A briefing on fiscal governance:
A principle-based finance and development approach
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Who gets to have a say in how we organise our fiscal space? Aid and debt conditionalities do restrict us from ordering our fiscal sovereignty. Such conditions can adversely impact the tripartite relationship between state building, finance, and development. If we want to strengthen a state's fiscal capacity, we must have strong fiscal transparency and public accountability measures put in place. These measures will aid a state to govern through principles, whether or not these principles are enshrined in a constitution or form part of subsidiary legislation, they are important if we want to protect a state's fiscal space.

The importance of these principles is that it allows the state to exercise its fiscal sovereignty over national ownership of its development strategies. The ***principle of inclusiveness, non-discrimination and an equitable approach to finance and development*** would protect a state against foreign interference in its fiscal matters or what a state does with its borrowed funds. These principles would allow a state to, for example, reject foreign conditions imposed on debt. Having these principles would also restrain IMF. Think of the IMF led structural adjustment programmes (SAP) - which is basically another word for a neo-colonial subordination tool to exploit Africa's capital. These SAPs directed the domestic state to restructure or reorganise its fiscal space to respond to an economic system that was crafted by external forces or foreign powers.[1] It reduced the post-colonial African states' fiscal sovereignty. A principle-based finance and development approach would not allow this.

Let's take this further, under these principles, the Washington Consensus which was introduced in Africa by the IMF supposedly to help support Africa meet its budget deficits, it trajected African economies along a neoliberal model which violated the African fisc - this is because it created a discriminatory approach to accessing the international economic markets on conditions developed by the former imperial powers organised today as the OECD or even the WTO.[2] When you have a principle-based finance and development approach then a state becomes accountable to its population and not foreign powers on how it manages its sovereign wealth and applies it to support the formation of a social welfare state.

The lack of accountability to the people, for example, can be exemplified through resource backed loans, which are

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[1] Okanga, Ogbu, and L. A. Latif. 'Tax Vulnerabilities in Africa: Revisiting Inclusivity in Global Tax Governance'. *African Journal of International Economic Law*, Vulnerabilities in International Economic Law, 1 (2). 2021.

[2] Latif, L.A., 'The Lure of the Welfare State following Decolonisation in Kenya' in Gurminder K Bhambra and Julia McClure (eds) *Imperial Inequalities: States, Empires, Taxation*. (Kilombo, 2022).

quite common but very secretive. This is where an extractives state agrees to take a loan which it secures by offering, for example, its mineral sector as a collateral. Many African countries are mineral producing states. Countries such as Angola, DRC and Zimbabwe have structured the natural resources and extractive sectors of their economy to permit taking out resource backed loans to support their government's financing of their development policies.[3] Information on resource backed loans is not shared with the public. These loans have short maturities, high interest rates and no commitments on how the money will be used. Resource backed loans can trap resource rich countries into losing control of their resources when a loan cannot be repaid at maturity because the debtor country is unable to scale up its resource production quickly enough to begin making payments.

If we have a principle-based finance and development approach the ***principles of openness, transparency, rule based fiscal decision making*** would not allow resource backed loans to crush the sovereignty of a debt defaulting country by its mineral sector being taken over. Let's also consider the argument on debt, and how a principle-based finance and development approach to debt would help support a human rights-based approach to development. To have a principle-based finance and development approach we therefore need to think about constructing a sustainable fiscal contract based on the following **9 rules.**

1. Rule 1 on developing a sustainable fiscal contract is to put people's social and economic well-being first. Therefore, no austerity. How do you secure this? I think it is best to keep to progressive taxation on income and to stop any increment on consumption taxes this is because any increase in consumption taxes will affect the poor and low-income earners. It will deteriorate their savings base which in turn will stunt the long-term development of a countries capital market.

2. Rule 2 is about disaggregating tax data on VAT based on what men and women pay and then to apply commensurate redistribution towards women economic improvement and access to public goods. When the revenue authorities of the African states collect tax they usually do not provide disaggregated tax data - in other words we do not know whether the tax was collected from low income earners, high income earners, middle income earners, how many of them were men, how many were women, how many from a taxable group comprised of vulnerable communities, whether the tax was collected as a result of an increase of royalties from which specific mining sector whether titanium whether oil whether gold? such disaggregated tax data is very valuable if a state is to provide fiscal transparency on how it is governing its revenue cycle and allowing it to contribute towards the formation of a welfare state or strengthen its social spending.

3. Rule 3 is to renegotiate double taxation agreements to remove tax

[3] Mihalyi D, Adam A and Hwang J, 'Resource-Backed Loans: Pitfalls and Potential' [2020] *NRGI.*

holidays and exemptions and replace these holidays and exemptions with a negotiated tax rate. We talk of special economic zones as well as economic processing zones which are usually tax exempt, a tax percentage can be applied to profits made on goods manufactured or produced out of this of these zones and I think this thinking is needed insofar as we are committed towards jumpstarting our economy's post the covid led restrictions and fiscal corrosions on the country's economic potential.

4. Rule 4 the licence fees paid by the informal sector workers should specifically be spent by the state in providing loans to informal sector workers to venture into the formal economy with their trade activities. By doing this a state will be expanding its taxable base and this is a long-time investment into a states' fiscal growth. When we try and map the entire African continent, we see that a significant chunk of the population is involved in the informal economy or some in the underground economy but we're not dealing with the underground economy because you know that is the subject of criminal law and an enabling environment for illicit finance we're more focusing on the informal economy itself. In Kenya we refer to the informal economy as *Juakali* and in Ghana we refer to it as the *Galamsey*. Because a large population of all African economies are informal workers or responds to the informal economies needs we need to be able to tap into this economy so that it can help the state create a sustainable fiscal base.

5. Rule 5 is very simple. It's to think about increasing the rate of royalties that mining companies or multinational corporations involved in the extractive industries pay on minerals. There are some countries in Africa that have negotiated their royalty rates between 3 to 5% obviously these double tax treaties were signed immediately after independence and at that time the royalty rate was indicated as between 3 to 5% but that amount is not commensurate with the economic needs of a state today, so we need to be able to renegotiate it to even 15-20 or even 30%. The market rate I think is about 15% but when we follow the AFRODAD slogan that Africa should be the *'rule maker and not the rule taker'* so let's apply that slogan to rule 5 - let us be the rule makers on establishing what rate of royalties is feasible for our economies.

6. Rule 6 is all about tapping into the diaspora. A lot of Kenyans live abroad and other Africans from neighbouring states live in foreign countries so our government should think of attracting the diaspora by issuing out diaspora bonds this is one way in which the government can think about generating revenue sustainably in the long term many of the diaspora who live abroad send remittances back home to their families through Western Union and their families use this to you know fund their economic well-being to supplement their incomes to build their houses and to also make small investments

in the agricultural sector so this is quite a ripe area that we need to tap into and bring within a sustainable fiscal contract and think about advising our county governments or even the national government on how they can improve their revenue collection base.

7. Rule 7 is quite close to my heart because it's something that I'm thinking about the importance of partnering with faith-based organisations (FBOs) to tap into their wealth tax and spend it on social improvement where the purpose of the FBO and the state aligns in terms of development priorities. In Islam, one of the fundamental pillars of being a Muslim is to contribute towards zakat. Zakat is in Arabic word and in English we define it to mean tax on wealth so every Muslim who is eligible having a certain amount of money in savings or properties or gold or shares or life stock even land which reaches a specific threshold must pay zakat annually, the taxable rate is 2.5% of anything above the zakat tax threshold. Collectively Muslims are contributing almost hundreds of millions of dollars in zakat. Usually, this amount is given to poor relatives, homeless people, it is used to finance the living expenses of widows, to construct schools, help people with their medical finances, send money as aid to Yemen, Palestine, Lebanon, where for example there have been famine or civil strife related problems. In Kenya, we have Muslims who pay zakat and we should think about getting them to start partnering with their county governments or even partnering with the national government so that Muslims can pool their zakat together and give it to the state so that the state can use that to supplement their health budget deficits. So when we're thinking about a sustainable fiscal contract and we want to think about innovative approaches we can look to zakat and we can see how a non-Muslim state or a Muslim minority state which does not practise Islamic law can actually access funds that are available under a different faith based legal system and use the faith funds to start financing certain development needs within the state. Obviously, this is contentious. It will be subject to a lot of discussion and the consent of the Muslims alongside a sort of a public private arrangement where the Muslims work together with the government to administer zakat funds so that it is used for the purpose for which Islamic law mandates.

8. Rule 8 is to tax the digitalising economy. To have a strong sustainable fiscal contract we need to be able to think of revenue streams that will always be turning in money into the state's revenue basket. One way to secure this is to tax the digital economy

9. Rule 9 is on strengthening enforcement of the STAR Initiative. This stands for stolen assets recovery initiative. A lot of government officials because of their corrupt tendencies steal public funds and then they transfer these stolen funds to offshore jurisdictions; for example, in Switzerland, Bahamas, Singapore,

Isle of Man in the UK. The idea of the STAR programme which was initiated by the World Bank is to try and identify track and trace these corrupt funds that have been transmitted out of an African country into European or Asian financial institutions and then to work with the foreign nation to try and freeze those funds and then transfer them back to the state from which those funds were looted. I think it's important if we want to think about strengthening a state fiscal system or to create a sustainable fiscal contract the state or the government should consider strengthening its approach to investigating and recovering stolen assets.

All these rules must be supported by an ***enabling environment.*** The enabling environment must be governed by a principle-based approach to finance and development. These principles must be institutionalised, we have to create systems, we have got to put in place institutions or structures to ensure that these principles are being implemented, and where they are not being implemented, they have to be enforced. This is where the judiciary becomes a critical factor in protecting a country's fiscal space because any government officer, any government institution that decides to violate any of these principles or to not apply any of these principles, then the remedy would lie by going to court to get an order of mandamus, for example, to compel the government to apply these principles. At the same time, institutions must exist to create or to allow the public to be able to hold government accountable. Public participation, therefore, in fiscal decision making is very important. It opens the fiscal space to accountability, transparency and responsibility. These are key features that are important to secure the fiscal base of a country.

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