

A conversation with Kieran Holmes, February 23, 2018

Participants

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Note: These notes were compiled by GiveWell and give an overview of the major points made by Kieran Holmes.

Summary

GiveWell spoke with Mr. Holmes to learn about his work with the governments of developing nations to reform their tax laws and increase government revenues. The conversation focused on the goals, components, and results of tax reform efforts Mr. Holmes has led, as well as the potential for future work in this area, including potential target countries and prospects for funding.

Components of tax reform

Mr. Holmes has worked with the governments of several developing nations to reform their tax policies and grow their revenues. Successfully implementing these reforms requires:

1. A strong and continued commitment to reform from the country's government
2. A long-term funder to support the project
3. Competent technical assistance

Goals of these reforms have included:

- Broadening the tax base
- Reducing tax rates
- Ensuring the tax structure is simple to make collection as easy as possible
- Creating a full suite of tax types (e.g., value-added, income, capital gains, and excise taxes)
- Shifting emphasis away from trade taxes toward non-trade taxes

In addition to reforming the law, key components to growing revenue include:

- Improving revenue collection procedures
- Putting adequate IT systems in place
- Trade facilitation and private sector development
- Regional integration
- Outreach programs to inform taxpayers about changes

Increased tax revenue strengthens the state and allows it to fund infrastructure development, enabling the growth of business and leading to increased employment and poverty reduction.

Broadening the tax base

Broadening a country's tax base involves both a) bringing additional compliant taxpayers into the base (e.g. by comprehensively registering taxpayers (both residents and non-residents having an income source in the country) and making sure they receive notifications when taxes are due) and b) expanding the tax law to capture more of the country's income (e.g. by drafting comprehensive source rules). The latter involves closing loopholes in existing law and producing a simply-written, comprehensive tax code that captures all forms of income. Some major sources of income are often overlooked in existing tax codes — for example, countries often levy an export tax on resources extracted by foreign companies but fail to tax profits that the company makes while in the country or the wages of the company's expatriate staff. Forms of income that are often effectively untaxed are dividends, interest, royalties, and management fees.

Reducing tax rates

Every country Mr. Holmes has worked in has been able to significantly increase revenues by broadening its tax base while also lowering tax rates. For instance, in Lesotho, reforms brought the top tax rate down from 53% to 35%. A similar decrease happened in Kiribati. The reduction was even larger in Rwanda, with the top rate coming down to 30%.

Country outcomes

Rwanda

In 2002, the UK's Department for International Development (DFID) brought Mr. Holmes in to manage a project to help the Rwandan government increase its revenue. After three weeks, Mr. Holmes put together a report for the government and met with the Commissioner General to present his recommendations. DFID then gave him a one-year contract to start to design reforms, redraft legislation, improve IT systems, etc. The Rwandan government approved of his work and developed confidence in him over time. Mr. Holmes ended up working in Rwanda for eight years in total. Mr. Holmes' work was mainly monitored through the Commissioner General, with whom he worked closely. The president of Rwanda took a direct personal interest in the tax reform work.

When Mr. Holmes first met with the Rwanda Revenue Authority (RRA) in 2002, it was collecting about 68 billion Rwandan francs a year. Last year, it collected over 1 trillion francs. (This has been a large real and sustained gain in revenue, albeit accompanied by some loss of value in the currency.) As a result, Rwanda has been empowered to finance its recurrent budget from its own resources and to make spending decisions based on its own revenues.

Rwanda's infrastructure, particularly in Kigali, has seen major improvements since 2002. The country has also improved significantly in terms of school attendance, health outcomes, university graduates, attracting businesses, etc. and is highly regarded as a serious reformer by the international community.

Rwanda was the first country to institute a Taxpayers' Day to celebrate and promote tax compliance, which has been successful and has been emulated by other countries. President Kagame addresses the taxpayers each year, and his speeches often include a call for Rwanda to rely on its own taxpayers rather than taking aid from other countries.

Lesotho

In the early 1990s, Mr. Holmes was sent by the UK government to advise Lesotho's government on taxing the Lesotho Highlands Water Project (LHWP), a large investment project to create large reservoirs in the mountains, pipe the water to South Africa, and generate electricity. Many businesses financed by the World Bank and the European Union (EU), and indeed many senior officials of those institutions, argued then that the project shouldn't be taxed because it was "aid" and not commerce. Mr. Holmes strongly advised Lesotho's government that it should tax the project, which it then did. Taxing that single project grew Lesotho's tax revenue by 2,000% over a six-year period in the 1990s and revenues have continued to grow strongly since then.

The tax law that Mr. Holmes worked on in Lesotho in 1993, with drafting assistance from the International Monetary Fund (IMF), is still in effect.

Burundi

Mr. Holmes became the first Commissioner General of the new Office Burundais des Recettes (OBR) in 2010. Burundi doubled its state revenue during the four years Mr. Holmes was active there. This involved significantly reducing corruption at the tax collection level. The country also dramatically improved its standing in the World Bank's *Doing Business* Index as well as in the Transparency International corruption rankings during this period.

Kiribati

Mr. Holmes's work led to a quadrupling of Kiribati's tax revenue during the second half of the 1980s.

Potential for future work

It might be possible to start an organization made up of tax professionals with a skill set similar to Mr. Holmes's in order to scale-up this kind of work. A project like this would require a manager who can talk to government leaders at a high level, as well as technically capable people to run trainings, provide policy advice, help with IT systems, etc.

This would also require a funder or funders able to invest significant financial support in many areas (e.g. HR systems, IT systems, buildings, training, capacity building, redrafting tax laws, and designing communications strategies). Mr. Holmes estimates that four or five years of work would cost between \$20 million and \$40 million, even for a small country. (Working in several countries at once could reduce costs somewhat.)

Strong political commitment from the country's government is vital for this kind of work to succeed.

Potential target countries

The Brookings Institute recently produced a paper identifying 31 "Severely Off Track" Countries (SOTCs) which it argues are the key to the next iteration of poverty reduction and which donors should focus on for the next ten to twenty years. Mr. Holmes thinks this analysis is probably correct and that these countries would benefit strongly from comprehensive domestic revenue mobilization strategies.

These include some large countries (e.g. the DRC, Nigeria) which have populations in the tens of millions. Some of the countries (e.g. Yemen, South Sudan, DRC) are in a full or partial state of war and are unlikely to be able to effectively implement reforms in the near term, but in some (e.g. Nigeria), reform does seem possible. Nigeria collects about 6% of its GDP in revenue, far below the African average of 18% and the developed world average of around 30%.

With funding, Mr. Holmes could potentially work on tax reform in a few more countries. He would only want to work in countries that demonstrate the strong political will necessary to push for reform and fight corruption. In addition to tax reform proper, Mr. Holmes would want to work on creating an environment more open to trade and investment. A well-designed revenue project would have the objective of facilitating trade and investment and private sector growth.

Many countries in West Africa (e.g. Burkina Faso, Togo, Mali, Niger) need stronger institutions and assistance with their revenue administrations. Some of these countries have asked Mr. Holmes for assistance; for instance, he did some work in Burkina Faso in 2016 and produced some recommendations, which the IMF endorsed, but Burkina Faso's government has not yet designed a comprehensive reform program.

South Sudan

Mr. Holmes thinks tax reforms similar to his work in Rwanda and Burundi might be possible in South Sudan, but a number of factors would need to shift to enable this. South Sudan would need to develop an environment that is conducive to investment or foreign business and where investors feel safe. Therefore, South Sudan needs to prioritize national security issues. Additionally, the police (under the Ministry of Internal Affairs), rather than the Ministry of Finance and Economic Planning, largely control the customs service, which leads to a sub-optimal result in terms of effective tax and customs administration. Mr. Holmes attended several high-level meetings to brief Cabinet members on the importance of transferring full control of customs to the Ministry of Finance and putting only professionally-trained customs officers in charge of the border posts; there was broad agreement that this should happen but so far there does not appear to be a real change in the status quo.

Prioritizing security around the country is a necessary condition for developing the economy. Once this is done, it might be possible to create a level of stability that would allow for investment in expanding the economy.

Some potential funders Mr. Holmes has talked to were reluctant to support tax reform work in South Sudan on the grounds that the South Sudanese government could spend the increased revenue on arms. Mr. Holmes dismisses this argument as he believes that it is always good to help countries to grow their domestic revenues and that any government that intends to buy arms would find a way to do so, regardless of whether or not it had support for collecting its revenues.

Ghana

Ghana might be a potentially promising target for reform. Mr. Holmes's impression is that Ghana's government seems to be generally knowledgeable and to understand the rationale for reform. Some reforms have already taken place, such as the establishment of the Ghana Revenue Authority. Ghana's government has made some investment in, e.g., improved IT systems, and further reforms are planned.

Uganda and Kenya

Uganda and Kenya made reforms to their tax systems a while ago, which Mr. Holmes thinks it could be beneficial to revisit and review.

Incentivizing countries to reduce corruption

Mr. Holmes' view (which he has expressed at the UN and elsewhere) is that bringing in outside experts to facilitate reforms is not in itself a sustainable strategy in the long term, although it can be a key component in the short to medium term. It is necessary for country governments to take full ownership of the steps necessary for mobilizing their own revenues, combatting corruption, and devising strategies for bringing their populations out of poverty.

Many of the "severely off track" countries mentioned above need to take steps to address corruption (e.g., by instituting and enforcing anti-corruption policies like those in Rwanda and Uganda) before they will be able to successfully accomplish tax reform or other reform projects. (Rwanda has had a zero-tolerance corruption policy for a number of decades, which has been a key element in establishing the attitude of the population toward corruption.) However, garnering political will to combat corruption can be very difficult because the beneficiaries of corruption are typically elites who also have political power.

Mr. Holmes thinks that, rather than imposing conditionality of any kind, it will likely be more productive for the international community to incentivize domestic resource mobilization and private sector development programs. For example, demonstrated commitment to such programs could be agreed upon as the trigger for greater international investment in infrastructure (e.g. roads, airports, fiber-optic cabling), while countries that do not show commitment to such programs would automatically go to the back of the queue for such assistance.

Other groups working in this area

It is now well recognized (e.g. by the IMF, World Bank, EU, and bilateral donors) that tax reform is essential to building strong in-country institutions, and that increasing government revenues is important for economic development. There is much stronger international recognition of the benefits of domestic resource mobilization than there was when Mr. Holmes began doing tax reform work in the 1980s. For instance, the UN recently held a conference on the issue, and the OECD's Base Erosion and Profit Shifting (BEPS) Project is ongoing.

DFID has been working to build revenue administrations in Africa for about 40 years but never developed a comprehensive repository of best practices or an in-house cadre of tax professionals it can deploy, preferring instead to rely on consultants for this work. When DFID decides to do a revenue-building program, it puts together an appeal to present to the business community and consulting firms to find technical specialists to help.

Tax Inspectors Without Borders is an organization that sends retired tax professionals to help governments build tax audit capacity.

The International Monetary Fund (IMF)

Mr. Holmes has worked closely with the IMF and thinks its work in this area is highly valuable. (For instance, when he worked in Kiribati, he contacted the IMF for legal advice for redrafting the tax law, which went well.) Mr. Holmes thinks that the IMF provides excellent advice and assistance to countries through its Legal and Fiscal Affairs Departments and that it has limited funds for deploying teams on medium-term assignments.

The IMF assesses countries using its Tax Administration Diagnostic Assessment Tool (TADAT), which includes a list of key components for an ideal tax system, and then produces a diagnostic report and gives the country recommendations for reforming its tax laws. The IMF then checks on the country's progress and offers further follow-up advice. The IMF also has regional offices around the world through which it interacts with and stays informed about countries in each region.

Funders in this area

Mr. Holmes's work in Kiribati, Lesotho, Rwanda, and South Sudan was funded by DFID, either directly or indirectly. His work in Burundi was funded by Trademark East Africa, a trade facilitation agency which is partly financed by DFID and partly by Scandinavian countries. The EU has sometimes funded work of this kind.

Donor coordination can be very difficult. USAID was interested in becoming involved in Mr. Holmes's work in Ethiopia at one point, but this didn't happen due to bureaucratic difficulties.

Following the launch of the Addis Tax Initiative in 2015 (which involved a pledge to double donor spending on tax reform), Mr. Holmes thought it was likely that there would be a major increase in institutional funding in this area, but this hasn't

materialized to any great extent. Mr. Holmes thinks this might now be a promising area for private philanthropy.

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