detail below.

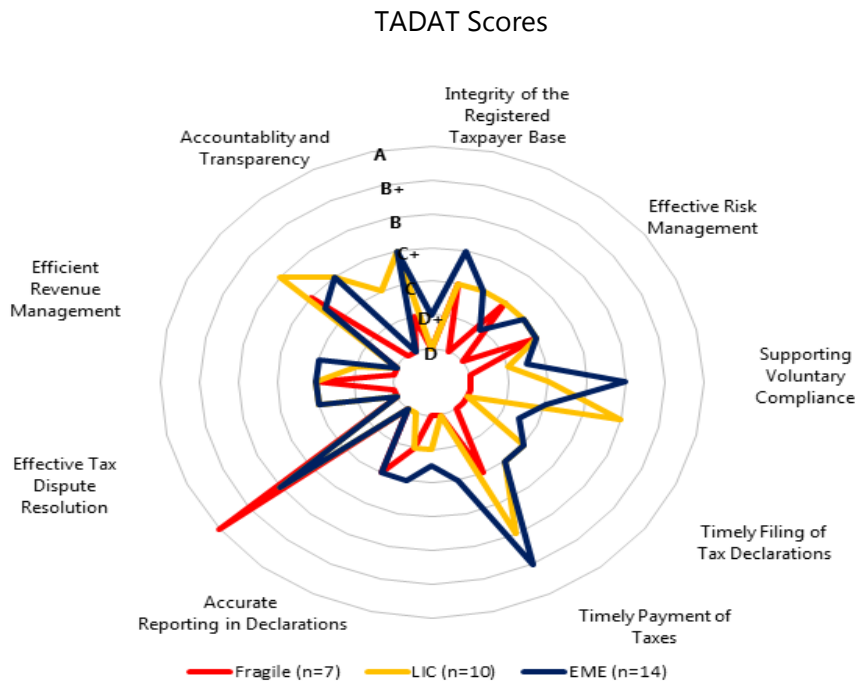
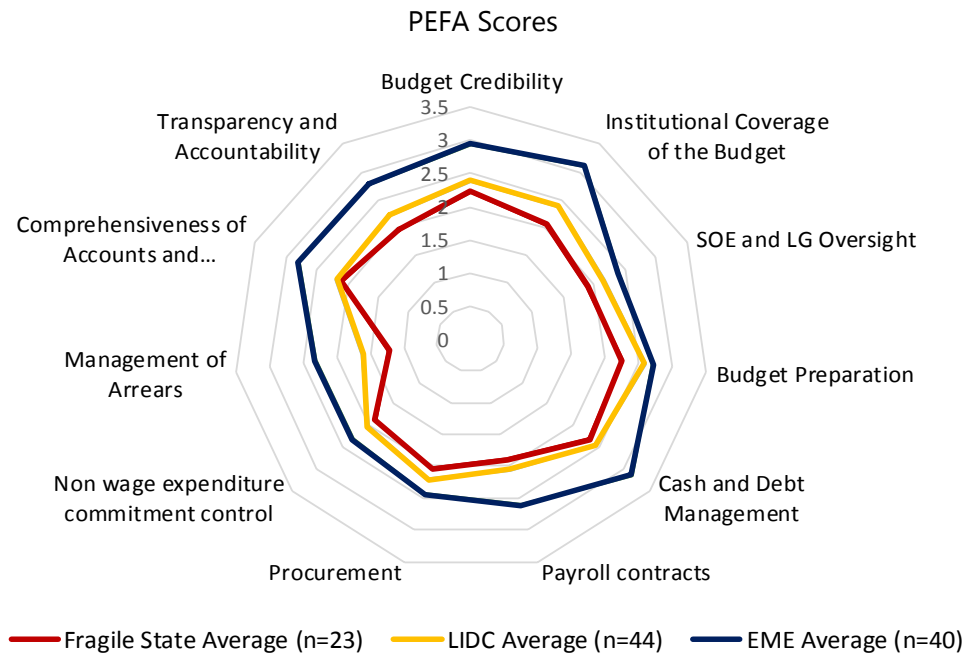
**62. TADAT remains too new to have many assessments to draw on, and there are no repeat TADATs yet.** Based on the assessments undertaken to date, the areas with the lowest scores (D) are timely filing and payment of taxes, and efficient revenue management, which refers to tax revenue accounting, timely payment of refunds, and provision of data for revenue forecasting. Some FS have scored well on the legal framework for resolving tax disputes, but this does not necessarily mean that this framework is administered effectively (Figure 9, bottom chart).

## F. Focus of Revenue and Expenditure TA in the Case Study Countries

**63. The focus of IMF TA in revenue and expenditure in the FS confirms that assistance is being targeted at the weakest areas, including those identified through PEFA and TADATs.** To illustrate this, figures 10 and 11 provide a more granular view of the main areas of fiscal TA for the case study countries. In the revenue area (Figure 10), the focus of TA has been on strengthening excise taxation and EI fiscal regimes,<sup>56</sup> rationalizing tax expenditures, and strengthening core operations in tax and customs administration (core tax operations include the weak areas identified by the TADATs, including timely filing and payment of taxes and efficient revenue management.) The TADAT does not assess the status of customs administration, so the main areas of focus of customs TA do not correspond to areas of weakness identified by a TADAT assessment. On the expenditure side (Figure 11), TA is focused on annual budget preparation, budget execution, cash management, and reporting—which correspond to the areas with the lowest PEFA scores (greatest weaknesses) in the FS.

<sup>56</sup> For more on the tax treatment of oil, gas, and minerals, see *The Taxation of Petroleum and Minerals: Principals, Problems and Practice* (IMF, 2010), which provides theoretical and practical guidance in this area.

**Figure 9. Average PEFA and TADAT Scores for FS Compared to Low-income and Emerging Market Countries**



Sources: IMF staff and TADAT secretariat

**Figure 10. A Granular View of IMF Revenue TA in the Case Study Countries**

		Afghanistan	Haiti	Kosovo	Liberia	Mali	Myanmar	South Sudan
Tax policy	Income/business taxes	Primary	Not a key	Secondary		Primary	Primary	Secondary
	VAT		Not a key			Primary		
	Indirect taxes	Secondary						
	Property taxes			Not a key				
	Sales taxes / Excises	Primary		Primary				Primary
	Rationalizing tax expenditures/tax incentives		Secondary	Secondary	Secondary	Primary	Primary	
	El taxation	Primary	Primary	Primary	Primary			
	Informal sector taxation		Not a key				Secondary	
Tax administration	Other (Tax Policy Unit, drafting legislation)		Secondary		Secondary		Secondary	
	Core processes (legal/operations)			Primary	Primary	Secondary	Primary	Primary
	IT-related issues				Secondary		Primary	Secondary
	LTU	Primary	Primary	Primary	Primary	Primary	Primary	Primary
	Segmentation / risk management		Secondary	Secondary		Secondary	Primary	
	Integration with customs			Not a key				Not a key
Customs administration	Organization/functions/Basic set up		Primary		Primary		Not a key	Primary
	Core operations		Primary				Secondary	Primary
	Introducing risk based processes	Secondary					Primary	
	Post-clearance audit	Secondary					Secondary	

	Primary revenue source
	Secondary revenue source
	Not a key source of revenue

Source: IMF

1/ Primary revenue source refers to taxes or administrative initiatives that generate the most revenue as a proportion of total revenue. Secondary revenue source refers to taxes or administrative initiatives that generate tax revenues, but less than the primary sources.

2/ Core processes and operations in tax administration refer to: ensuring the integrity of the taxpayer database, providing taxpayer services, ensuring compliance with filing and payment obligations, administering audit and other verification programs. For customs, these refer to: trade facilitation and service initiatives, control of importers' and exporters' reporting and payment obligations, the application of customs controls during the clearance process, and the enforcement of customs laws through audit and anti-smuggling programs.

**Figure 11. A Granular View of IMF Expenditure TA in the Case Study Countries**

PFM area	Topics	Afghanistan	Haiti	Kosovo	Liberia	Mali	Myanmar	South Sudan	Timor Leste
Budget preparation	Annual Budget preparation								
	MTEF/MTEF								
	Performance Budgeting								
	Fiscal Rules								
Budget execution	Basic budget controls over cash and ability to pay								
	Commitment controls								
	Arrears								
	IFMIS								
Cash and debt Management	Availability of comprehensive info on govt bank accounts								
	TSA								
	Cash forecasting								
	Debt management								
Reporting	Bank reconciliation								
	Basic budget exec.-acc., report.								
	CoAs								
	IPSAS cash								
	Other (IFMIS)								
Other	Public Investment Management								
	Fiscal risks management								
	PFM legal framework								
	SOEs oversight								
	Fiscal decentralization								

■ Core areas  
■ Other areas

Source: IMF

## TRENDS IN FAD TA

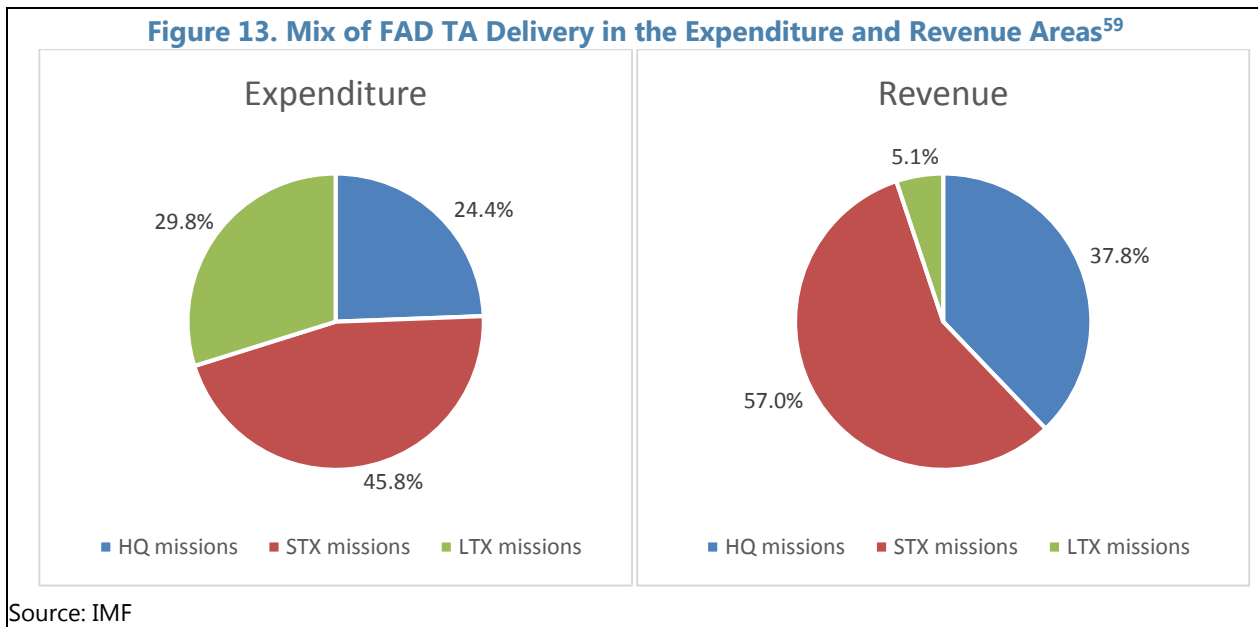
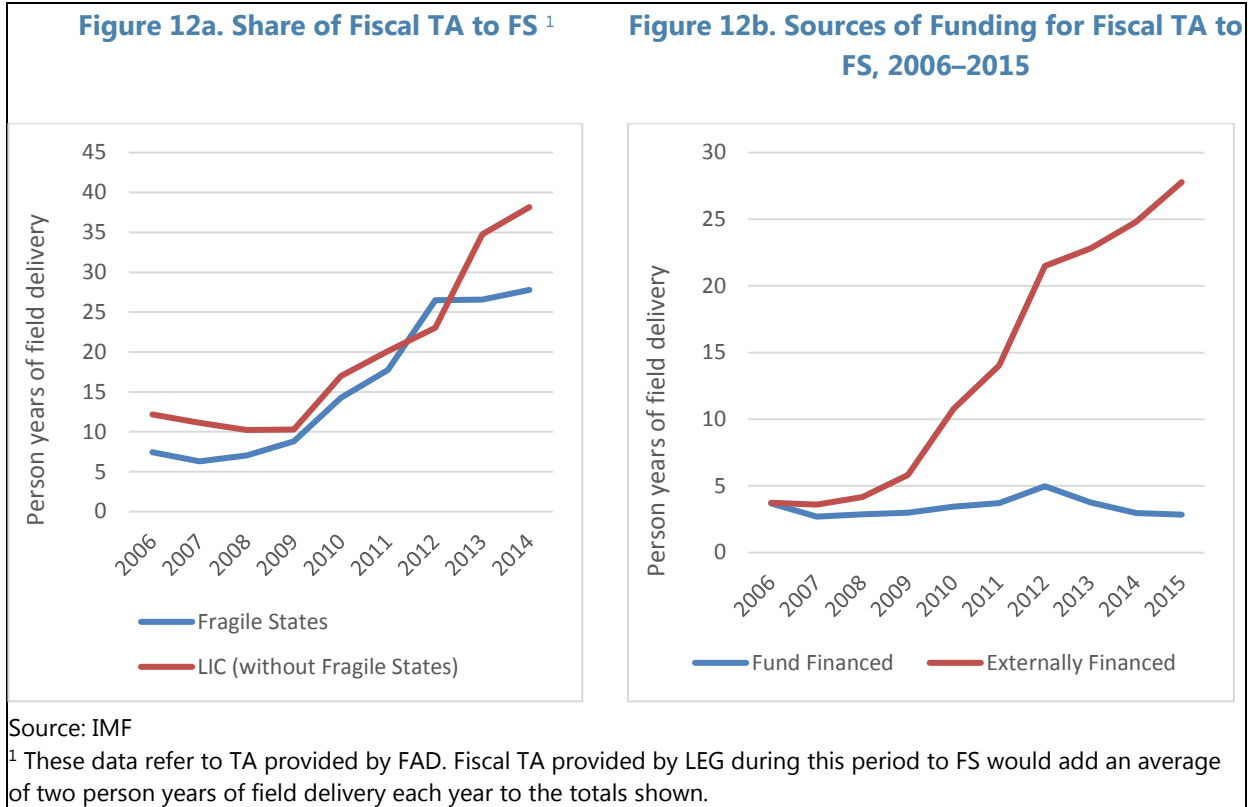
**64. Fiscal TA to all LICs, as well as FS, has increased during the past decade, made possible by rising external funding.**<sup>57</sup> (Figure 12a and 12b).

**65. The IMF missions from HQ define overall reform strategies, while the ten RTACs, long-term advisors, and short-term advisors support implementation of these strategies.**<sup>58</sup> TA from headquarters is around one-third of total TA that FAD delivers in both revenue and expenditure areas (Figure 13). A critical role of HQ staff is backstopping RTAC and short- and long-term experts to ensure that overall TA and training actively supports implementation of FAD-recommended strategies.

<sup>57</sup> An important funding source is multi-donor trust funds such as the TPA-TTF, its successor, the new Revenue Mobilization Trust Fund (RM-TF), and the Managing Natural Resources Wealth Trust Fund (MNRW-TF). The RM-TF is supported by the following current and prospective partners: the governments of Australia, Belgium, the European Commission, France, Germany, Japan, Korea, Kuwait, Luxembourg, the Netherlands, Norway, and Switzerland. More information: [http://www.imf.org/external/np/ins/english/pdf/RMTF\\_Program\\_Document.pdf](http://www.imf.org/external/np/ins/english/pdf/RMTF_Program_Document.pdf). The MNRW is supported by Australia, the European Commission, Kuwait, the Netherlands, Norway, Oman, and Switzerland. For more information: <http://www.imf.org/en/Capacity%20Development/trust-fund/MNRW-TTF>. In addition, there are number of bilateral funding sources including from the governments of Belgium, Canada, Denmark, Japan, and Switzerland.

<sup>58</sup> This approach is followed in all FS and LICs.





<sup>59</sup> "Revenue" refers to tax policy and revenue administration. "Expenditure" includes expenditure policy and public financial management.

**66. The mix between long-term and short-term experts (LTXs and STXs) is different in the revenue and expenditure areas, with expenditure using more resident advisors compared to revenue.** One reason for this is that PFM reforms typically require interventions across a greater number of agencies. Further, donors often require assurance on behalf of their governments that donor funds are being used in an effective and transparent manner. The IMF seeks to draw on local expertise when recruiting experts: two-thirds of the resident revenue advisors and one-half of the resident PFM advisors in SSA come from countries in the region.

**67. All three modalities—HQ missions, LTXs, and STXs—also deliver workshops, seminars and other training activities to develop capacity.** This includes resident advisors in the IMF’s RTACs in four regions (APD, AFR, MCD and WHD), who provide support to nearly all FS. This arrangement offers opportunities for officials to learn from peers and creates incentives for them to implement more sophisticated reforms.<sup>60</sup> The IMF’s Institute for Capacity Development (ICD) offers training on fiscal issues to officials in FS—as described in Box 5 below. In addition, the recently approved Revenue Mobilization Trust Fund includes a training module to support training activities in tax policy and administration. Officials from FS who participate in TADAT assessments generally receive training in the TADAT methodology before the assessment starts.

#### Box 5. IMF Training on Fiscal Issues in FS

In recent years, the IMF has sought to increase training on fiscal issues in FS to help future leaders rebuild institutions and cope with immediate crises. Training groups of officials on macroeconomic and fiscal issues complements more technically-focused TA, and builds sustainable institutional capacity over the long term.

IMF training on fiscal issues includes courses on Budget Formulation and PFM, Combatting Fiscal and Customs Fraud, Management of Oil and Natural Gas Revenues, Macroeconomic Management and Fiscal Policy, Medium-Term Expenditure Frameworks, and Fiscal Transparency and Fiscal Risk Management.

Attendees in IMF courses covering fiscal issues increased from 1372 to 3714, or 171 percent, between 2013 and 2016. Over the same period attendees in all IMF courses increased 82 percent. During this period, the proportion of attendees from FS has fallen, from around 22 percent of total in 2013 to around two percent of total in 2016. This drop may be attributable to instability and capacity constraints, and highlights the difficulties in building capacity in these countries.

The expansion of on-line learning at the IMF has the potential of benefitting more officials in FS. As long as internet connections are maintained, on-line learning enables officials and citizens to pursue training even during periods of interrupted travel. On-line learning reaches a broad audience beyond government officials and thus helps disseminate training more widely than face to face teaching.

Source: ICD

<sup>60</sup> In this regard, the role of regional organizations is important. For example, the West African Economic and Monetary Union (WAEMU) and the Central African Economic and Monetary Community (CEMAC) have provided excellent access to countries such as Guinea, Guinea Bissau, and Mali on the implementation of PFM directives. CEMAC has supported the adoption of international customs standards by its member countries. Regional tax organizations such as the African Tax Administration Forum (ATAF) and CREDAF (Centre de rencontre et de recherche des dirigeants des administrations fiscales) offer training and peer-to-peer activities for tax officials from FS.

## Coordinating TA with other donors and TA providers

**68. FAD TA teams invest considerable time and effort in coordinating TA advice and activities with other donors/TA providers** in a country before, during, and after the mission takes place. But coordination is a complex task that is made easier when country authorities are clearly leading coordination efforts, when donor/TA agencies are working to a single plan with clear objectives, and when there are donor coordination groups in a country. The active role that the head of Liberia's Revenue Authority has played in recent years in coordinating donor activities has been critical to the success of tax administration reforms there. The informal PFM working group that was set up in South Sudan with representatives of the IMF and ten other development partners helped coordinate activities from this large group. Donor coordination is a big challenge given the number of players; there are at least 35 donor agencies that provide some type of technical assistance in tax and customs administration to the SSA countries. In this regard, the concept of a MTRS discussed previously would provide a robust framework for coordinating multiple donor activities, especially in countries with considerable TA needs. In time, the PCT should also provide a venue for discussing TA activities among the IMF, the World Bank, the OECD, and the UN, with additional collaboration from the Inter-American Development Bank (IDB), the World Customs Organization (WCO), and perhaps others. The July 2016 PCT report referred to earlier offers general reflections on how to make capacity building and other types of support more effective, with many of the proposals as applicable to FS as to LICs in general.

**69. Cooperation with the World Bank is an important component of the IMF's technical assistance work.** IMF staff liaise closely with their counterparts in the World Bank, both at the HQ level and in the field, on policy issues and the day-to-day implementation of TA. World Bank staff participate in IMF strategy meetings (and vice versa), and steering committees of its trust funds. This allows both institutions to discuss and coordinate country reform priorities, technical assistance programs, and modes of collaboration. In several countries, the IMF designs overall fiscal reform strategies and World Bank projects provide support to implement key aspects of these strategies. There is also inter-agency collaboration on research projects and publications.<sup>61</sup>

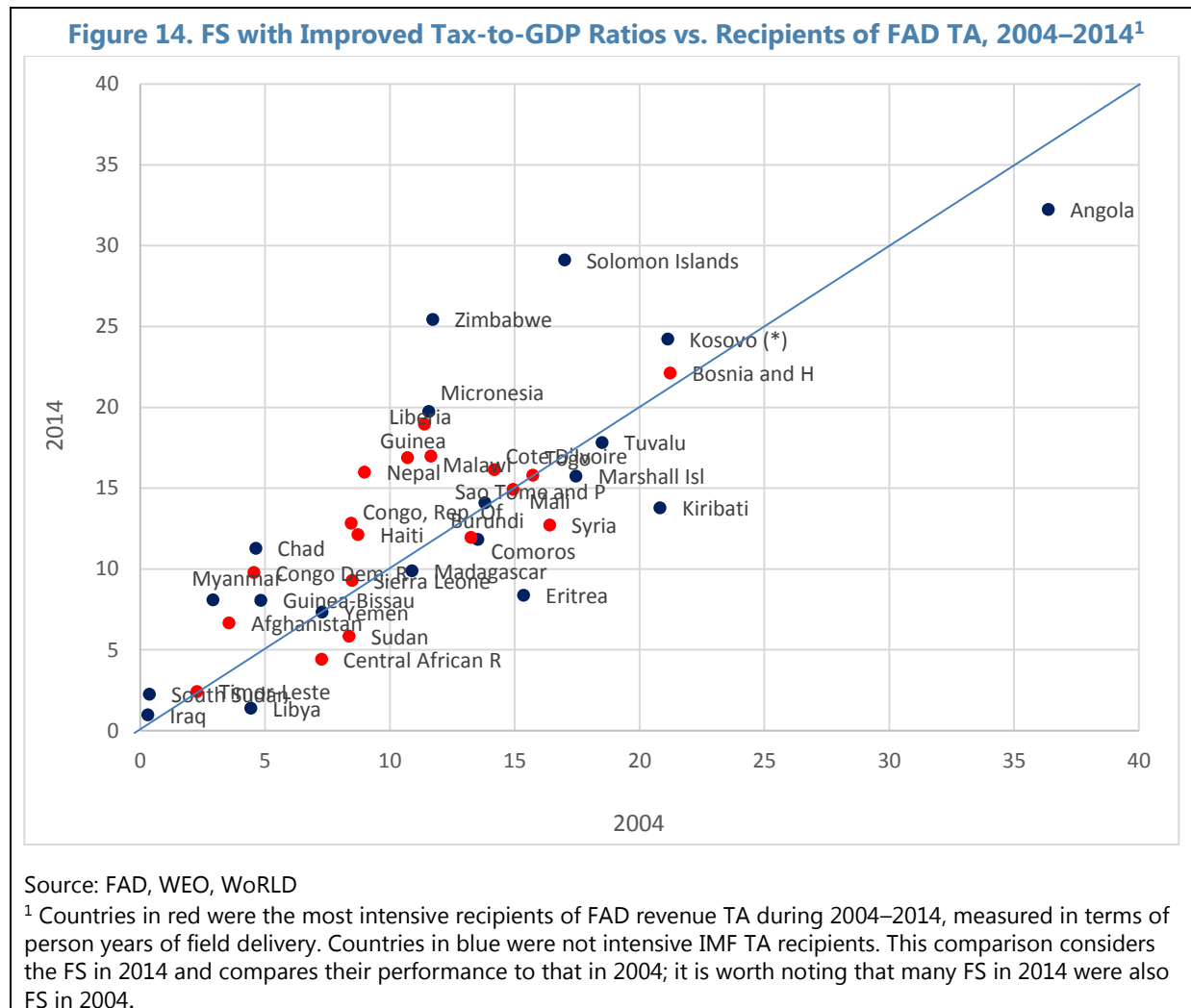
## PRELIMINARY ASSESSMENT OF OUTCOMES

**70. There are well-known limitations to measuring the impact of TA in general, and in particular in FS,** not least because it is difficult, if not impossible, to isolate the effects of technical assistance on revenue and expenditure outcomes from other factors such as the overall performance of the economy.

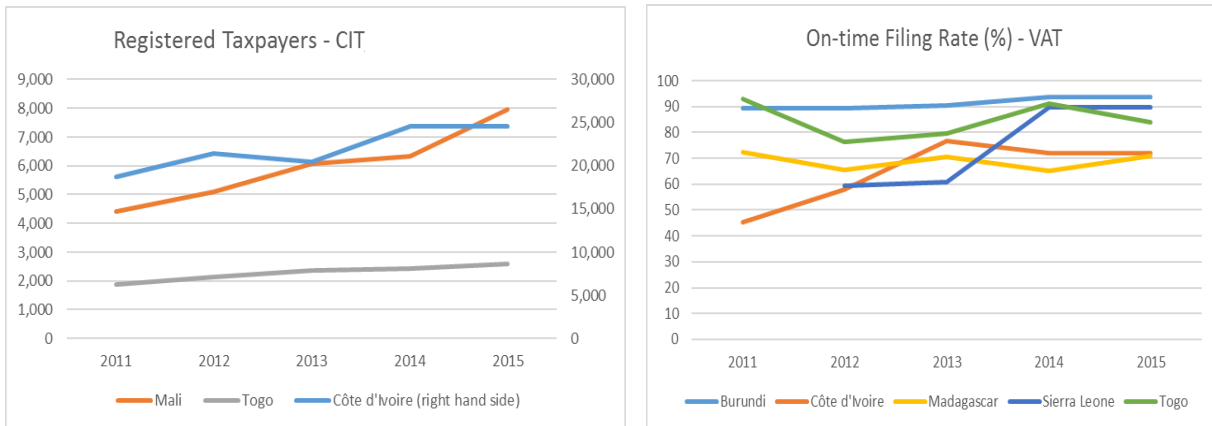
**71. That said, FS with improved tax-to-GDP ratios during 2004–2014 have been the most intensive recipients of IMF revenue TA.** Eleven out of the 19 FS with improved revenue performance during the 2004–2014 period accounted for almost 70 percent of IMF TA provided to

<sup>61</sup> An example is the Handbook on Administering Fiscal Regimes for Extractive Industries (2014).

FS in tax and customs administration during this period (intensive TA recipients are highlighted in red in Figure 14).



**72. Although data are still scarce, there are some preliminary indications that improvements in selected tax administration performance indicators have had a positive effect in terms of revenue outcomes for selected FS.** Data that some FS have reported through the Revenue Administration Fiscal Information Tool (RA-FIT), suggest that improvements in the accuracy and comprehensiveness of the taxpayer register, and on-time filing for the value-added tax, have occurred at the same time as revenue ratios have risen in Cote d’Ivoire, Mali, Togo and Sierra Leone (Figures 15a and 15b). Granular data of this type for FS is scarce: only eleven FS provided data to RA-FIT that was considered to be of acceptable quality. Within this small sample, nearly 40 percent reported positive trends in the two indicators highlighted, which coincided with improved revenue performance.

**Figure 15. Registered CIT Taxpayers and On-Time Filing Rates for the VAT**

Source: Revenue Administration Fiscal Information Tool

**73. Revenue conditionality in IMF programs does not appear to have a significant impact on revenue outcomes in FS, at least during the program period.** Increasingly, revenue conditionality in IMF programs in general is being drawn from fiscal TA provided by the IMF, reflecting that countries are drawing on this technical advice to formulate their reform strategies in the revenue area. In countries where institutions are relatively stronger, IMF conditionality is effective in improving their revenue performance (Crevelli and Gupta, 2016). Since basic institutions and administrative capacity are weak in FS, revenue conditionality is not as effective in enhancing their revenue performance during the program period. This suggests that the impact of implementing reforms will only be felt over a longer period, extending beyond the program period.

**74. There is some evidence that PFM capacity building efforts have coincided with improvements in PFM outcomes.** PEFA scores have improved significantly in countries where FAD's TA has been more intensive (Figure 16). For example, in Kosovo and Timor-Leste four core PFM indicators improved between two PEFA assessments, while in Liberia and Mali two core indicators improved, one remained constant and one worsened. The results are more mixed in the case of Haiti. A detailed comparative assessment for all PEFA indicators for these six countries is provided in Appendix VI.

**75. There has been an improvement in budget credibility for a group of FS between 2011 and 2016 (Figure 17).** This, as measured by the difference between budget forecast and outturn, suggests that the capacity to formulate realistic budgets, essential for implementing basic fiscal policies has improved.

**Figure 16. PEFA Scores in Core PFM Areas in Case Study Countries, 2005–2014<sup>1</sup>**

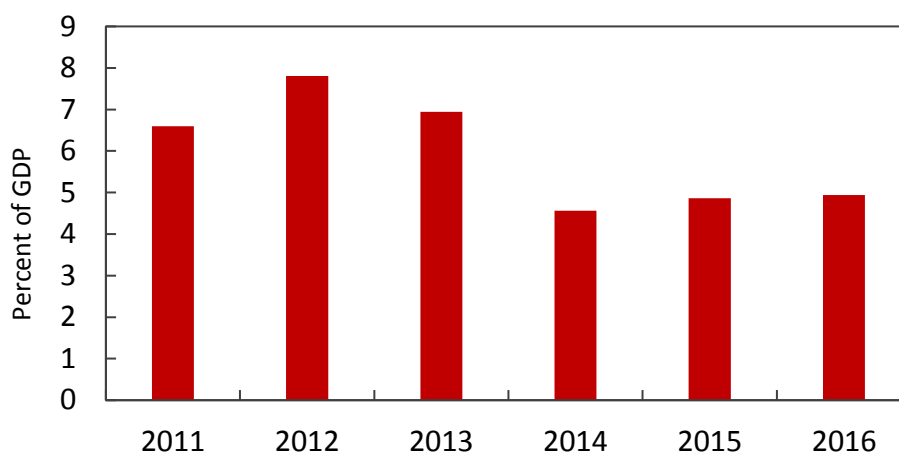
Country/ Area	Year		Budget Credibility		Cash Management		Accounts and Reporting		Transparency		TA Provided in the corresponding period
	First	Most Recent	From	To	From	To	From	To	From	To	
Afghanistan	2005	2013	2.67	1.83	0.00	3.50	2.17	2.67	1.50	2.88	8
Haiti	2008	2012	1.67	1.83	1.50	1.50	1.33	1.17	1.75	1.13	11
Kosovo	2007	2009	2.67	3.33	3.50	4.00	3.50	3.67	2.50	2.75	4
Liberia	2009	2016	2.67	2.17	2.50	2.50	1.67	2.17	1.38	2.38	43
Mali	2008	2011	3.33	4.00	2.50	3.50	1.83	1.83	1.88	1.63	10
Timor Leste	2007	2014	1.67	1.83	1.50	3.50	2.00	3.33	1.88	2.88	4

Decreased    No Change    Increased

<sup>1</sup> The range of scores is 0 (lowest) to 4 (highest).

Source: IMF

**Figure 17. Budget Expenditure Forecast Errors, 2011–2016  
(as a percent of GDP)**



Source: WEO, October 2016

\*Democratic Republic of Congo, Somalia, Tuvalu, West Bank & Gaza, and Yemen are missing data.

## LESSONS LEARNED

### **76. Target fiscal TA to achieve fiscal stability, financial control, and secure 'own' revenues.**

In the early stages of fragility (including immediately post-conflict or post disaster) the focus on the revenue side should be on targeted revenue collection based on the easiest-to-collect taxes (e.g., customs duties and excises at the border, withholding taxes, taxes on telecommunications), setting up a basic organizational structure for the tax and customs administrations, and introducing/strengthening/rebuilding core administrative processes such as registration, filing and payment in relation to the major taxpayers and the major taxes. Administrative limitations, especially in the immediate post-conflict stage, mean that tax policies should be kept simple so they can be easily understood and administered. Tax policy and administrative reform design should comprise an integrated package. On the expenditure side the focus should be on four key pillars: annual budget preparation, control of budget execution, cash management and basic fiscal reporting.

**77. Set priorities and pay attention to the sequencing of reforms.** On the revenue side, more complex reforms such as setting up an integrated revenue authority should be considered only once a sound organizational structure has been established in both the tax and customs administrations. On the expenditure side, more advanced reforms such as medium-term budgeting should be introduced only when basic PFM systems are in place. Building fiscal institutions takes a long time, especially in FS, and reforms often span several political cycles. Successful reform programs are most likely to be those in which successive governments are building on previous governments' efforts, and not 'starting from scratch'.

**78. Promote effective donor coordination.** Effective coordination among donors—in an increasingly crowded field—is a complex task. The country case studies have highlighted that to facilitate such coordination country authorities must be in the lead, all donor and TA assistance should follow a single plan with clear goals and milestones (here, medium-term revenue and expenditure strategies could play a key role), and donor coordination groups should be established if they do not already exist.

**79. There is value in having a medium-term reform focus.** In this regard, ongoing and future efforts to design and implement formal MTRS and PFM reform strategies may help countries exit fragility. Once FS move to the 'third' stage—those beyond the 'basic needs' stage—the focus should be on designing and implementing formal MTRS and PFM reform plans to help lift countries out of fragility.

**80. Do not underestimate the importance of customs.** Considerable attention is often paid to reforming the tax administration in FS, while customs is considered secondary. One lesson from the case studies, and from IMF experience in general, is that more attention needs to be paid to reforming and strengthening customs—especially when revenue from taxes at the border is significant. Customs is often a bell-weather for the degree of corruption and arbitrariness in a country—effective reform of customs can help improve public perceptions of fiscal institutions.

**81. Consider a more extensive TA presence and more flexible TA delivery modes.** As sustainable reforms in FS are long-term in nature, and are often constrained by the security situation, increasing the intensity and duration of TA and the flexibility of TA delivery modalities should be an important element of future capacity development strategies. This may require posting long-term advisors to provide more permanent, hands-on support when reforms are being designed. It may also help increase the authorities' confidence regarding the strategy to be followed, ensure continuity, and accelerate the pace of reform implementation. But broadening the use of long-term advisors has cost implications, which is likely to mean less resources for some countries. Security considerations in many FS pose constraints. The use of short term and peripatetic experts and increased use of modern communications technology can provide greater flexibility to deliver assistance according to a country's needs, absorptive capacity and security situation.

**82. Further integrate TA to FS into IMF lending and surveillance operations.** Building fiscal capacity in FS is a significant challenge. Further "mainstreaming" TA into the IMF's surveillance work, giving TA advice a prominent role in the Article IV consultation process, stands to benefit FS.<sup>62</sup> This 'integration' should be more substantially reflected in country policy notes.

## ISSUES FOR DISCUSSION

1. Do Directors agree with the approach that the IMF has been following, building fiscal institutions in an incremental way based on the 'starting' conditions?
2. Thus far the mix of TA in revenue and expenditure has been driven by country circumstances. Do Directors agree with the mix adopted thus far?
3. Do Directors believe the balance of modalities for dealing with the special needs of fragile states set out in the paper to be appropriate?
4. Do Directors have suggestions, beyond those in the paper, for making IMF support for fiscal capacity building in fragile states more effective?

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<sup>62</sup> The current coverage for "mainstreaming" exercises is around 25 countries each year.



## Appendix I. Analytical Groups

<b>FS Analytical Group</b>		
(39 countries)		
<b>LICs (20)</b>	<b>LMICs (13)</b>	<b>UMICs (6)</b>
Afghanistan	Congo, Republic of	Angola
Burundi	Côte d'Ivoire	Bosnia and Herzegovina
Central African Republic	Kiribati	Iraq
Chad	Kosovo	Libya
Comoros	Micronesia	Marshall Islands
Congo Democratic Republic	Myanmar	Tuvalu
Eritrea	São Tomé and Príncipe	
Guinea	Solomon Islands	
Guinea-Bissau	Sudan	
Haiti	Syria	
Liberia	Timor-Leste	
Madagascar	West Bank and Gaza	
Malawi	Yemen	
Mali		
Nepal		
Sierra Leone		
Somalia		
South Sudan		
Togo		
Zimbabwe		

<b>Non-FS Analytical Group</b>				
(98 countries)				
<b>LICs (10)</b>	<b>LMICs (40)</b>	<b>UMICs (48)</b>		
Benin	Armenia	Tunisia	Albania	Palau
Burkina Faso	Bangladesh	Ukraine	Algeria	Panama
Ethiopia	Bhutan	Uzbekistan	Argentina	Paraguay
Gambia	Bolivia	Vanuatu	Azerbaijan	Peru
Mozambique	Cambodia	Vietnam	Belarus	Romania
Niger	Cameroon	Zambia	Belize	Russia
Rwanda	Cape Verde		Botswana	Serbia
Senegal	Djibouti		Brazil	South Africa
Tanzania	Egypt		Bulgaria	St. Lucia
Uganda	El Salvador		China	St. Vincent & the Grenadines
	Ghana		Colombia	Suriname
	Guatemala		Costa Rica	Thailand
	Honduras		Dominica	Turkey
	India		Dominican Republic	Turkmenistan
	Indonesia		Ecuador	Venezuela
	Kenya		Equatorial Guinea	
	Kyrgyz		Fiji	
	Lao PDR		Gabon	
	Lesotho		Georgia	
	Mauritania		Grenada	
	Moldova		Guyana	
	Mongolia		Iran	
	Morocco		Jamaica	
	Nicaragua		Jordan	
	Nigeria		Kazakhstan	
	Pakistan		Lebanon	
	Papua New Guinea		Macedonia	
	Philippines		Malaysia	
	Samoa		Maldives	
	Sri Lanka		Mauritius	
	Swaziland		Mexico	
	Tajikistan		Montenegro	
	Tonga		Namibia	

**Other - High Income Countries (HICs)**

(54 countries)

**HICs (54)**

Antigua and Barbuda	Greece	Portugal
Australia	Hungary	Qatar
Austria	Iceland	San Marino
Bahamas	Ireland	Saudi Arabia
Bahrain	Israel	Seychelles
Barbados	Italy	Singapore
Belgium	Japan	Slovak Republic
Brunei Darussalam	Kuwait	Slovenia
Canada	Latvia	South Korea
Chile	Lithuania	Spain
Croatia	Luxembourg	St. Kitts and Nevis
Cyprus	Malta	Sweden
Czech Republic	Nauru	Switzerland
Denmark	Netherlands	Trinidad and Tobago
Estonia	New Zealand	United Arab Emirates
Finland	Norway	United Kingdom
France	Oman	United States
Germany	Poland	Uruguay

## Appendix II. Recent IMF Publications on FS

In the past decade, the IMF has prepared three major papers and a guidance note on issues relating to the IMF's broader engagement in FS.

**In 2008, the IMF reviewed its experience and discussed options to enhance the quality of its engagement with FS.**<sup>1</sup> It observed that the IMF had been engaged in some form in almost all FS to improve economic management and performance, though it had not adopted a specific and differentiated policy toward them.

**In 2011, the IMF's Strategy, Policy and Review Department (SPR) prepared a paper identifying how the IMF's engagement with FS could be strengthened,** considering recent experience and the evolving thinking in the international community.<sup>2</sup> The following were the key recommendations on proposed changes to IMF policies and practices: (1) For fragile LICs, fuller use of the Rapid Credit Facility (RCF) to support a more flexible approach to adjustment and reforms where needed. For fragile Middle Income Countries (MICs), establishment of a unified non-concessional facility for emergency assistance, which would provide greater flexibility; (2) Greater flexibility built into program design, while being mindful of applicable conditionality standards, to reflect better FS' limited implementation capacity, as well as the importance of delivering "quick wins" to populations; (3) Fuller attention to the political context in fragile situations; (4) Closer coordination with donors, particularly in the field, to help foster prioritization on key objectives, participate in the process of identification of "quick wins," and assess the financial implications of such priorities, including the identification of financing gaps; and (5) Continued efforts to plan for technical assistance over a medium-term horizon and to provide "boots-on-the-ground." Following the Executive Board's discussion of the 2011 paper, a staff guidance note was issued (2012), providing operational guidance on the IMF's engagement with low and middle-income countries in fragile situations.<sup>3</sup>

With regards to the use of the RCF, this facility allows the use of small amounts of Fund financing while countries prepare policies that would merit support under upper credit tranche arrangements. It has been used in a few cases by FS.

**A 2015 paper,**<sup>4</sup> based on surveys of country authorities, area department teams, and functional departments, takes stock of the state of IMF engagement with FS. It outlines possible follow-up actions in the areas of capacity building, financing facilities and program design, and policy support, including a new pilot approach for providing support to FS using a CBF that would establish goals for institution building, identify immediate and planned TA and training from the IMF and other

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<sup>1</sup> IMF (2008).

<sup>2</sup> IMF (2011).

<sup>3</sup> IMF (2012).

<sup>4</sup> IMF (2015).

development partners, and allow for fine tuning of support, where needed, based on the evolving needs of FS. This proposed CBF will build on the new results based management (RBM) framework which will help strengthen monitoring and reviewing of outcomes of the CBF. It also proposed steps to strengthen program success in protecting priority social spending through more targeted specification of spending floors and adoption of contingency plans to preserve spending from fiscal shocks and that training on political economy issues continued, and knowledge-sharing across teams working on FS will be fostered, including through a new intranet-based FS thematic site. As mentioned in the paper, the CBF framework is now being piloted in a few countries, including 5 SSA countries.

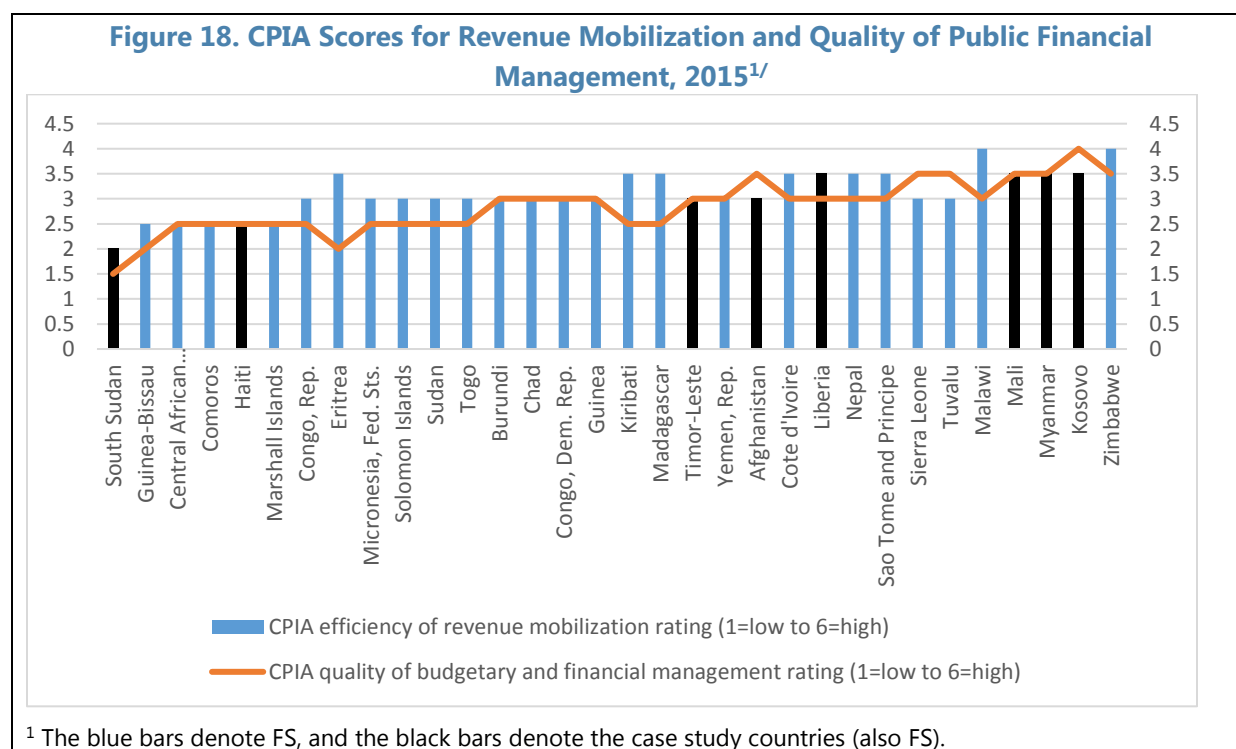
**Its 2015 paper, AFR assessed the state of fragility in SSA and progress made in building resilience, including the role of fiscal policies and institutions.**<sup>5</sup> The paper suggests that there are three key factors that determine the success of countries in building resilience, namely: (1) sufficiently inclusive political arrangement that helps sustain peace and prevent major political turmoil; (2) A committed leadership that is both willing and capable of promoting policies that translate this strategy into action and implement reforms that improve governance, transparency, and accountability. This is particularly important in the countries under analysis which started with weak institutions that were unable to provide adequate checks and balances. The leadership factor is critical as it allows for policies and reforms that promote economic stability, generate policy space to deliver improvements in living standards, and, over time, help strengthen institutions and build capacity; and (3) Strong international support in the form of financial and technical assistance focused simultaneously on security and on development. International stakeholders should be prepared to engage with fragile countries on a long-term basis, providing financial assistance in ways that can improve the effectiveness of the state, coordinating their efforts closely, and focusing capacity development efforts on economic institutions.

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<sup>5</sup> Gelbard et al. (2015).

## Appendix III. CPIA Scores for Revenue Mobilization and Quality of PFM

The CPIA sub-scores for ‘revenue mobilization’ and the ‘quality of budget and financial management’ in the case study countries are generally consistent with the countries’ fiscal capacity as described in the case studies. The World Bank’s CPIA rating of the quality of financial management assesses the extent to which there is: (i) a comprehensive and credible budget, linked to policy priorities; (ii) effective financial management systems to ensure that the budget is implemented as intended in a controlled and predictable way; and (iii) timely and accurate accounting and fiscal reporting, including timely audit of public accounts and effective arrangements for follow up.<sup>1</sup> The criterion for revenue mobilization assesses the overall pattern of revenue mobilization, including the statutory tax structure as well as revenue from all sources as they are actually collected. There are separate sub-ratings for tax policy and tax administration.<sup>2</sup> In four countries (Afghanistan, Kosovo, Liberia and South Sudan), the ratings for the PFM and revenue mobilization sub-criteria are different, with revenue mobilization capacity assessed as higher in South Sudan and Liberia, and PFM capacity rated higher in Afghanistan and Kosovo (Figure 18).



<sup>1</sup> It is not entirely surprising that the CPIA rating is consistent with FAD’s assessment of country case studies’ PFM capacity, considering that the ‘guideposts’ used include the PEFA framework and the IMF Code of Good Practices on Fiscal Transparency. On the revenue side, the ‘guideposts’ used include the World Economic Forum’s Global Competitiveness Index, the World Bank Enterprise Survey, the revenue questions of past PEFA assessments, and the World Bank’s ‘Doing Business’ Survey.

<sup>2</sup> CPIA 2015 Criteria, The World Bank Group.

## Appendix IV. Financial Management vs. Total CPIA Scores for Countries that Left Fragility, 2005–2015



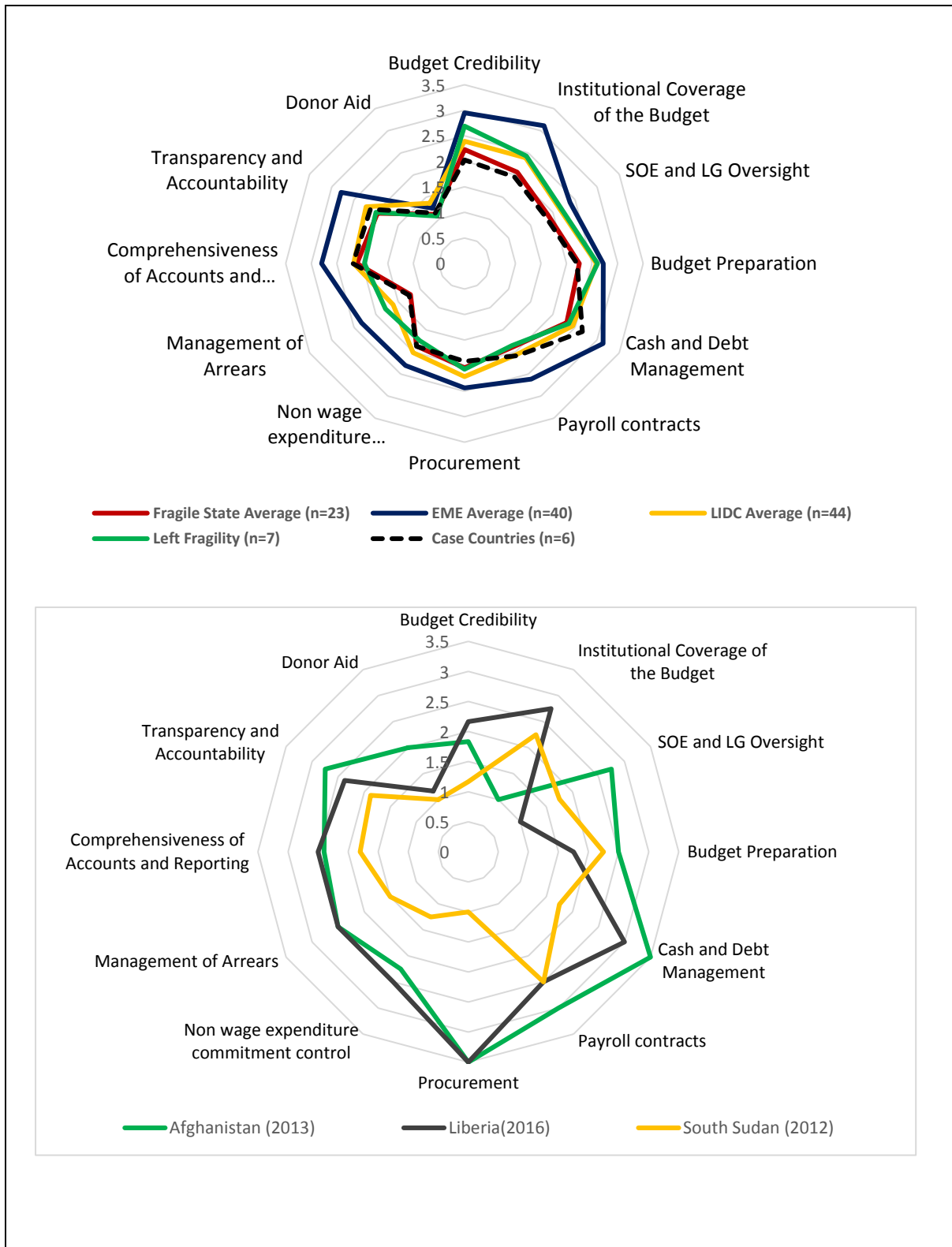
## Appendix V. IMF Lending Arrangements by Country

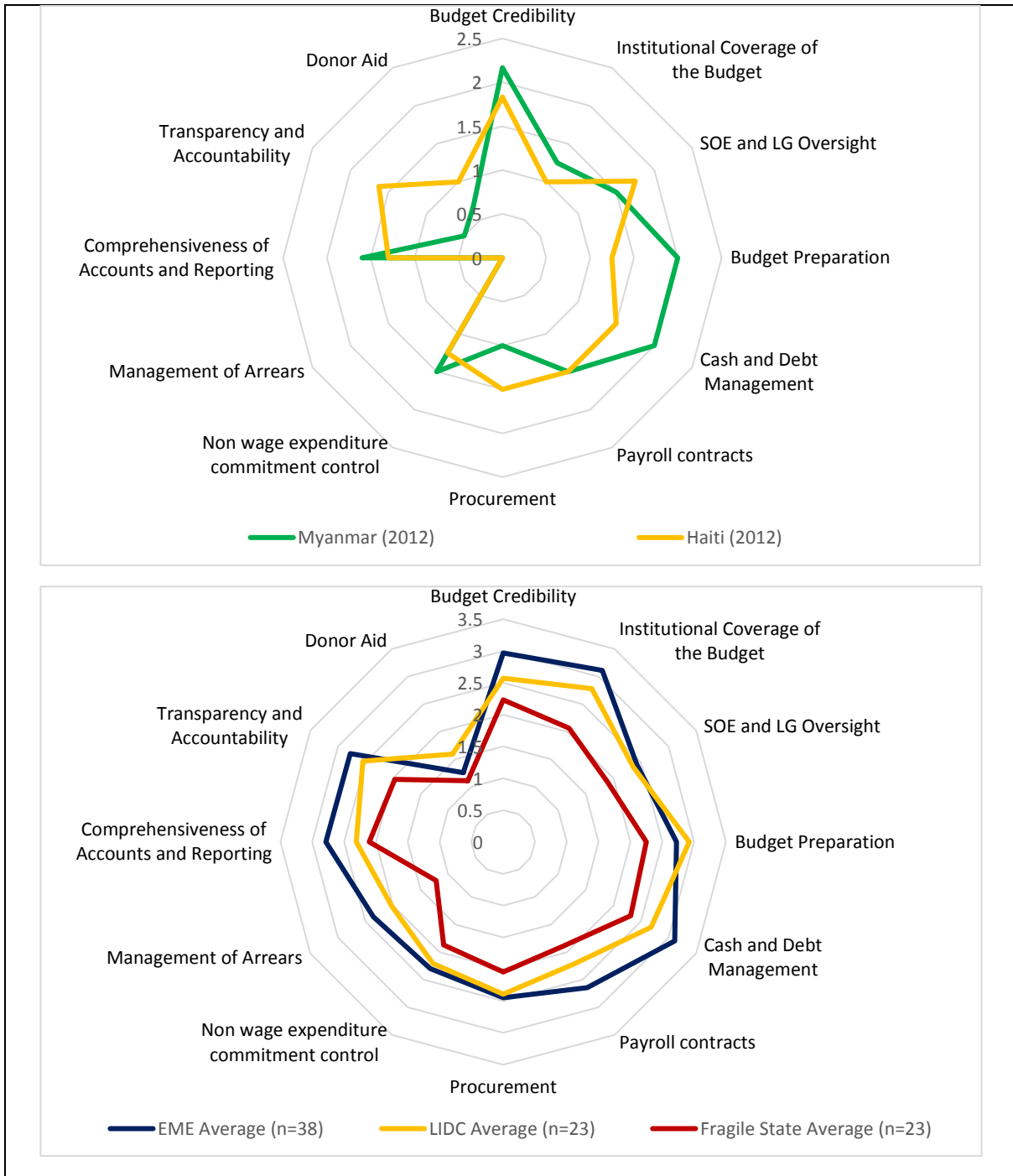
Country	Lending arrangements in the period
Afghanistan	ECF (2006–2014, 2016–2019)
Angola	SbA (2009–2012)
Bosnia and Herzegovina	SbA (2009–2015)
Burundi	ECF (2004–2016)
Central African Republic	ECF (2006–2014)
Chad	ECF (2005–2017)
Comoros	ECF (2009–2013)
Congo, Republic of	ECF (2004–2011)
Cote d'Ivoire	ECF (2002–2015)
Congo, Democratic Republic	ECF (2002–2012)
Guinea	ECF (2007–2016)
Guinea-Bissau	ECF (2010–2013)
Haiti	ECF (2006–2014)
Iraq	SbA (2005–2013)
Kosovo	SbA (2010–2013)
Liberia	EFF (2008), ECF (2008–2017)
Madagascar	ECF (2001–2009)
Malawi	ECF (2005–2008), ESF (2008–2009), ECF (2010–2017)
Mali	ECF (2004–2017)
Nepal	ECF (2003–2007)
Sao Tome and Principe	ECF (2005–2015)
Sierra Leone	ECF (2006–2016)
Solomon Islands	SbCF (2010–2012), ECF (2012–2016)
Togo	ECF (2008–2011)
Yemen, Republic of	ECF (2010–2016)

There were no lending arrangements for Eritrea, Kiribati, Libya, Marshall Islands, Federated States of Micronesia, Republic of the Union of Myanmar, South Sudan, Sudan, Syrian Arab Republic, Timor-Leste, Tuvalu, Zimbabwe, Somalia, or West Bank and Gaza.



## Appendix VI. PEFA Indicators for Case Study Countries







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