

Executive Summary

Since the establishment of the 2030 Agenda for Sustainable Development and Sustainable Development Goals (SDGs) in 2015, the international community has been working to achieve these goals through various discussions. The international community estimates that the funding for achieving SDGs is US\$ 66 billion annually for social development and US\$ 7 trillion for infrastructure investment, but unlike the implementation of MDGs centered on official development assistance (ODA), efforts are being made to secure new sources of funding and mechanisms. Discussions on financing for development have been ongoing since the Monterey Declaration in 2002 and continued until the Doha meeting in 2008, and was once again highlighted in the 2010 Busan Global Partnership. With the SDGs ahead, in July 2015, at the Third Development Finance meeting held in Addis Ababa, the international community's efforts for more than a decade have finally settled down.

As domestic resources in developing countries have emerged as the most promising sources of funding for development, it has been reflected in the SDGs on the target of 17.1 “Strengthen domestic recourse mobilization, including through international support to developing countries, to improve domestic capacity for tax and other revenue collection” under the goal 17 while emphasizing the importance of the indicator 17.1.1 total government revenues as a proportion of GDP and 17.1.2 proportion of domestic budget funded by domestic taxes. However, discussions on development finance in Korea tend to be concentrated on the public-private partnership (PPP) and/or the expansion of development financing centered on mixed finance, which is a combination of international private and international public funds. In fact, through various reports and academic research on the development finance, the studies or discussions on DRM have been rather inactive.

At this extent, this study was planned as a ground research that will explore the possibility of KOICA's exploration and expansion in this issue by covering the issues from the concept definition of DRM to actual project status of each country. In particular, DRM discussions, which are limited to the tax sector, should be extended to various issues defined by AAAAA so that they can be used as basic data for domestic debate in future. Also, the report can be utilized to grasp international discussions and further to identify the potential projects at the end.

Domestic resources mobilization (DRM) means all resources generated from public and private sectors in developing countries. In the meantime, OECD (2010) defines DRM as the widest definition of savings from domestic sources and all resources allocated to economic and socially productive investments. USAID (2015) and EU (2010) define it as domestic public funds, and as a whole process of generating and spending government revenues from domestic sources such as tax and non-taxable resources.

Low tax revenues depress central government administration and slow public goods and services provision. This lack of public services is ultimately responsible for tax resistance and tax evasion, leading to the impossibility of establishing and imposing tax policies. In the end, the tax authorities focus more on areas where they can work easily rather than on areas with high resistance, and it leads to a perception that incentives for tax evasion are larger, resulting in a vicious cycle in which tax revenues are lowered again. In order to overcome these 'low revenue traps' or 'vicious circle of low revenue', it is important that various subjects surrounding the tax system raise awareness of each role and build the national public finance management capacity.

It also includes various issues that affect the formation and function of the state, such as the right to domestic natural resources, taxes on international capital, illegal financial flows and the revitalization of the domestic private sector related

to the securing of national financial revenues. In sum, DRM can be viewed as an overall process of national development through the expansion of government revenues, and the Addis Ababa (AAAA) endeavored to capture some of the various issues that arise in this process.

In AAAA, DRM is defined as domestic public resources mobilization in the very first of the action areas. Domestic public resources (financial resources) are essential to providing public goods and services, increasing equity, and managing macroeconomic stability. It is a key component of mobilization of development resources to achieve SDGs, as well as social commitment and accountability dimensions emphasized by AAAA. AAAA also discuss the overall governance of the country from sound tax policies, sustainable economic growth through tax expansion, creation of additional resources through the stabilization of tax administration, and subsequent corruption in accordance with other tax treaties or discussions on development through ODA. It also clarifies the prevention of illegal financial flows and tax evasion and the linkage of mobilization of domestic resources.

It should be noted that in this globalized world, the emphasis is on the mobilization of domestic resources through international tax cooperation, beyond the border line. The way in which AAAA deals with DRM is not only the creation or expansion of tax revenue through the strengthening of tax administration ability, but also the transformation and strengthening of the tax system through international tax cooperation, the change of domestic governance for securing the most sustainable development resources. In short, AAAA recognizes that, in a vulnerable tax system, the government does not trust taxpayers, and taxpayers have a vicious circle of little incentive through taxes. Thus, breaking the vicious cycle by strengthening the taxation capacity can promote common interest in the economic growth of the government and citizens, promote improvement in other aspects of national competitiveness, strengthen the tax management system and promote

public participation, and so improve accountability (OECD 2010).

Various international mechanisms and initiatives are working in the process of discussing DRM-related SDGs and development resources. The Tax Inspectors Without Borders(TIWB) dispatches former tax auditors to the countries in order to assist tax investigators in addressing the difficulties of MNEs tax investigations in developing countries. They are either directly involved or offer advice. Addis Tax Initiative, which was established in July 2015, aims to double the support for technical cooperation in the tax sector by 2020, and aims to strengthen the mobilization of resources to achieve SDGs and ensure inclusive development. The OECD DAC is also working to monitor DRM support efforts in the international community by introducing CRS codes in 2016. UN Convention against Corruption (UNCAC), Extractive Industries Transparency Initiative (EITI), Financial Action Task Force on Money Laundering (FATF), and UN Committee of Experts on International Cooperation in Tax Matters, the Global Forum on Transparency and Information Sharing for Tax Purposes, regional development banks including the African Development Bank, the European Commission and the regional tax organizations are actively engaged in international tax cooperation.

In addition to the activities of tax-related organizations, there are a variety of projects through ODA and other international cooperation. The success cases of these DRM support projects can be seen in the case of Rwanda and Paraguay. In the case of Rwanda, it is regarded the establishing a long-term supportive relationship with donors including UK as well as the willingness of the recipient country to reform its tax system as major factors of success. As a result, the total government revenues by GDP increased by about 50% from 2001 to 2013, and these results played an important role in increasing the mobilization of domestic resources for development purposes, particularly in health and education sectors. Approximately 53% of all health spending in Rwanda in 2008 was external resources including ODA for health purposes, but fell to 38% in 2013. Health

expenditure per capita has doubled up from US \$ 32 to US \$ 70 over the same period. Government spending on health increased from 3.2% of GDP to 6.5%. This is a good example of the government allocating its DRM to its own welfare budget. Paraguay succeeded in reforming the tax system through triangular cooperation through the Latin American tax experts communities. It is a good example of strengthening the capacity of public finance management (PFM), which increases government revenue through the tax base expansion and tax compliance campaign despite the lower tax rate.

OECD DAC donors have also continued to expand DRM-related activities since 2010. The United States, the United Kingdom, Germany, Canada, and Norway are leading countries in DRM support. On the recipient side, support for Africa is the highest at 47%, followed by Asia at 31% and Latin America at 6%. Compared to Africa 44%, Asia 38% and Central and South America 12%. The proportion of total ODA support is more noticeably concentrated in Africa. In terms of income levels, the DRM-targeted ODA has been allocated to the least developed countries (52%) and 26% to the low-income countries (LMICs).

Among the priority partner countries of Korea, Bolivia had the highest tax revenue with respect to GDP with 28.3%, followed by Vietnam with 24.26%, Mozambique with 21.9%, Uzbekistan with 20.2% and Senegal with 18.8%. They are the countries (except Senegal) with a growth rate of over 5.5% and most of the government revenues depend on tax revenues.

According to the various assumptions and calculations, in order to implement global standards such as SDGs and climate change, it is generally expected that tax revenue should be more than 15% of GDP. In this regard, countries such as Bangladesh, Pakistan, Sri Lanka, Ethiopia and Indonesia can be categorized as having a burden of increasing tax revenue relative to economic growth and scale. However, when we look at the countries where ODA for DRM is actually supported,

it is confirmed that the support for Sri Lanka, Bangladesh and Indonesia is relatively low. Data also confirms the need to pay attention to the countries such as Vietnam, Indonesia, Bangladesh, Azerbaijan and Peru, where the amount of illegal financial flows has been steadily increasing since 2004.

By 2015, Korea has provided a total of US\$ 3.4 million in ODA for DRM purposes. All of the reported projects in 2015 was provided by KOICA, and the two projects among them amounted to US\$ 3.13 million, accounting for the majority of the total. Among KOICA's projects, tax-related projects carried out before 2010 were only about 0.2% per annum. Korea's support for ODA related to strengthening taxation has been supported mainly by the support of ICT-based single window system of KCS which is widely known as UNI-Pass. In addition, the training program for public officials or tax experts in developing countries has opened a total of more than 120 courses. However, ODA support with utilizing other modalities such as general budget support, sector budget support, basket financing, and South-South cooperation projects, which are generally considered to have direct or indirect effects on strengthening public finance management capacity had not been tried yet. Korea's ODA, which promised to increase the ODA for DRM sector after joining ATI, should be diversified in support field and diversification of modality.

In conclusion, this report emphasizes Korea's DRM-related support should be based on particularly its long-term policies and strategies, and its close partnership approach with the recipient country. In general, tax reform should be carried out on the basis of trust and confidence in the circulation process that uses the tax collection process carried out transparently, the collected tax on domestic welfare and economic growth while minimizing the tax resistance of the people. In addition, governance reforms, including the public financial system, as well as the establishment, settlement, modification and improvement of the system, must take place over a long period of time. Therefore, Korea's ODA also needs to find programs that are supported by various governance programs over

the medium to long term period of time. Secondly, in addition to the short-term and rather technical projects, we need to develop “package programs” to support the establishment of the taxation system of the recipient country with the tax consultation project and the system and policies related to local finance. Thirdly, to secure the transparency of taxation and DRM related ODA, it is important to strengthen policy coherence at home and abroad, and it is possible to plan a pilot project to enhance policy coherence that is considered to be the weakest in Korea. It is possible to envisage a partnership program in which the Korea Financial Services Commission (FSC), the Ministry of Strategy and Finance, the Ministry of Foreign Affairs, EDCF, and KOICA participate.

Among Korea’s key partners, Myanmar, Bangladesh, Pakistan and Sri Lanka can be categorized as fragile states. In particular, it is emphasized that DRM support should be provided throughout the state-building process in fragile states i.e. Afghanistan, Haiti, Chad, etc. In addition, it is necessary to actively utilize it as a tool to alleviate aid reliance by paying attention to the negative correlation between aid inflows and government revenues regarding the aid dependency. When we think of the ultimate goal of aid is to achieve sustainable growth without ODA support, it is necessary to consider it as a part of the exit strategy of donors especially in the countries with high economic growth rates.

Also, the modality of Korea’s DRM-related ODA is very limited in either project or training program. As the discussions on the use of country system become active, the budget support should be more favorable, however, the donor country risk still remains. Instead, we need to expand DRM related ODA by using the basket financing. It is also possible to consider ways in which international financial institutions such as the World Bank and the IMF will support the multilateral trust fund, which is being implemented to support the tax sector in the recipient country. It is also possible to establish a cooperation system with ODA implementation agencies such as the UK, Norway, Germany, and the United

States, which are currently leading donors related to the DRM related ODA.

Lastly, further research is needed to understand the DRM demand and the activities of the donor agencies. The formation and reform of the tax system is not simply a matter of approach from a technical point, but rather a close examination of the political and economic situation, culture, and structure of the entire government of the country. Thus we need to target specific countries which we can engage in the taxation sector. Then the research should focus on the other donor organizations that are currently being implemented or planned to be implemented in the sector. We can possibly seek the partnership and the way of harmonization in the country for a more effective project implementation.