FISCAL POLICIES TO TACKLE INEQUALITY IN GHANA, BURKINA FASO AND SIERRA LEONE

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This report looks in-depth at the record of 3 countries - Burkina Faso, Ghana and Sierra Leone - on their governments' efforts to reduce inequality through fiscal policies. The report identifies areas where each government can take action to make their tax and spending work harder to redress inequality. It is intended to be used by both technical (i.e. experts in tax or spending) and less specialised audiences. It therefore starts with an executive summary which highlights the key lessons and recommendations across the three countries, intended for a broad audience. This is followed by a more in-depth "technical" report, which contains more detailed analysis of policies, organised in three country case studies. Annexes contain data-sets and charts.

ACRONYMS

CIT	Corporate Income Tax
CSO	Civil society organisation
ECOWAS	Economic Community of West African States
GDP	Gross Domestic Product
GFI	Global Financial Integrity
GST	General Sales Tax
GSW	Government Spending Watch
IFFs	Illicit Financial Flows
IHDI	Inequality Human Development index
IMF	International Monetary Fund
LIC	Low-Income Country
LMIC	Lower-Middle Income Country
ODA	Official development assistance
OECD	Organisation for Economic Co-operation and Development
OOP	Out-of-Pocket (health spending)
PIT	Personal Income Tax
UIS	UNESCO Institute of Statistics
WAEMU	West African Economic and Monetary Union
WASH	Water, Sanitation and Hygiene
WEO	World Economic Outlook
WHO	World Health Organisation
VAT	Value added tax

GLOSSARY OF TERMS

Capital gains taxes	Taxes on the profits from the sale of capital assets such as stocks and shares, land and buildings, businesses, and valuable assets such as works of art.
Consumption taxes	Taxes such as value added tax, general sales taxes, and excise taxes.
Corporate taxes	Taxes on the profits made by companies. The tax is generally imposed on net taxable income, specified in the company's financial statement.
Debt servicing	Making payments on the principal and interest on outstanding loans.
Direct taxes	Taxes that are charged on physical or legal persons directly upon their salary, profits, dividends, rents or other types of income.
Fiscal space	Fiscal space refers to the room governments have in their existing budgets to increase spending, depending on the budget deficit, revenues and debt levels.
General sales tax	A tax added to the value of all sales with no allowance for claiming a rebate on tax paid.
Gini (Coefficient)	The Gini is a measurement of the income distribution of a country's residents. This number, which ranges between 0 and 1 and is based on residents' net income, helps define the gap between the rich and the poor, with 0 representing perfect equality and 1 representing perfect inequality. The Gini coefficient is the most commonly used measure of inequality.
Incentives	A specific provision not to tax something that otherwise would be taxed (also referred to as exemption).
Income taxes	Taxes on income, profits, inheritance, payroll and capital gains, which are generally divided between taxes payable by individuals and corporations.
Indirect taxes	A form of tax charged upon transactions, usually on their gross value. Examples include sales taxes, value added taxes, goods and services taxes, stamp duties, land taxes, excise and customs duties, and levies of all sorts.
Palma measure of inequality	The Palma ratio is defined as the ratio of the richest 10% of the population's share of gross national income divided by the poorest 40% share.
Progressive taxation	A tax system in which the share of income paid In tax increases as the income increases, so that a higher level of tax is collected from taxpayers who earn more and a lower level from those who earn less.
Regressive taxation	A tax system in which the share of income paid In tax decreases as the amount subject to tax increases.
Revenues	Funds that the government, as a result of its sovereign powers, collects from the public. Typical revenues include individual and corporate income taxes, payroll taxes, value-added taxes, sales taxes, levies, and excise taxes.
Royalties	Royalties are usage-based payments for ongoing use of an asset as prescribed in a licence agreement, for example natural resources such as oil, minerals, fisheries and forests. Royalties are typically agreed upon as a percentage of revenues raised from the use or gradual depletion of an asset.
Secrecy jurisdiction	Secrecy jurisdictions are countries and territories that provide financial secrecy which undermines the regulation of another jurisdiction for the primary benefit

	and use of those not resident in their geographical domain.
Social security payments	Payments made by individuals to fund government-provided health, unemployment, pensions and other basic social rights.
Special economic zone	Similar to an export processing zone (EPZ), but the activities can include domestic market-orientated business activities.
Tax	A fee levied by a government on a transaction, product or activity in order to finance government expenditure.
Tax avoidance	The term given to the practice of seeking to minimise a tax bill within the law (as opposed to illegal methods, which are classed as tax evasion or fraud). This often involves manipulating the tax base to minimise the tax payable.
Tax base	The collective value of transactions, assets, items and other activities that a jurisdiction chooses to tax.
Tax burden	The total amount of tax paid by an individual, organisation or population. Also referred to as tax incidence.
Tax competition	The pressure on governments to reduce taxes, usually to attract investment, either by way of reduction in declared tax rates or through the granting of special allowances and incentives.
Tax compliance	Payment of tax due without engaging in tax avoidance or evasion.
Tax dodging	A legally imprecise term that is often used by tax justice campaigners when it is not clear whether tax is being avoided or evaded. It highlights the fact that many tax avoidance strategies are abusive, while being considered legal.
Tax evasion	Illegal methods used to pay less tax. Also known as tax fraud.
Tax expenditure	The cost of tax incentives of all types in terms of lost potential tax revenue. As with any other expenditure, it should be considered as an investment and evaluated on the basis of cost and benefit.
Tax haven	See secrecy jurisdiction.
Tax holiday	A period during which a company investing in a country does not have to pay tax under an agreement with the government.
Tax incentives	A tax incentive is an aspect of national tax law designed to encourage a certain type of behaviour. This may be accomplished through means such as limited periods of tax holidays or permanent tax deductions on certain items.
Tax potential	The potential capacity of a country to raise revenue, based on factors such as its level of GDP and the structure of its economy
Value added tax (VAT)	A tax charged by businesses on sales and services but which allows businesses to claim credit from the government for any tax they are charged by other businesses in the production chain. Different from the general services tax, which does not require proof of being an intermediate producer.

EXECUTIVE SUMMARY

1. Inequality Has Human Costs in All Three Countries

In too many developing countries, economic inequality is stopping growth from reducing poverty and delivering shared prosperity. Dangerously rising levels of inequality are harming development and growth, and undermining poverty reduction.[1] In Sub-Saharan Africa, the gap between rich and poor is second only to Latin America, and the benefits of growth are too often accruing mainly to a small minority. Seven of the world's most unequal countries are in Africa,[2] and one-third of African countries are seeing increasing inequality.[3] Inequality is less marked in West than Southern or East Africa,[4] but is on the rise and unacceptably high in some countries.

All three countries face inequality problems. Comparing the income of the top and bottom 40%[5]:

- Ghana is "averagely unequal" among African countries. As in many other lower-middle income countries (LMICs), rapid recent income rises have been accompanied by rapidly growing inequality, making it imperative for government to focus on fighting inequality.
- Burkina Faso and Sierra Leone are less unequal - both falling in the top performing third. Burkina Faso has slightly reduced inequality in recent years; and Sierra Leone has the lowest inequality of the three, and is fourth best of 15 countries in West Africa.[6] Nevertheless, this is mainly because, as low-income countries (LICs) Burkina Faso and Sierra Leone have fewer high-income citizens - if they grow faster in future, their high levels of extreme poverty will stay unchanged and inequality will rise rapidly unless policies are put in pace to ensure prosperity is shared.

Moreover, all three countries are being hit by a fall in commodity prices and demand, which is likely to continue in the coming years, slowing growth and reducing resources to tackle inequality. Nowhere is this starker than in Ghana, which is struggling with huge debt bills and fiscal deficits; while growth driven by exports of gold, oil and cocoa has been hit by falling prices. In this context, governments will need to focus even more closely on progressive taxation and spending to target inequality.

Economic inequality intersects with, and compounds other inequalities based on gender or ethnicity. These have a huge impact on the poorest: more than one in 100 women die in childbirth in Serra Leone;[7] and 60,000 children die before their fifth birthday from preventable causes in Burkina Faso.[8]

2. The Role of Government Tax and Spending Policies

Inequality is not inevitable: it is a product of policy choices made by governments. Having made global commitments to reduce inequality (Goal 10 of the Sustainable Development Goals is to "Reduce Inequality Within and Among Countries"), governments need to build development strategies that put tackling inequality front and centre. There is very strong evidence that progressive taxation and progressive spending have played a key role in reducing the gap between rich and poor in countries around the world.[9] Oxfam's May 2016 briefing paper ("The Time is Now: Building a human economy for Africa"[10]) has also shown Africa must act to: "crack down on tax dodging and maximize progressive revenues to invest in the classrooms, clinics and crops that will create a more human economy."

This report therefore aims to identify how the governments of Burkina Faso, Ghana and Sierra Leone, could enhance their fiscal policies (tax and spending) to combat inequality. It looks firstly at whether they collect the maximum progressive tax revenue; and secondly at whether they maximise progressive spending. Each country's national wealth dramatically affects its ability to collect tax and to spend, so Ghana is compared with other LMICs, and Burkina Faso and Sierra Leone with other LICs.

Box. 1. What is a progressive or regressive fiscal system?

A progressive tax system is one where wealthier individuals (and corporations) pay a higher percentage of their income or wealth in tax than do poorer citizens. A tax system is regressive when the percentage paid in tax decreases as the income or wealth increases.

Spending can also be progressive or regressive, that is, can benefit poorer or wealthier citizens more. Progressive tax, spending or overall fiscal systems will reduce inequality, while regressive systems will exacerbate inequality.

3. Are tax systems helping to fight inequality?

Maximising "progressive" taxation means taxing the richest corporations and individuals more in order to redistribute resources in society. The role of taxation in reducing inequality has been clearly documented in OECD[11] and developing[12] countries.

To assess whether countries' tax systems are progressive, this study uses three indicators, with data taken from the Development Finance International/Oxfam International tax progressivity database:

1. *Are the governments making enough effort to collect tax compared to their potential?*
2. *Are the governments designing and intending their tax systems to be progressive ?*
3. *Are the governments actually collecting taxes which have a progressive impact ?*

3.1. Governments are not collecting enough tax

Most African governments are not collecting as much tax as they could: while the average tax-to-GDP ratio has risen from 18% to 21% in the last 10 years, there is scope to raise this significantly.[13] Among the countries in this study, this is particularly true of Ghana and Sierra Leone. Ghana collects a higher level of tax/GDP, at 15.3% compared to only 14.3% in Burkina Faso and 9.7% in Sierra Leone (the second worst in the ECOWAS region). However, Ghana is much wealthier than the other countries, has more mineral resources (which yield high taxes) and relies less on smallholder agriculture (which yields much less tax): compared with an LMIC average of 24% it is not doing well.[14]

Both Ghana and Sierra Leone are collecting only half their "potential" tax revenues – with only Guinea-Bissau and Nigeria performing worse in West Africa - whereas Burkina Faso is collecting 73%.

Why are countries not collecting enough tax ? There are four main reasons:

1. **Tax Breaks.** All three countries offer widespread tax exemptions to corporations (as well as "deductions" on personal income tax), supposedly to attract investment and promote growth – and donors and foreign corporations usually request these: yet global analysis has shown that the vast majority of tax exemptions bring no such benefits. Sierra Leone has the highest level of published exemptions, 7-8 times its health and education budgets. Ghanaian and Burkinabe data are major underestimates: nevertheless, Burkina Faso's exemptions are at least twice its health budget and equal to education; and Ghana's are 80% of health and two-thirds of education. All three governments have recently begun to reduce exemptions, but could do much more.

2. **Extractives Sectors.** All three have historically failed to tax extractive sectors (mining and petroleum) sufficiently. In spite of IMF advice to tax oil companies at 50%, Ghana negotiated deals with petroleum companies at only 35%. In Burkina Faso, mining companies contribute

only 15% of revenue (compared with 60% of exports), and government was criticised for many years for giving lower tax rates (17.5%) to the mining sector, and exemptions to mines and cotton. All three countries have recently been revising their mining codes and renegotiating agreements with individual companies, but the benefits need to be closely evaluated by civil society through greater transparency of contracts and reporting on revenues.

3. **Tax Dodging**. Evasion, avoidance and illicit flows by corporations and individuals are widespread in all three countries. They are very hard to quantify, though data suggest that Sierra Leone is losing 10% of GDP a year, Burkina Faso 4% and Ghana 2% to illicit flows through trade mispricing alone.[15] Tax dodging by rich individuals also amounts to huge amounts of money, with many not even being registered for taxpaying in the countries. Virtually all of this dodging is by the wealthy, making the tax system much less progressive; and the poorer the country, the less resources and manpower it has to try to combat tax dodging, by thorough auditing, or to participate in complex global initiatives to combat dodging.

4. **Tax Treaties.** Tax treaties between countries were originally signed to stop taxpayers being taxed on the same income by two countries. However, they now cost developing countries large amounts of revenue because they set lower tax rates on dividends or capital gains, or lower deductions of upfront "withholding" taxes, from corporations headquartered in other countries. In worst cases, they allow corporations to avoid paying any tax in the developing country. All three countries have tax treaties, but they are much more prevalent in Ghana (12 compared to 3 in Burkina Faso and Sierra Leone). All three sets of treaties set low rates for withholding taxes, though in Ghana these are comparable to local tax rates. All three governments should renegotiate their tax treaties in order to increase their revenue.

For all three countries, it must be an urgent priority to collect more tax, by ending unnecessary tax breaks, taxing extractives more effectively, combating tax dodging, and renegotiating tax treaties. All have been changing their domestic policies to collect more, by increasing mining tax rates and reducing exemptions. However, these measures have been largely offset by falling commodity prices (and Ebola in Sierra Leone) – and they will require international support to eliminate exemptions on donor funds, agree to renegotiate treaties, and exchange information to fight tax dodging.

3.2. Governments should design tax systems more progressively

To fight inequality, it is also vital to design the tax system to be fair. This means having higher rates on higher-income individuals, and corporations, who can afford to pay more; and lower rates for the poor, thresholds below which they pay no tax, or exemptions for goods they buy.

In most countries, the greatest scope for designing a progressive tax system is in personal income tax. This is because it is often set at a higher rate for people with higher income, and a lower rate for lower income citizens, and because many of the poorest do not have to pay any income tax because they earn less than a minimum threshold for payment, or work in the informal (untaxed) economy. Taxation of companies ought also to be very progressive, because most countries do not have multiple rates, but companies with larger profits should pay more tax: but many large corporations dodge their taxes.

On the other hand, taxes on consumption (such as VAT and sales tax) are generally regressive because the poor consume a higher share of their income than the rich. However, governments can take specific measures to avoid this, such as applying a minimum threshold for VAT to exempt small traders, or exempting goods (such as basic foods) which are the main expenditures of the poor.

Taxes on financial wealth (capital gains and financial wealth) are usually highly progressive in that only the wealthier corporations and citizens tend to have major stocks of wealth; and taxes on property and land can be highly progressive if designed with higher rates for larger holdings.

How do the three countries perform ?

- Ghana's tax system has a less progressive design than its neighbours. It has low income tax rates, so the wealthy pay relatively little. Its personal income tax thresholds mean some relatively poor people pay tax, while many rich do not pay the top rate. It has one of the highest VAT rates in developing countries, though it does set a high minimum threshold and exclude many goods the poor buy. It could also do much more to tax capital gains, dividends, interest, property and wealth.
- Burkina Faso's tax system is also not designed very progressively, with relatively low rates of income tax, and its high top personal tax threshold may be letting some high earners pay too little. It also has a very high VAT rate, and does not set a minimum VAT threshold (meaning all traders have to pay), though it does exempt most products the poor buy. On the other hand, it has relatively high capital gains tax, and progressive property taxes.
- Sierra Leone has a much more progressively designed tax system, with a higher top personal income tax rate and fairer thresholds which exclude the poorer and make the wealthier pay top rates; and higher corporate tax rates. It also has a slightly lower General Sales Tax (equivalent to VAT) rate than its neighbors. On the other hand, it has no GST exemptions for basic foodstuffs, no capital gains tax, and taxes on rent, dividends and interest are well below those on income.

All three countries could take measures to design their tax systems more progressively, with Ghana and Burkina Faso increasing income tax rates and adjusting thresholds, Sierra Leone and Ghana improving efforts to tax wealth, and Sierra Leone reforming its GST.

3.3. Governments should collect their more progressive taxes

It is equally important to measure what is *actually* being collected, and its impact – also known as "incidence" on inequality. Across the world, if a country relies mostly on taxing natural resource wealth, corporations, personal incomes, property or wealth, this has generally been found to make its tax collection more progressive and redistributive. Conversely, an overreliance on indirect taxes (such as VAT; or customs and excise duties) tends[16] to be regressive, as the poor spend a larger percentage of their meagre funds on these goods. An overreliance on VAT can also make tax systems more regressive in their gender impacts, as women usually bear greater responsibility for caring for their families, and spend a greater proportion of their income on goods and services.

Unfortunately, indirect taxes are much easier to collect than direct taxes, especially in lower-income countries: while all pay indirect taxes automatically as they spend, direct taxes are often dodged for the reasons discussed in 3.2 above. As a result, VAT has tended to mobilise most of the taxes in lower income countries, making the actual tax collection potentially much less progressive than its design.

All three countries suffer from these characteristics of high indirect and low direct taxes, but to differing degrees. Burkina Faso collects 80% in indirect taxes, making its impact likely to be strongly regressive, whereas Sierra Leone and Ghana's indirect shares are only 60% and 55% respectively, making the regressive impact of these indirect taxes less strong.

As discussed in 3.2, the tax system's design can also help to make actual collection more progressive. So even if a country is relying mainly on indirect taxes, if these are designed to be less regressive (through exemptions and higher thresholds), their actual regressive effect can be minimised.

Analysis of the actual "incidence" of tax is available only for Ghana - It should be a national priority to conduct studies of tax incidence in Burkina Faso and Sierra Leone. They show that Ghana's personal income tax is very progressive, most indirect taxes are relatively neutral (including VAT because of the high minimum threshold for payment, and exemptions of basic goods), and taxes on cocoa exports are regressive. Overall, the tax system in Ghana is marginally progressive: but it could be much more so if government collected higher amounts of personal and corporate income tax.

All three countries need to increase collection of direct taxes – in part by making their design more progressive - thereby making sure that the rich, especially corporations, pay their fair share.

4. Is government spending helping to fight inequality?

Spending on public services (such as education, health and social protection) has a strong impact on reducing inequality – accounting for 69% of overall fiscal impact on inequality.[17] When governments invest in free public education and health services, the poorest don't have to pay for them, saving them very high shares of their regular earnings. If governments use their tax revenues to fund social protection systems (rather than asking people to fund their own protection), they also make direct transfers to poorer citizens, giving them an income boost.

Nevertheless, as with tax, spending within these sectors can be more or less progressively (or even occasionally regressively) designed, and therefore have varying impacts on inequality. For example, education and health spending may be better at fighting inequality if they focus on basic services (which the poor use most), and if they are targeted at poorer areas of the country.

To assess whether countries' spending systems are progressive, this study uses two indicators, with data taken from the DFI/OI Government Spending Watch database:

1. *Are the governments allocating enough funds to education, health and social protection ?*
2. *Is the spending progressively designed, and therefore having a progressive impact ?*
3. *What other types of spending may be limiting scope to fight inequality via social spending ?*

4.1. Governments need to spend much more to fund free health care

Health spending tends to be the most equity enhancing, as more poor people access public services, but can be regressive if spending is skewed to serving urban middle classes with expensive tertiary care, or if countries charge user fees for healthcare, excluding or bankrupting the poorest.

All three countries fall below the African Union "Abuja" commitment to spend 15% of their budget on health (Ghana 8%, Burkina Faso 10% and Sierra Leone 11%). They are all also below the "Chatham House recommendation" of US$86 per person to meet essential healthcare needs of all (Ghana US$32, Burkina Faso the furthest off at US$18, and Sierra Leone at US$21) –Burkina Faso and Sierra Leone are spending less than a quarter of the amount needed for basic healthcare for all their citizens.

Sierra Leone historically spent much less (around 6.5% of its budget in 2011), but increased spending thereafter to remove user fees for pregnant women, lactating mothers and children under five, under a Free Health Care Initiative (FHCI). The Ebola crisis led to a further dramatic scale up, with a doubling of "on budget" donor health, and it is vital that these funds be transferred into a long-term plan to strengthen the fragile health system. Low spending has brought severe health worker shortages – with some of the worst ratios of midwives to patients in the world, leaving many patients without care, or paying themselves – with 75% of heath care spending being private out of pocket payments.

Ghana has recently reduced the share of its budget going to health spending by around one third, due to its economic crisis, and this needs reversing, especially given that 29% of health spending is still from out of pocket payments. The National Health Insurance Scheme (NHIS) was supposed to provide free coverage for all, but continues to have issues with equity of access and outcomes. Things have improved since Oxfam has pointed out in 2012 that 82% of citizens were excluded and still paid user fees, and twice as many rich people were signed up as poor people.[18]

Burkina Faso also needs to raise its spending levels to comply with its April 2016 law making healthcare free for children under five, pregnant women, deliveries and caesareans, and breast and uterine cancer screening. If implemented, this policy could save the lives of 30,000 children each

year. [19] Given that 92.5% of women currently pay user fees,[20] and 37% of national health spending comes from out-of-pocket payments, this law will require a large scale up of financing.

4.2. Governments need to make education spending more equitable

Education spending tends not to be as progressive as it should, especially if user fees are charged and combined with other factors lead to high primary and secondary school drop-out rates for poorer children; or if high shares of budgets are allocated to upper secondary and tertiary levels of education which mainly benefit higher income groups. Conversely, investment in good quality basic education, with a strong focus on equity of provision and outcomes, especially early years' (pre-primary) education for the most marginalised children, can boost equality dramatically.

All three countries in this study fall within the ranges of spending recommended by the "Incheon Framework for Action" international recommendation to meet the SDG 4 education goals and targets by 2030 – to spend 15-20% of budget or 4-6% of GDP. There is not much difference among them, with Ghana and Burkina Faso spending 17% of budget and 5% of GDP, and Sierra Leone allocating 18% of its budget but slightly lower on GDP (4%) due to its low tax revenues. It is clear all three countries have prioritised education – though they could all do more to move to the top ends of these ranges.

Education spending has been found to be very progressive in Ghana, as there is strong support to pre-primary, primary and lower secondary. Particularly speculator progress has been made in terms of pre-primary education, on which Ghana spends more than 6% of its education budget, very high within sub-Saharan Africa,[21] and has achieved near-universal pre-primary enrolment. [22] However, it is still spending two-thirds of its education budget on secondary and tertiary education.

Burkina Faso's spending has been shown to be less progressive, even though the government is channelling over 65% to primary education. This is because very few poor children complete primary school:[23] as a result, the wealthiest 10% consume 50% of public expenditure, while the bottom 10% use less than 1%. Helping poorer children complete education in Burkina Faso will require additional support, like school meals, social protection spending, and investment in early years schooling.

In Sierra Leone, education spending is very skewed towards tertiary (31%) and secondary (23%). This is likely to have a regressive impact in a country where wealth is the largest factor explaining a lack of schooling (either entry, progression or completion through levels). For instance, 84% of the wealthiest quintile complete primary school, compared to only 34% of the poorest; for secondary school the figures are 41% and 1%. This means the richest are consuming the vast majority of resources.

4.3. Much more non-contributory social protection spending is essential

The impact of social protection on inequality varies greatly, depending on how it is financed, the type of programmes, and who is targeted. For instance, social protection spending on contributory pensions tends to support those in the formal economy (who tend to be wealthier, especially in lower-income countries), making social protection more regressive. However, non-contributory cash transfers, funded by tax revenues, can be both pro-poor and equalising, especially if they are comprehensive in covering a large share of the population.

All three countries are falling way short of the AU Windhoek Conference commitment by African governments to fund a basic Social Protection Floor, the cost of which was determined at 4.5% of GDP. In the most recent years for which ILO comparable data were available, Ghana spent most (2.3%), followed by Burkina Faso (1.8%) and Sierra Leone (0.61%).

In addition, all three countries have very unprogressive structures in their social protection programmes. Ghana spends virtually all its social protection funds on contributory pensions and other systems for civil servants, and only 0.02% of GDP on cash transfers. The Livelihood Empowerment Against Poverty (LEAP) cash transfer programme gives grants to those in extreme poverty and marginalisation. It has been shown to be very progressive, and highly effective in

addressing inequality. But it is currently too small to address inequality country wide, and needs to be scaled up.

Burkina Faso and Sierra Leone appear to have less regressive systems. Burkina Faso is spending 0.36% of GDP (around one fifth of the total) on non-contributory social protection, and Sierra Leone is spending around 0.1% of GDP (one sixth of the total). Both also have large contributory pensions for civil servants, but slightly more non-contributory spending.

All countries therefore need not only to spend a lot more on social protection, but to reorient spending massively towards their poorer citizens and to fund it from general tax revenues.

4.4. Spending must be better focused on inequality fighting sectors

Why are countries unable to spend enough on fighting inequality ? Because they are spending too much on other areas which have no impact on reducing inequality (such as debt service or defence or infrastructure), or might exacerbate inequality (eg energy subsidies, depending on their design).

Ghana is currently experiencing severe fiscal crisis due to large debt servicing: this was 60% of the 2015 budget, nearly doubling since 2012. This dramatic rise has squeezed budgets for the social sectors – debt service is almost 4 times the education budget, and 8 times health. Previous regressive electricity subsidies have now been ended, so the main candidate for freeing up fiscal space is debt reduction, which should be a top priority for Ghana. On the other hand, infrastructure (while responsible for some of the debt) is not a major share of government spending.

In Sierra Leone, debt service remains low at only 7% of the budget, and defence accounts for only 3%. However, one quarter of the 2015 budget was for road projects, and a further 9% for energy. There is a vital need to improve infrastructure, but it will be vital to assess whether this is reducing poverty and inequality. It is also important that any rises in one area are not off-set by decreases elsewhere. For instance, recent increases in health are being offset by lower spending in education.

In Burkina Faso, debt servicing remains relatively low at only 11% of total spending, infrastructure at only 8%, and defence at 5%. Government is spending a considerable share of its funds on other sectors which could in principle have an anti-inequality impact, such as agriculture (9%) and water and sanitation (5%). There is no obvious source of spending crowding out social spending.

4.5. All countries need to better tackle rural and regional inequalities

All countries in this study have large inequalities based on region and rurality. For instance, in Ghana, infant and child mortality is twice as high in rural areas [24], while 31% of children from the Northern region compared to only 3% in greater Accra have never been to school. In Burkina Faso in the Sahel region 74% of children have never been to school, while the Central region this is only 11%. Such inequalities are often mirrored in spending patterns. In Burkina Faso, poorer regions receive less: Boucle du Mouhoun and Nord – two of the poorest regions in Burkina Faso – received a combined 11% of all health care spending; while the wealthier Centre region received 29%.[25]

Addressing this must entail targeted strategies. International evidence shows that this requires additional resources channelled to each pupil in poor regions, and extra support with programmes such as school meals and transfers for school attendance.[26] Such investments in poorer areas pay off with better outcomes. For instance, in Ghana the same investment in school buildings in the North as in other regions, would lead to a four-fold improvement in the number of primary completers.[27] A number of countries, such as South Africa, Brazil[28] and Ecuador[29] have well developed systems of allocating spending to redress disadvantage, and all countries in this study could learn from these.

The final key way for governments to combat inequality through their spending is to undertake gender-responsive budgeting analysis, assessing the degree to which women benefit from all types

of spending. A recent comprehensive study assessing gender budgeting efforts around the world, marked most West African countries very poorly.[30]

5. Recommendations

Based on the detailed country case studies, and the evidence compiled above, the following areas have been identified as areas for action by the Ghanaian, Burkina Faso and Sierra Leone governments.

The Ghanaian government should focus on the following:

1. Tax

- **Enhance tax effort** by: clamping down on tax exemptions and deductions; increasing petroleum sector corporate tax rates; fighting tax dodging more effectively; and renegotiating tax treaties to allow higher withholding taxes, capital gains taxes and taxes on dividends.
- **Make the design of its tax system more progressive** by: increasing taxes on capital gains, inheritance and gifts to match income tax rates; increasing personal and corporate income rates to match regional levels, while raising minimum tax thresholds further to exempt poor citizens.
- **Make its tax collection more progressive** by: sharply increasing the proportion of taxes coming from personal and corporate income tax (by reducing exemptions, deductions and dodging), and capital gains/property/wealth taxes, ending taxes on cocoa exports, and increasing excise duties on bottled water and soft drinks.

2. Spending

- **Free up funds for anti-inequality spending by:** reducing the debt service burden, if necessary through debt restructuring and relief; and cutting regressive electricity subsidies. Given the very tight fiscal constraints in Ghana, this and revenue mobilisation most be the top priorities.
- **Increase spending on cash transfer programmes targeting the poor,** by dramatically scaling up the LEAP cash transfer programme into a comprehensive national social protection floor.
- **Increase the pro-poor and progressive nature of education spending,** by spending even more on primary and junior secondary education, as more poor children progress to higher levels.
- **Improve the progressiveness of health spending, and halt the reduction in spending overall,** in order to make the NHIS universal and reduce regressive out-of-pocket payments.
- **Address geographical inequalities through better constructed financing formulae**, to overcome continuing urban-rural and North-South divides.

The Burkina Faso government should focus on the following:

1. Tax

- **Enhance tax effort** by: reducing exemptions and deductions; fighting tax dodging more effectively on corporate and personal income tax; and renegotiating tax treaties to allow higher withholding taxes, capital gains taxes and taxes on dividends.
- **Make the design of its tax system more progressive** by: increasing taxes on capital gains, inheritance and gifts to match income tax rates; increasing corporate and especially top personal income tax rates to match regional levels, while reducing its maximum PIT thresholds to ensure that wealthy citizens pay their fair share; and introducing a minimum threshold for VAT to exempt small traders and their customers from VAT payment.

- **Make its tax collection more progressive** by: sharply increasing the proportion of taxes coming from personal and corporate income tax (by reducing exemptions, deductions and dodging), and capital gains/property/wealth taxes, introducing a minimum VAT threshold; and carrying out a detailed tax incidence study to measure the actual impact of taxes on inequality.

2. Spending

- **Make education spending more progressive,** by carrying out a detailed incidence analysis of education to identify how to make it more progressive, including by region and rurality; reorienting spending to be more progressive according to its findings;, and providing complementary support including school meals and cash transfers.
- **Boost health spending to deliver on the new policy of dropping user fees for children and women,** working towards universalizing free health care over the medium term.
- **Scale-up non-contributory spending on social protection,** with the long-term aim of achieving a universal social protection floor.
- **Address geographical inequalities through better constructed financing formulae**, to address continuing urban-rural and North-South divides.

The Sierra Leone government should focus on the following:

1. Tax

- **Enhance tax effort** by: reducing exemptions and deductions; fighting tax dodging more effectively on corporate and personal income tax; changing its GST into a VAT; and renegotiating tax treaties to allow higher withholding taxes, capital gains taxes and taxes on dividends.
- **Make the design of its tax system more progressive** by: increasing taxes on capital gains, inheritance and gifts to match income tax rates; perhaps reducing the bottom rate of personal income tax; replacing the GST with a pro-poor VAT including exemptions on basic goods but eliminating other exemptions; and reducing the minimum GST/VAT threshold to ensure middle-income businesses pay tax.
- **Make tax collection more progressive** by: increasing the proportion of taxes from personal and corporate income tax (by reducing exemptions, deductions and dodging), and capital gains/ property/wealth taxes; making the GST/VAT more progressive and reducing regressive exemptions; and carrying out an incidence study to measure actual impact on inequality.

Spending

- **Invest more in lower levels of education to increase impact on inequality, and reverse the overall education spending decline in 2016 budgets.** Based on a comprehensive analysis of education spending incidence, reconfigure spending to be more pro-poor and inequality busting, moving spending from higher levels to lower levels where most of the poor access education.
- **Sustainably increase financing for education to scale up fee-free health services**, firstly for women and children, as committed to in the Free Health Care Initiative (FHCI), with the long term ambition of achieving free Universal Health Coverage.
- **Scale up spending on social protection dramatically from current very low levels,** through non-contributory cash transfer programmes which can be gradually scaled up into a universal floor.
- **Address large scale spatial inequalities** through better targeted financing aimed at targeting geographical inequality.

Background

This study presents data on the analytical trends of revenue inflows and public spending and how these relate to economic inequality in Ghana, Sierra Leone and Burkina Faso. It looks at the three countries individually, and compared with one another, while also aiming to contextualise this within broader global and regional trends (where appropriate). This intends to build a strong evidence base for advocacy actions and messages of IBIS and partners.

This report takes as its starting point that progressive taxation and progressive social spending are strongly anti-inequality. Taken together, these fiscal policies helps to correct inequality by redistributing from rich to poor.[31] Conversely, when public social spending favours the wealthy in a society, or when tax systems are regressive, fiscal policies can actually exacerbate inequality.

This study therefore focuses on assessing the progressivity of tax and spending in each country in the study (see box 1). It does so through the lens of the likely or intended impact on economic inequality.
It then uses this evidence to identify areas where each of the government can take action to make their tax and spending work harder to redress inequality.

The first section presents the global evidence to back up these assumptions, and the methodology derived to analyse the countries from this evidence, including outlining the choice of data and analysis for the country case studies. This is followed by section two, which includes evidence from each country case study, as well as cross country comparison data in Annex 1 and 2.

The global evidence (section 1) and the country studies (section 2) follow the same formats:
1. Inequality analysis, evidence and data;
2. Outlining the detailed evidence for the impact of progressive taxation on inequality;
3. Outlining the detailed evidence for the impact of government spending on inequality.

Each country study has a list of detailed recommendations for policy change by the respective governments, which could also be used as key advocacy asks for civil society organisations.

SECTION 1. METHOLOLOGY AND DATA SOURCES

This first section outlines the methodology and data sources used to assess the three countries in this study. It firstly outlines the choice of evidence used to assess inequality in each country. It then looks at the evidence for the role that governments can play in fiscal redistribution; that is, how taxes and spending have been shown to tackle inequality across different countries, and, therefore, how this has driven the choices methodology and data on which to assess the countries in this study.

Inequality: explaining measurements and data used

This report looks at *economic inequality,* using the Gini and the Palma measures of economic inequality (see box 2 for more information). However, other inequalities are also of huge importance to poverty and social justice. Horizontal or group based inequalities, such as gender or marginalised ethnic groups, also intersect with vertical (income based) inequalities. Horizontal inequalities tend to be more country specific, based on geographic, demographic and cultural dynamics. Such inequalities also tend to have a huge impact on access to, and likely outcomes from, other critical factors for individual opportunities and wellbeing, such as level of education or health – in other words, the human development cost of inequality. As such, this report also touches on other areas of inequality, presented largely through data for the UN Inequality Human Development index (IHDI). The Inequality Human Development index (IHDI) combines a country's average achievements in health, education and income with how those achievements are distributed among country's population, when compared to the Human Development Index (i.e. without an inequality lens applied). Under perfect equality the IHDI is equal to the HDI, but falls below the HDI when inequality rises.

Box 2. Measuring inequality: The Gini and the Palma

The Gini coefficient is perhaps the most well-known measure of economic inequality, and is the most widespread tool used in measuring inequality and the income distribution of a country's residents, helping to define the gap between the rich and the poor. To assess a Gini score for a country a number, which ranges between 0 and 1, is given and is based on residents' income, with 0 representing perfect equality and 1 representing perfect inequality. The Gini coefficient is the most commonly used measure of inequality. Therefore, in this study, we look at the Gini coefficient in each of the three countries to assess whether they are in tackling inequality.

However, it is also vital to understand the extremes of distribution; that is the very poor, compared with the rich. In sub-Saharan Africa, where 35% of the population live in extreme poverty[32], an analysis which accounts for these levels of poverty, and not just the bottom, say, 10% is important. This is especially important for an organisation such as Oxfam IBIS who are interested in understanding the impact of inequality on poverty and the low income individuals and families. Therefore, we have also looked at the Palma ratio, which compares the income of the richest 10% against that of the poorest 40%. For both measures the authors have used the latest World Bank data.

Taxation: global evidence and methodology/data used for measuring tax progressivity

There is consensus globally that more equitable and progressive taxes are key weapons in reducing inequality. In almost all developing countries this will involve, firstly, increasingly domestic revenues through bringing in greater taxation revenues, and secondly, ensuring this is done "fairly".

In recent years, the amount of tax collected by developing countries has started to increase. However, overall, levels of tax collection remain much lower than in OECD countries, and in many

countries it is lower than the 20% tax-to-GDP ratio recommended by the UNDP. As a result, the budget available for basic public services suffers.

However, while increasing revenues through tax is important, it is also critical to make sure taxation is fair in order to ensure that tax can play a role which helps to address inequality, and that any expansion of taxation does not increase the burden on the poor. [33] Understanding the concepts of progressive or regressive tax systems is vital. If a country relies on taxation of resource wealth, corporate taxation, high incomes or taxation of property or wealth, while collecting less tax from those on low incomes, this would generally be considered progressive.

Conversely, a reliance on consumption taxes (such as VAT levied on food, fuel and other goods) *tends* to be considered regressive, as the poorest use these as well as the rich, and spend a larger percentage of their meagre resources on them.

In reality, tax systems in most countries are regressive (or at best are not progressive enough)[34]. One of the major issues in many developing countries is an overreliance on VAT: over the last 20 or so years VAT has become an increasingly important source of tax revenue in developing countries, meaning that many have raised more tax, but in a regressive way. While developed country economies tend to rely on VAT for about 30% of total tax revenues, in developing countries the percentage is often dramatically higher, averaging around 50%. In Latin America almost two-thirds of tax revenues come from consumption taxes (with VAT accounting for most of this).[35] This greater dependence on VAT as a source of revenue is often a result of pressures from international financial institutions and donors, but it is also because many countries have very large informal sectors and significant rural populations, from whom it is difficult for governments with weak tax administrations to collect income tax.[36]

But, in spite of conventional wisdom, VAT is not always completely regressive, and when assessing how regressive VAT is in a particular context, it is worth looking at specific items and the impact of the extra cost of VAT on the rights of the poorest and most vulnerable. For instance, tax systems can often also be regressive in their gender impacts too, as women are disproportionately affected, for example by consumption taxes: because they usually bear greater responsibility for caring for their families, they spend a greater proportion of their wages than men on goods and services.

In a progressive system, companies, especially rich multinationals, pay their fair share of tax. Taxation of companies is a very important part of any tax system, particularly in developing countries, where there are fewer possibilities for developing a strong tax base. Corporate taxation is also (theoretically) a relatively easy tax to implement, as often there are very few large corporations in low-income countries, making it less complex to administer.

Personal income tax also tends to be progressive, because it is often set at a higher rate for people with higher income levels, and many of the poorest have to pay none due to their work being outside the formal economy. However, income tax has tended to provide a relatively small (although growing) proportion of revenue in most developing countries, due to problems with tax administration capacity. Because tax administrations can be weak in low-income countries, taxes due to be paid by wealthier people or companies are often not collected properly.[37] In addition, many of the wealthiest members of society manage to avoid or evade their tax payments, and tax collection is way below potential levels, due to very high levels of tax dodging by corporations and wealthy individuals, and excessive tax exemptions that benefit elites or the most powerful sectors/companies (without proven evidence of adding value to the country). Fairer taxation must include greater tax being paid by big corporations, particularly multinationals; taking steps to curb tax avoidance; stronger taxation and royalty collection for extractive industries; and dramatically reducing tax exemptions and closing other loopholes which encourage tax avoidance, while also limiting the areas which unfairly burden the poor.

This study, therefore, assesses how well the three countries are doing in terms of raising more revenues through taxation, contextualising this in terms of the overall budget financing sources for each country, and it then assesses how progressively or regressively the tax is raised.

Cross-country measurements of tax progressivity are hard to find, due to a lack of data or studies with comparable methodology. Over the last 12 months Development Finance International (DFI), in collaboration with Oxfam, has compiled a Tax Progressivity Database, which allows analysis of tax progressivity across 155 countries.[38] In this study we have deployed the database and its methodology.

The database is underpinned by evidence about how tax systems can be progressive or regressive: it attempts to assess whether a country is collecting the maximum amount of tax in a progressive way.

It uses data to answer three critical sets of questions for each country, in three indicators:

Indicator 1: Is the Tax System designed to be progressive? This indicator attempts to look at how well designed a system is to tackle inequality (that is the degree to which tax rates, thresholds and exemptions are designed to minimize burdens on the poor and increase those on the rich) and inequality. The first way in which governments can show commitment to fight inequality through tax is therefore to design progressive taxes (as outlined above)

To assess whether countries are designing their tax systems to be progressive, we look at the progressivity of the three main sources of tax in most countries – personal income tax, corporate income tax and VAT/general sales tax. We then rank these – for personal and corporate income taxes, which are strongly progressive, we give them higher scores for higher rates; whereas for VAT/sales tax, we give them higher scores for lower rates.[39]

To assess whether the tax collected is actually progressive, we look at the share of different taxes in total tax collection, and their likely/actual impact or "incidence" on inequality, based on multiple global and national studies conducted in recent years. The "incidence" is assessed based on the composition of tax collected in each country, split between VAT, excise duties, customs duties, social security contributions. personal income tax and corporate income tax.

Indicator 2: Is Actual Tax Collection Progressive? The *actual progressivity* of the tax system (ie what proportion of their income people at different income levels pay in taxes) has a major impact on fighting inequality.[40] This second indicator attempts to look at what is really collected in taxes and how much impact this has on inequality. This is important to measure as this also helps to capture where tax is *actually* being collected, and the likely impact on inequality.

Many countries allow so many tax breaks that their "on paper" (i.e. Indicator 1) tax system and the "in reality" tax collection are very different.

Indicator 3: Are Countries Collecting Enough Tax Revenue? This indicator shows whether countries are collecting as much tax as they should. [41] This is vital to funding anti-inequality spending, and also helps to explain differences between indicator 1 and indicator 2 – in that countries which collect tax less effectively are generally failing to collect progressive income taxes, and so are actually less progressive than their "on paper" tax system suggests.

The last two indicators focus on showing the "in practice" progressivity and likely inequality impact of tax regimes. This is vitally important, as estimates of tax losses in reality are staggering. As discussed above, many developing countries are collecting much less than they can or should do. The amount of tax collected by a country, compared to the amount it could be collecting, is often undermined by domestic policy choices (eg exemptions or "sweetheart" deals for large corporations or rich individuals), international factors (eg treaties with other countries, tax dodging by multinationals and individuals, and demands for tax exemptions by donors or corporations), and low administrative tax collection capacity. [42] The IMF has produced reports including to the G20 demonstrating that the vast majority of tax exemptions are of no benefit for attracting investment

or promoting growth. Beyond corporate exemptions, low-income countries suffer additionally from demands for exemptions by aid donors – even for highly profitable private sector projects funded by their "development financing institutions" such as the International Finance Corporation (IFC) of the World Bank.[43] They also lose large amounts of personal income tax due to tax deductions for a wide range of expenses, especially private education, health and pension payments.

Tax dodging, that is avoidance (legal) and evasion (illegal) of taxes by corporations and individuals is also costing the countries in this study billions of dollars a year.

On the corporate side, the Independent Commission for the Reform of International Corporate Taxation (ICRICT) estimated that one element of these practices – companies shifting their profits to lower-tax jurisdictions – was costing developing countries a third of the tax they should be collecting.[44]

As for individuals, Oxfam has estimated that wealth being hidden offshore by "high net worth individuals" costs more than US$190 billion a year:[45] and many of these individuals are not even registered for taxpaying in their home African countries.

Virtually all this avoidance and evasion is by the wealthiest, making the tax system much less progressive; and it is the major reason why countries collect far less corporate and personal income tax than they should, sharply reducing revenues to spend on fighting inequality. The poorer the developing country, the less resources and manpower it has available to combat tax dodging, by auditing companies and individuals thoroughly, or to participate in complex global initiatives to combat profit-shifting, end bank secrecy and exchange information with other tax authorities.

Government spending: global evidence and methodology/data used

Collecting enough revenues, progressively, is only one half of the potential fiscal redistributive role that governments can play. These revenues must also be spent "progressively" - in other words with a focus on playing a strong redistributive role -to help tackle inequality.

Social spending, on public services such as education, health and social protection, has been shown to have a strong impact on reducing inequality. [46] Evidence from more than 150 countries, rich and poor alike, spanning over 30 years,[47] shows that, overall, investment in health, education and social protection tackles inequality.

This is because government spending helps to reduce income inequality, by compensating for unfair income and wealth distribution.[48] When governments invest in public services - especially health[49] and education[50] - and when this is heavily subsidised or, even better, free, the poorest don't have to use their earnings to pay for it. What's more, this tends to account for a far greater proportion of household income for the poorest than for the richest. This has been shown to boost household incomes for lower income households by as much as (if not more) than their regular earnings. If governments invest in social protection payments, especially when using tax revenues[51], they also make a direct transfer to a section of society, giving it an income boost. Both this "in kind" transfer and "direct" transfer therefore has a redistributive impact from richer sections to poorer sections of societies, and evidence has shown almost always shown to fight inequality.

Given the overwhelming evidence that education, health and social protection are key to fighting inequality, this study focuses mainly on spending levels in these three areas of spending. The paper identifies whether the countries are allocating enough resources to these areas, by comparing them with international or regional recommendations/commitments and against other similar countries – with this data summarised and compared in Annex 1.

For each sector, the study looks at overall trends in spending in 2013 to 2015-16 (latest available years) using the Government Spending Watch (GSW) database, and analysing budget documents for each of the three study countries.

The study also compares spending on each of the three sectors with other countries, by income group, and across sub-Saharan Africa, as spending tends to be relatively similar at country income and regional level - with graphs in the annex which show each country against other sub-Saharan Africa countries and according to their country income group. This, therefore, allows a comparator on which to judge each countries spending. This data is also drawn mainly from the GSW database, but is also
supplemented with other sources where required for cross-country comparison, including: World Health Organisation (WHO) spending data on health; UNESCO Institute of Statistics (UIS) for education; and ILO social protection data.[52] This is compiled and quality checked as part of the DFI global social sector spending database.

What is the likely or actual impact on inequality of social spending?
The study also looks at the likely impact that spending within each of the social sectors will have on inequality. This is because spending *within* each of these sectors, can be more or less progressive, and in some instances, regressive.[53] Across the three sectors in this study, generally, health and education are slightly more progressive than social protection, because more is spent in relative and absolute terms on those services that are more frequently used by the poor – this is especially the case for basic education and primary health care, which the poorest tend to access the most.

Health spending tends to be the most pro-poor as well as equity enhancing, due to more poor people accessing public health services. However, this too can be regressive, for instance, when spending is skewed towards serving urban middle classes with expensive tertiary health care. Moreover, many of the poorest countries still charge user fees for accessing healthcare, which excludes or bankrupts the poorest, and drives up inequality. For instance, existence of “user fees” can have a very detrimental impact on inequality, often leading to “catastrophic” [54], and “impoverishing” health expenditure by poorer households, or leading them not to seek care.[55]

While often pro-poor, education tends to not be as progressive as could be, and can actually be regressive in low-income countries with very low participation or completion rates in basic education. Some of these continue to charge user fees for primary school, and the majority charge fees for secondary school, which is very regressive. This also happens when a significant share of education budgets is allocated to levels of education which are disproportionately accessed by higher income groups. [56] By prioritising higher levels of education, some low-income countries are allocating most of their resources to educate those who were already the most advantaged at birth (because very few of the poorest make it through to secondary, let alone tertiary level), to the detriment of financing quality primary education for the most marginalised children. Conversely, investment in good quality basic education, with a strong focus on equity of provision and outcomes, especially early years’ education for the most marginalised children, can have a particular equality boosting impact,[57] makinganalysis of spending by level of education (between primary, secondary and tertiary) vital.[58]

Finally, the impact of social protection on inequality and poverty varies greatly across countries, depending, for example, on how this is financed, the type of programmes, who is targeted, and the wealth of a country. There is considerable variation across countries, and there also tends to be a mix of regressive and progressive spending within social protection itself.[59] For instance, social protection spending which is focused in low-income countries on contributory pensions, tends to support those in the formal economy (who tend to be wealthier). This tends to make social protection overall more regressive. But evidence shows that cash transfers when targeted at the

poor, and with tax revenues finding them, can be both pro-poor and equalising. As a result, this study focuses on cash transfers which are non-contributory, where possible in the country studies.

For the country studies below we analyse the likely impact on inequality according to the likely progressive or regressive nature of spending within each sector using a "benefit incidence study" estimates (that is using estimates for the amount by which it reduces the Gini coefficient/inequality).[60] This is then complemented by a more in-depth analysis of specific spending programmes in the country, as well as an overview of the total budget spending, highlighting areas which are likely to have the least impact on tackling inequality.

Box 3. Social protection: measuring contributory and non-contributory spending

Contributory schemes, such as pensions, tend to have very limited access for those outside the formal economy. This means in countries with large informal economies any such schemes are likely to miss those most in need, and the poorest - not least as this on low and irregular incomes means they cannot save on a regular basis, and/or there is no counterpart (such as the employer) to match contributions of the worker. Finally, contributory schemes tend to miss those not in employment at all, such as women caring for children, people with disabilities, etc.

This limits the capacity for such schemes to tackle inequality and poverty. It is for this reason that non-contributory, tax financed cash transfer schemes, can be the best tool for tacking inequality and poverty, and why in this report we distinguish between spending on social protection which is "contributory and non-contributory" (see figure one below). When analysing budget figures, as part of the detailed budget analysis, we only classify non-contributory social (measuring both, according to data availability). However, we have also obtained and analysed figures on social spending, which includes non-contributory and contributory social protection (as there is no way for this to the two types to be analysed differently in this data set), for a larger cross country comparable data set on "total social sector spending". This is indicated in the text as "social sector spending, including contributory and non-contributory social protection".

It is also worth noting that the study also addresses, where appropriate, whether spending is also likely to be pro-poor, as well as equity enhancing. This is because social spending can tackle and make a country more equal, even if the spending is not focused more on those at the very bottom.

What's the total composition of spending?

The report also attempts to breakdown the overall budget, identifying areas of government spending which are unlikely to impact on inequality, notably debt servicing and defence. This is because not only does spending on social services matter, but how the overall budget is split also matters, given there is strong evidence to suggest that the *composition* of budgets also matters. In other words, the more of the total budget spent on areas likely to smooth out inequality, such as social services, compared to government spending which might actually exacerbate inequality (eg energy subsidies), or spending which might have a neutral impact but be crowding out anti=-inequality spending (i.e. debt servicing), the larger the inequality impact.[61]

Where available, the study also identifies other type of spending which might be likely to as well as programmes specifically trying to combat geographical inequalities. Notably, spending on Water, Sanitation and Hygiene (WASH) - where spending data is available – and on agriculture. For instance, there is also evidence to suggest that WASH spending has an impact on inequality and poverty, as well as being central to tackling gender inequalities, enabling women to spend less time on unpaid work.[62] Women in poorer countries face even higher inequality in care work because a lack of infrastructure, technology and public services means they spend more time in their day looking after their home and family. In Sub-Saharan Africa, women spend 5 billion hours a year

collecting water because there are often no water sources nearby.[63] Therefore, where available, we have included WASH spending where data are available (Ghana and Sierra Leone). However, there is very limited data availability on WASH spending data in Burkina Faso. While agriculture can be very important also; African leaders recognized in the Malabo Declaration in 2014[20] that for growth in Africa is to be inclusive and is to tackle rising inequality, it must be rooted in agriculture, and above all in small-scale agriculture. However, spending on agriculture by most African government tends to be focused on larger scale support and very little funds dedicated to anti-inequality or pro-poor efforts (eg agricultural subsidies and inputs targeted to smallholders).

SECTION 2. COUNTRY PROFILES

Ghana country case study

1. Inequality in Ghana

The second largest economy of the western Africa region, Ghana has recorded growth of real GDP by 5.8% between 2000 and 2009.[64] Since 2005, despite the international financial crisis, Ghana showed higher annual average growth rate of 7%, enabling Ghana to move from being a Low-Income Country (LIC) to a Lower- Middle Income Country (LMIC). This was also matched by reductions in poverty levels in Ghana, as these fell from around 50% in 1990 to 25% in 2014.[65]

However, this growth and overall poverty reduction has not been matched by a decrease in income inequality. In fact, the Gini Index rose from 37 in 1992 to 42 in 2006 against 46 in 2011 (latest available data). This shows that although the level of poverty declined between 1991 and 2006, no change was observed in terms of inequality reduction.[66] Further, the Palma ratio averaged 2.2, demonstrating that the 10% rich households in Ghana receive 2.2 times the total income of the poorest 40% in 2011 (latest available year). In short, total poverty is reducing in Ghana, but economic inequality is on the rise, and many of the poorest are missing out on overall growth and increases in national wealth.

The Human Development Index showed a score of 0.579 in 2014 against 0.541 in 2011; when adjusted to inequality (IHDI), the score is 0.38, suggesting a 33.1% loss in quality of life due to inequality. During the same year, the gender inequality index surged to 0.554, above the world average (0.449).

Furthermore, there are large geographical based inequalities. For instance, infant and child mortality are more pronounced in rural than urban areas with infant mortality rate estimated at 106 deaths per 1,000 live births for the poorest households, against 52 deaths per 1000 live births for the richest households.[67] According to World Education Inequalities (WIDE) database from the UNESCO Global Education Monitoring report, Ghana has large inequalities in terms of regions and ethnicity. For instance, 31% of children from the Northern region compared to only 3% in the greater Accra region have never been to school; while only 25% of children in the Northern region completes secondary school, compared to 69% in greater Accra. These are urban-rural and regional inequalities matter also in terms of fiscal policy.

2. Tax policy in Ghana – is it progressive and combatting inequality?

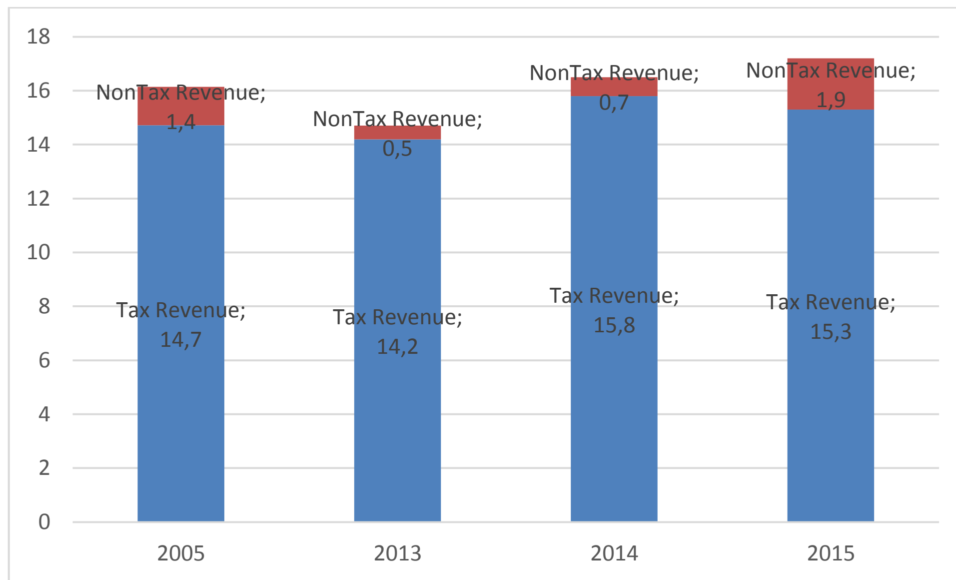
2.1. Is Ghana collecting enough tax?

Ghana has been performing relatively badly in terms of revenue raising (see chart 1). It has a total revenue/GDP ratio of 17%, and a tax to GDP ratio of 15.3% (the difference reflecting non-

tax revenues mainly from oil and gas).[68] As shown in Annex Chart 26, This puts its tax to GDP ratio below average in West Africa, with Benin, Burkina Faso. Guinea- Bissau, Nigeria and Sierra Leone performing worse.

Moreover, in spite of GDP growth moving it into Lower-Middle Income status, Ghana’s revenue and tax to GDP ratios stagnated during 2004-13. It was not until the government began to receive oil and gas revenues, and to take new measures to reduce the fiscal deficit (including a clampdown on exemptions) that these rations rose significantly in 2014-15.

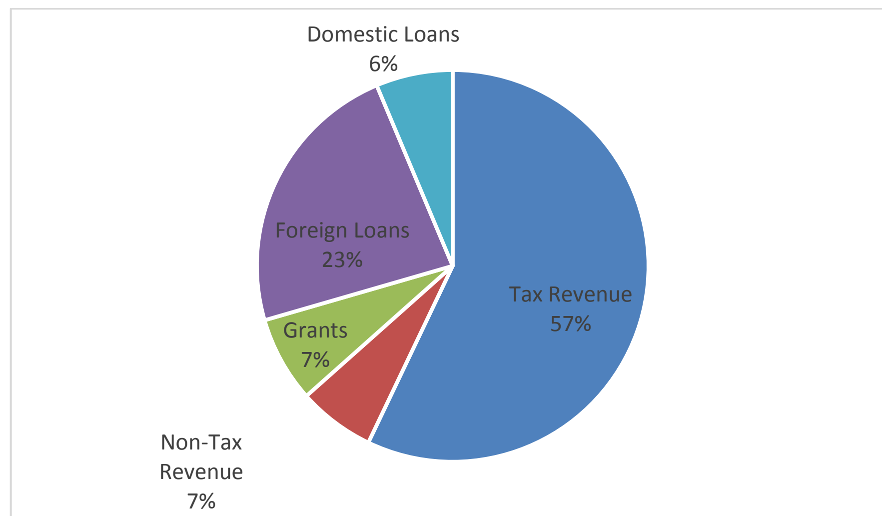
Chart 1. Ghana's revenue collection as % of GDP (2005 and 2013-15)



Source: IMF Country Documents

Chart 2 shows the overall sources of financing for Ghana's budget in 2015. Revenue represents around two-thirds of the total, of which tax revenue is around 90%. Grants and domestic loans are both relatively small, but foreign loan disbursements are very large, increasing debt. Only around a quarter of these loans are aid (concessional), whereas three quarters is non-concessional. This means that aid funds only around 12% of Ghana's budget, down from around 35% ten years ago: this reflects Ghana's graduation to LMIC status, which has led to falls in aid.

Chart 2: Ghana's Budget Financing Sources (2015)



Source: IMF Ghana Country Report 16/321, October 2016

What are the reasons for the revenue shortfall?

1. large **tax exemptions and deductions** are mainly responsible. Ghana has a very complex list of special regimes for foreign investors, sectors, regions, smaller enterprises, start-ups and export-

oriented investments, as well as deductions for reinvestment and training. It has also negotiated a wide range of ad hoc deals giving companies lower tax rates. Ghana began publishing the scale of its tax exemptions in 2007,[69] showing very considerable losses from tax expenditures averaging 3% of GDP or 23% of tax revenues. This amount of US$1.3 billion a year represents two-thirds of the education budget and 80% of the health budget.[70] It is widely regarded (including by the IMF) as a considerable underestimate of the scale of exemptions, because it covers only some of the formal exemptions. The Ghanaian government, aware of the reduction in tax revenues this has brought, has recently begun to streamline exemptions, for example ending those on tourism in 2015. On the personal income tax side, there are a large number of deductions which mainly benefit wealthier taxpayers, including for health insurance, education fees and pension contributions.

2. A second reason has been a **failure to tax extractives sufficiently**. Based on calculations of the actual profitability of gold and bauxite operations, and the potential profitability of oil and gas investments in 2008-09, the IMF advised Ghana to increase CIT rates on new projects to 35% for mining and 50% for petroleum. However, government then negotiated ad hoc deals with petroleum companies taxing them at only 35%.

3. A third reason is **tax dodging** – through evasion, avoidance and illicit flows by corporations and individuals. These are very hard to quantify though Global Financial Integrity (GFI) data have suggested that Ghana is losing US$401 million a year (under 2% of GDP) due to illicit flows through trade mispricing alone.[71]

4. A final reason is the influence of **tax treaties**. Ghana has signed treaties with 12 countries (Belgium, Denmark, France, Gambia, Germany, Italy, Netherlands, Nigeria, South Africa, Sweden, United Kingdom). These set low rates for the taxes Ghana can deduct up front from companies headquartered in these countries (withholding taxes) before they can start shifting profits out of Ghana, and therefore reduce Ghana's tax revenue. However, they have had less effect on reducing tax revenue than in other countries, because Ghana has set very low withholding tax rates (between 8% and 20%) which are generally similar to the ceilings in the treaties (ie Ghana has deprived itself of withholding taxes).

2.2. Is Ghana designing its tax system with an intent to be progressive?

To assess the "structural" or intended progressivity of Ghana's tax system, it is necessary to look in turn at each of its major taxes:

- **Personal Income Tax:** Ghana's top rates are well below African and LMIC averages at only 25%; and its lowest rate of 5% is also among the lowest worldwide. Its minimum threshold for paying personal income tax is less than one third of per capita GDP, making it one of the lowest in the world and ensuring that some relatively poor taxpayers are included in the tax net. On the other hand, its top tax threshold is almost 20 times as high, a much wider range than in most countries, implying that some high earners may not be paying their fair share of tax. Recently, government has increased thresholds more sharply for low earners to try to remedy this.
- **Value Added Tax**: Ghana has increased its VAT rate from 12.5% to 17.5% since 2003 (though labelling the first 2.5% increase as a levy to cover extension of the national health insurance scheme), with the last increase in 2015. On both occasions, Ghana followed IMF advice, and had little choice because it had gaping budget deficits and needed to use all options to fill them. It now has one of the highest VAT rates in developing countries, well above LMIC and African average. Recently, it has focussed on broadening the coverage of the VAT by eliminating "unprogressive" exemptions – for example in 2014, including the financial sector, domestic airlines and haulage companies. It also has a wide range of "pro-poor exemptions" including

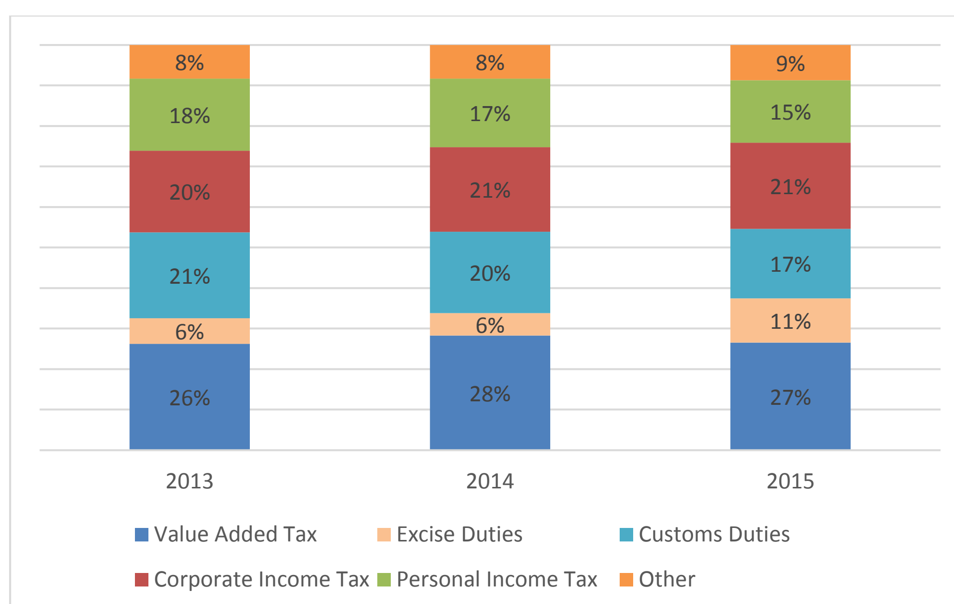
basic foodstuffs, health, public transport, water and electricity. Ghana also has relatively high VAT thresholds at 25 times per capita GDP, meaning that smaller traders and their (poorer) customers are largely exempt (though these have been frozen since 2013).

- **Corporate Income Tax**: Ghana cut its CIT gradually from 32.5% in 2001 to 25% in 2006, engaging in an active "race to the bottom", encouraged by higher resulting scores in the World Bank's Doing Business Index. It has kept it at that level since, placing it in the bottom third in West Africa where rates range from 15% to 35%, with only Cape Verde having a lower rate. Recently, other countries such as Cote d'Ivoire have justified similar CIT cuts on the grounds of maintaining competitiveness with Ghana – even though WAEMU has tried to combat this by setting a minimum CIT rate of 30% (Action Aid 2014).
- **Other Progressive Taxes:** Ghana has in 2016 increased its very low capital gains tax rate of 15% to 25%, matching income tax rates and removing scope for tax arbitrage by companies and individuals. It also has low taxes on dividends and interest of only 8%. Ghana's property taxes are also very low: it taxes rental income at between 8% (residential) and 15% (non-residential), and property value at between 0.5% and 3% (varying by region). Its wealth taxes – insofar as they exist at all - are similarly low: it has no inheritance tax and its taxes on gifts range from 5% to 15%.
- **Other Generally Regressive Taxes:** Ghana has a social security rate of 18.5%, marginally below global and LMIC averages, and slightly above the African average. Its excise and customs systems still have less regressive structures, with higher rates on luxury goods and lower on basics.

2.3. Is Ghana collecting progressive or regressive taxes ?

As shown in Chart 3, Ghana collects approximately 55% of its taxes from indirect taxes (VAT, excise duties and customs duties), which have been found globally to be regressive, and around 30% of its tax from VAT. On the other hand, it collects relatively little (only 1%) of its revenue from social security, which has been found to be even more regressive than VAT. Collection of direct tax has, however, increased from 30% to 45% of the total since 2000, due to increased corporate and personal income, and the exploitation of oil and gas resources.

Chart 3. Breakdown of Ghana's total tax collection by type of tax



Based on incidence coefficients derived from Martinez-Vazquez et al, Ghana's tax system should be marginally regressive, increasing the Gini by around 0.006. However, Ghana is the only country in

our sample to have benefited from a recent actual incidence analysis using the Ghana Livings Standards Survey, undertaken by the Commitment to Equity (CEQ) initiative. Its results show that personal income tax in Ghana decreases inequality by 0.009 (quite significantly), but has a relatively marginal effect on poverty, whereas indirect taxes have an insignificant effect either way on inequality, but increase poverty significantly.[72] In more detail, PAYE income taxes are highly progressive, as are presumptive income taxes on the formal sector, with presumptive income taxes on the informal sector being less progressive due to the smaller scale of most informal businesses. Among indirect taxes, VAT and import duties are virtually neutral, while taxes on cocoa exports are highly regressive. Excise duties on bottled water, soft drinks and most alcohol are progressive, those on petrol are virtually neutral, and those on tobacco products are regressive. Overall, the tax system is found to be marginally progressive, reducing the Gini by 0.013, which would place Ghana around 50th of 155 in terms of tax progressivity.

What explains these results ? The relatively small effect of direct taxes reflects their relative lack of progressivity (compared to other countries) and large problems with collection (the productivity of PIT in Ghana – the extra amount collected for each $ of GDP – is very low at only 11 cents) due to exemptions, deductions and dodging. The surprisingly neutral effect of VAT and import duties reflects the existence of widespread exemptions, for both pro-poor and non-pro-poor reasons, which mean that its productivity is also relatively low at only 27 cents per $ of consumption. Trends over time (decreasing progressivity of PAYE since 2010 and sharply decreasing regressivity of VAT since 1987) also reflect increasing exemptions as well as large increases in VAT thresholds.

However, this analysis does not include the impact of corporate income tax and other direct corporate taxes, which are around 20% of total revenue. These should in principle be among the most progressive taxes - but have potential to be regressive if there is widespread exemption and dodging. Depending on the impact of these factors, they could be increasing progressivity by reducing the Gini by around 0.03, or having virtually no impact at all on inequality.

3. Government spending in Ghana: is it combatting inequality?

3.1. How much is Ghana spending on key inequality busting social sectors?

Ghana spends slightly above average proportion of its budget on the three social sectors of education, health and social protection (non-contributory and contributory), when compared to Low-Middle Income countries, ranking 19th among 44 Low-Middle Income Countries (LMICs) in 2015 (see chart 25 in Annex 2). When compared to other LMICs on sector specific spending, Ghana tends to spend more overall on education than many other LMICs, slightly less on health, very much in the middle on social protection (with contributory social protection, included).

On education, in 2016, Ghana was spending 17% of budget, and 5% of GDP on education, meaning the country is meeting the overall Incheon targets of spending 15-20% of budget and 4-6% of GDP. On health they are spending 8%, which is below the Abuja commitment, and as mentioned above is also below similar income country groups.

One notable feature of Ghana's spending when looked at over a three-year range is it has been making marginal decreases in the areas of health and education. This is perhaps most notable in health, which has fallen from 12.5% in 2013, to 8% in 2016, moving it further away from the Abuja target of spending 15% of budget on health. Another international recommended measure for health spending – the so called "Chatham house recommendation" – is that governments should spend US$86 capita per year to ensure essential and basic health coverage. Ghana is below this at around $32 in 2015 (down from $41 in 2014). This would mean that Ghana would need to more than double spending to meet this target.

Finally, both WASH and social protection spending are reducing. Spending on social protection, in particular, is low by LMIC standards. Even including contributory spending, latest figures show this to be standing at 2.37% (in 2011[73]). When only looking at only non-contributory social protection spending – i.e. that which has the largest impact on poverty and inequality - this is currently below 1% of budget, and is low compared to other similar income group countries.

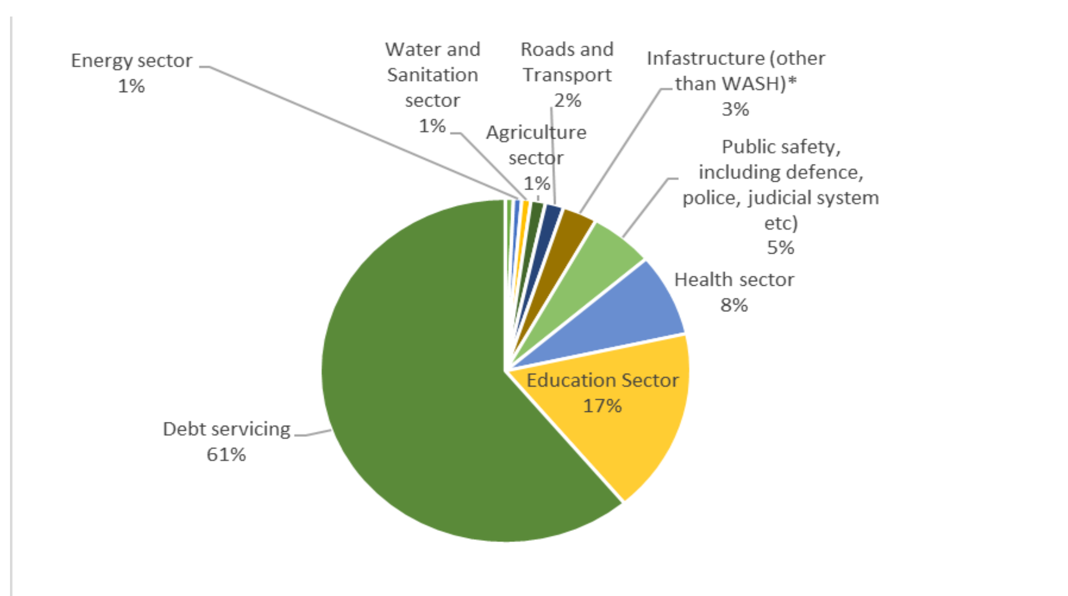
Table 1. Ghana overall breakdown of budget, 2016

Sector/spending area	% of budget
Social protection, excluding contributory schemes*	0.7%
Energy sector	0.7%
Water and Sanitation sector	0.8%
Agriculture sector	1.3%
Roads and Transport	1.6%
Infrastructure (other than WASH) *	3.0%
Public safety, including defence, police, judicial system etc)	5.6%
Health sector	7.8%
Education Sector	17.4%
Debt servicing	61.0%

Source: Government Spending Watch analysis of budget (including classfication by the GSW), this is based on budget publications, and pre-existing budget analysis by GSW.

*Social protection excludes contributory pensions, social security payments and gratuity payments.
**Water and Sanitation is extracted from other infrastructure spending
***Debt servicing is actual 2015 data, and therefore a slight overestimate as other actual spending was cut during the year.

Chart 4. Breakdown of overall budget categories Ghana, 2015 planned



The reduction in the share of spending on social services over the last three years, in large part reflects spiralling debt levels. After receiving US$7.4 billion in cancellation of its external debt between 2000 and 2005 due to the Heavily Indebted Poor Countries (HIPC) and Multilateral Debt Relief (MDRI) Initiatives, Ghana has borrowed extensively since 2005, both externally and domestically, so that debt has risen from 25% to 73% of GDP. The external debt has increasingly been owed to commercial creditors, which have risen to 25% of the total as Ghana has issued US$5 billion of Eurobonds. In addition, domestic debt service costs have risen sharply due to high deficit financing needs and inflation levels, pushing interest rates up to 20-30% and making domestic debt responsible for 54% of debt service. About 85% of the borrowing has been for budget financing, due to large budget deficits around election periods, as well as the need to borrow to repay earlier loans as they have fallen due. The remaining 15% has been spent about three quarters for infrastructure, and a quarter on social and productive sectors. Since 2015, the debt burden has also been exacerbated by falling oil prices which have led to other spending cuts and increased the share of debt service in total spending. The fall in the Ghanaian cedi also increased external debt costs in cedis, as well as exacerbating inflation through import price rises, which pushed up domestic debt interest rates.

Debt service rose from 35% of the budget in 2012 to 61% in 2015. Given the fall in aid over the last decade, it looks as though in 2016 Ghana might for the first time pay more in external debt service than it receives in foreign aid. This has left Ghana with reduced fiscal space on which to spend on critical social services, with chart 5 and table 2 above showing that debt service is more than 3.5 times education spending, and almost 8 times as high as the health budget for 2015. In spite of efforts to protect the social sectors, they have seen cuts in the last two years.

1.2. What do we know about sector spending, and its inequality effect in Ghana?

A number of detailed benefit incidence analyses have been carried out in Ghana. The most recent of these, looking at both tax and transfers by the Commitment to Equity (CEQ) project, has identified areas where Ghana is spending very progressively, which is helping to address inequality, and less progressively, in their overall social sector spending. [74]

Using this analysis and applying this to the latest budget figures, this study estimates that two-thirds of the overall inequality reduction is accounted for by spending on education and health: spending on education is the most inequality-reducing (accounting for around two-thirds of the reduction in Gini from government spending), partly because Ghana spends a high share of its education budget on pre-primary, primary and junior secondary schooling, which benefit lower-income groups. Overall, public spending on pre-primary, primary, and junior high school is also quite progressive, more so than is typical in middle-income countries.

The CEQ study also identified (pre-)primary education spending as having excellent targeting and as very inequality reducing. Significantly, since this study Ghana has increased spending and now allocates more than 6% of education budgets to pre-primary education, which was the highest level from a sample of sub-Saharan African countries.[75] As a result, Ghana has achieved moved from enrolment in of only 28% just a few years ago to near-universal pre-primary enrolment in 2015. [76]

The expenditure which the CEQ found best targeted to the poor is the free school feeding program for selected primary and junior secondary schools. The government has committed to an expansion in the 2016 budget year to of the school feeding programme to cover 3,000,000 pupils nationwide. The school feeding programme has been shown to particularly help re-dress geographical inequalities. Ensuring this continues to play a vital role in inequality is a key opportunity.

The split of spending below, shows how this is currently being allocated, which could certainly see a larger proportion allocated to pre-primary. With a new commitment to make secondary education progressively free from the 2015/2016 academic year, there will also be a need to do so mindful of ensuring this helps make spending more progressive, especially (See table) as there is already a marked concentration of spending on secondary (and this is currently relatively progressive). However, as the government scales up secondary even further, and make this free, it will be important to maintain budgets at pre-primary, primary and within lower secondary, given the progressivity of this spend, to ensure no child is left behind.

Spending on health is somewhat less progressive (accounting for only around one third of the reduction in Gini due to government spending), because although the public health system and health insurance have been expanded to cover most of the population in recent years, health spending is only around 2/3 the level of education, and some lower-income patients remain uncovered by health insurance and discouraged by OOP payments needed to access care. Finally, in terms of health, expenditures were seen to be about average in the CEQ study, in terms of their impact on inequality. However, the NHIS has come under a lot of scrutiny for its inequity in terms of access and outcomes. For instance, as Oxfam has pointed out in 2012, as many as 82% of citizens remain excluded. Twice as many rich people are signed up to the NHIS as poor people. 64% of the rich are registered compared with just 29% of the poorest. In other words, the middle class are more likely to capture spending, and poorer are less likely to access it, yet, those excluded from the NHIS still pay user fees, as this is heavily subsidised by VAT.[77] Moreover the WHO/World Bank have shown that Ghana is very susceptible to "catastrophic out-of-pocket expenditure" (see above explanation), at least one quarter of the population was further pushed into poverty, as a result of this.[78] The same Oxfam report also identified ways inefficiencies in health spending which could help to increase funds for health by decreasing inequalities and inefficiencies which would seem especially critical in terms of decreasing spending available due to debt servicing needs in recent year. However, even in light of this decreased fiscal space it is really important that Ghana does much more to reverse declining spending, which makes expanding progressive spending and eliminating fees every more out of reach.

The CEQ study also highlighted the Livelihood Empowerment Against Poverty (LEAP) Programme as being a very progressive programme overall. The LEAP programme is a cash transfer programme, and gives cash grants to those in extreme poverty and marginalisation, for instance, in 2016 it supported 2,100 beneficiaries with hearing difficulties with hearing aids. However, the overall size cash transfer social protection programmes in Ghana was shown by CEQ to be too small to have a large impact on inequality, (even though it has the highest marginal impact on inequality).[79] Given this, an expansion of LEAP could have a much larger impact on inequality. In the 2016 budget the government of Ghana committed to expanding the LEAP to expand to cover 116,000 beneficiaries in 180 districts in all the 10 Regions in 2015; to 250,000 beneficiary households, and further future expansion.[80] It should be noted that when contributory social protection – i.e. pensions and other contribution schemes – are included into social protection spending this has the impact of making overall social protection spending more neutral.

In the CEQ incidence study, indirect (mostly electricity) subsidies were measured to be higher in Ghana than the other countries. The three indirect subsidies for fertilizer, kerosene, and electricity were found to have different incidences. The fertilizer subsidy was equally distributed across incomes, with a largely neutral impact. The subsidy for electricity was regressive; electricity consumption is more concentrated among richer households than poorer ones. Subsidies were virtually eliminated in the 2014 budget and therefore are not a viable source for spending savings.

Finally, across all spending to redress inequality in Ghana, there are large urban-rural divides. The poverty reduction policies of 1990-2010 were more favorable to populations living in urban and southern areas, and less so to rural and northern residents. Ghana would do well to address their geographical inequality through better constructed "equitable spending formulas". This often applies to certain sectors too, and can mean focusing more resources on addressing inequality. For instance, a pilot study in Ghana, under the Simulations for Equity in Education (SEE) Project, illustrates the strong cost-effectiveness argument to be made for targeting resources towards marginalized children, (as oppose to a flat equal distribution per child approach). The study showed that if 500 pre-primary schools were built and spread evenly throughout the country, the number of primary completers would total 6,202. However, if these schools were situated in the North of the country and in those districts where 90% or more of the children come from poor households, then the number of additional primary completers would equal 27,327. In other words, for the same investment there would be an almost four-fold improvement in the numbers of primary completers, provided that resources are targeted towards disadvantage focusing on both region and poverty. It is critical to overcome previous regional inequalities that Ghana applies both an analysis to overcoming inequality and addressing this through spending formulas to address this within all social sectors and within the budget.[81]

4. Conclusions and Recommendations

Economic inequality is on the increase in Ghana, which is also impacting on the fight to reduce extreme poverty. Large parts of the Ghanaian population remain locked out of the gains from growth. This is compounded by large inequalities which also exist within Ghana based on region and rurality. It is crucial that the Ghanaian government works to address this spiralling inequality.

Overall, according to the DFI/OI tax structural progressivity index, Ghana comes in the bottom third of countries, scoring particularly badly for very low personal and corporate income tax rates. Only Cape Verde and Guinea-Bissau in West Africa score lower. In other words, Ghana's tax system is not progressive, when compared to its neighbours - or globally. It could also do a great deal more to tax capital gains, property and wealth to build a more progressive tax system "on paper".

Moreover, according to the DFI/OI tax incidence indicator, Ghana is approximately halfway down the tax incidence index, with a tax system which is marginally progressive. Its tax system is doing very little – and could work much harder - to tackle inequality. The very high levels of corporate tax exemptions and dodging, resulting in low corporate income tax collection, explains much of this, and emphasises the need to increase the progressivity of the tax structure, and collect more income tax.

Moreover, Ghana is estimated to be losing $1.3 billion a year, giving away exemptions equalling 3% of GDP or 23% of current revenues, 65% of the education budget or 80% of the health budget. In a country struggling with mounting debt, collecting more tax progressively, by halting unnecessary exemptions and taxing the wealthier better must be an urgent priority.

On the spending front, Ghana is currently experiencing severe fiscal restraints due to large debt servicing eating into the budget available for spending on the "equity boosting" social sectors. This has seen budgets reduce in recent years on the social sectors. Reductions in budgets are most marked in health. Given that health and education account for two-thirds of the reduction in inequality as a result of social spending, it is absolutely vital that any reductions in health spending are reversed, and greater allocations help scale up access for the poorest, and ultimately move towards universal health care. Moreover, the existing health budget needs to work better addressing inequality and to increase inefficiencies in the system.

Education is seen to be very progressive in Ghana, not least the focus on supporting pre-primary, primary and lower secondary. Particularly speculator progress has been made in terms of increased allocations to pre-primary meaning there is now near universal enrolment. The Ghanaian government should be commended on this, and must continue to ensure that education spending remains progressive and thus helps to fight inequality – especially in these fiscally restrained times and with greater pressure towards expansion at higher levels.

Social protection could be made to work much harder to combat inequality. The LEAP programme has been shown to be highly effective in terms of addressing inequality but too small in coverage to help address inequality. This should be scaled up as a key tool in addressing inequality.

Finally, addressing geographical inequality must be improved through better analysis of the budget and the use of equity spending formula.

The priority recommendations to make Ghana's fiscal policy fight inequality better are:

1. Tax

- **Enhance tax effort** by: clamping down on tax exemptions and deductions; increasing petroleum sector corporate tax rates; fighting tax dodging more effectively; and renegotiating tax treaties to allow higher withholding taxes, capital gains taxes and taxes on dividends.
- **Make the design of its tax system more progressive** by: increasing taxes on capital gains, inheritance and gifts to match income tax rates; increasing personal and corporate income rates to match regional levels, while raising minimum tax thresholds further to exempt poor citizens.
- **Make its tax collection more progressive** by: sharply increasing the proportion of taxes coming from personal and corporate income tax (by reducing exemptions, deductions and dodging), and capital gains/property/wealth taxes, ending taxes on cocoa exports, and increasing excise duties on bottled water and soft drinks.

2. Spending

- **Free up funds for anti-inequality spending by:** reducing the debt service burden, if necessary through debt restructuring and relief; and cutting regressive electricity subsidies. Given the very tight fiscal constraints in Ghana, this and revenue mobilisation most be the top priorities.
- **Increase spending on cash transfer programmes targeting the poor,** by dramatically scaling up the LEAP cash transfer programme into a comprehensive national social protection floor.
- **Increase the pro-poor and progressive nature of education spending,** by spending even more on primary and junior secondary education, as more poor children progress to higher levels.
- **Improve the progressiveness of health spending, and halt the reduction in spending overall,** in order to make the NHIS universal and reduce regressive out-of-pocket payments.
- **Address geographical inequalities through better constructed financing formulae**, to overcome continuing urban-rural and North-South divides.

Country case study 2. Burkina Faso country profile

1. Inequality in Burkina Faso

Burkina Faso's economy has been growing in recent years. However, unlike many other countries, it was one of 45 developing countries where poor people benefited equally or more from growth than the better off during the period of 1990-2010. During that period in Burkina Faso, poverty rates fell from 71% to 45%, with the bottom 40% growing 1.6 percentage points faster than the average.[82] The government should be commended for any efforts in helping to accomplish this.

The Palma ratio averaged 1.9 from 2005-2013, demonstrating that the 10% richest households receive 1.9 times the total income of the poorest 40%. However, latest data from the World Bank for 2015, suggests this might be 1.84, suggesting a slight reduction in recent years. According to IDHR the Gini was 39.8 for 2005-2013 (latest data is 2009). Taken together, Burkina Faso has lower economic inequality compared to Ghana in both the Gini and Palma, but slightly higher than Sierra Leone.[83]

Burkina Faso's HDI value for 2014 is 0.402— putting it in the low human development category— at 183 out of 188 countries. Between 2005 and 2014, Burkina Faso's HDI value increased from 0.324 to 0.402, an increase of 24.2% or an average annual increase of about 2.43%. Between 1980 and 2014, Burkina Faso's life expectancy increased by 12.7 years, and expected years of schooling increased by 6.6 years. When the HDI is discounted for inequality, it falls to 0.261, a loss of 35%.

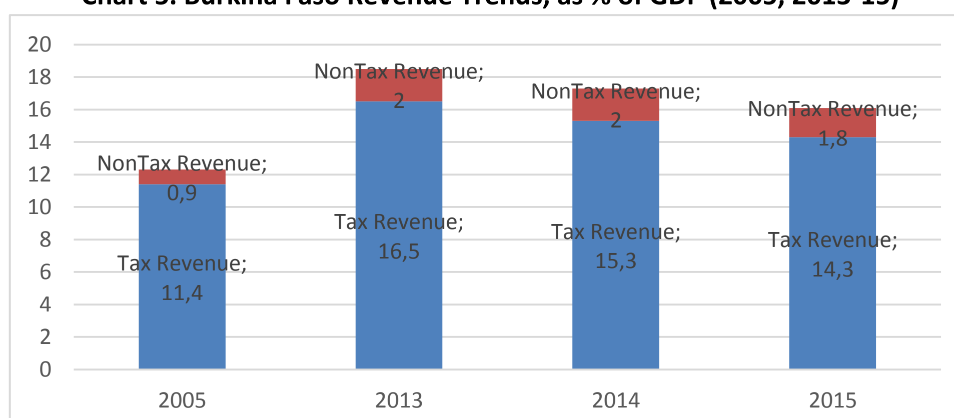
Education inequalities are stark in Burkina Faso by region: in the Sahel region 74% of children have never been to school. While in the centre this is only 11%, primary completion rate is only 7% in Sahel and 54% in the centre. While in 2015, Save the Children estimated that 60,000 children died before their fifth birthday from preventable causes.[84]

2. Tax policy in Burkina Faso – how well is it combatting inequality?

2.1. Is Burkina Faso collecting enough tax?

At first sight, as shown in Chart 5, Burkina Faso seems to be performing poorly on overall and tax revenue collection as of 2015, with ratios to GDP of only 16.1% and 14.3% respectively. In terms of tax collection, this means that it ranks 12th among ECOWAS members, with only Nigeria, Sierra Leone and Guinea-Bissau doing worse. However, longer-term analysis shows that Burkina Faso achieved steady increases between 2005 and 2013, reaching a peak of 18.5% for revenue/GDP, which would put it third from the top in ECOWAS. The political instability in 2014-15 has resulted in a fall in revenue collection, but the IMF expects revenue to rise back to pre-crisis levels by 2018.

Chart 5. Burkina Faso Revenue Trends, as % of GDP (2005, 2013-15)

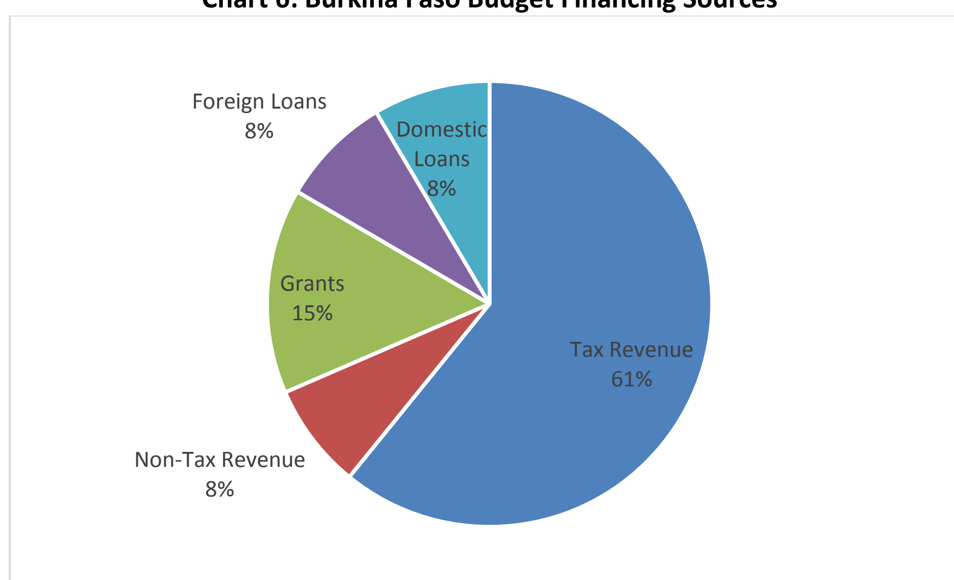


Source: IMF Country Documents

In addition, Burkina Faso has a very low per capita GDP compared even to most of its neighbours, a relatively small extractives sector, and very high dependence on agriculture. All of these factors reduce its tax collection potential considerably: as a result, Burkina Faso is doing relatively well in terms of its efforts to collect tax compared to its potential, which is assessed by the IMF at being 21.4%, as shown in Annex Chart 26 giving Burkina Faso a tax "effort" of 73%, which places it in the top third of countries globally and well ahead of Ghana and Sierra Leone.

Chart 6 shows the high share which revenue represents (69%) of total budget financing as of 2015. Of this, almost 90% is tax revenue. As almost all foreign borrowing by Burkina Faso is concessional, around a quarter of the budget is funded by aid (foreign loans + grants) - and this was in a year when political instability slowed aid disbursements even more than tax collection – typically in recent years, around 35% of the budget has been aid funded.

Chart 6: Burkina Faso Budget Financing Sources



Nevertheless, Burkina Faso is falling short of its tax potential. What are the reasons for this ?

1. **tax exemptions and deductions** play an important role. Burkina Faso has multiple different systems of tax exemptions – a recent survey found 642 different types of exemption by analysing only around 2/3 of its revenue. Government began analysing the scale of its tax exemptions only in 2013, and found that in that year they exceeded FCFA 144 billion,[85] around 44% of the taxes actually collected from the three taxes analysed (VAT, customs and stamp duties). Even this amount (which is 2.3% of GDP and 40% of the education budget or 75% of the health budget) represents a considerable underestimate of exemptions, as only taxes accounting for 2/3 of revenues were analysed, and only 204/642 exemptions were quantified. In reality, tax exemptions are probably around 5% of GDP, about the same as the education budget or twice the health budget. The government, having realised the large scale of exemptions, is trying to streamline them, for example extending VAT to the financial and telecom/ICT sectors in the 2016 budget.

2. A second reason has been a **failure to tax extractives sufficiently**. Government has been criticised for giving excessive exemptions for very profitable sectors such as mining (and cotton), a preferential

CIT rate of 17.5% to the mining sector, and failing to begin collecting extractives taxes (and end "exploration holidays" rapidly enough) when companies begin making large profits – all of which has meant that mining companies contribute only around 15% of government revenue (compared with 60% of exports). A new mining code introduced in 2016 has revised these arrangements but will have only a gradual effect as current exemptions expire – though the opening of a new manganese mine may help to increase revenues more rapidly.

3. A third reason is **tax dodging** – through evasion, avoidance and illicit flows by corporations and individuals. These are very hard to quantify, but GFI data have suggested that Burkina Faso is losing US$426 million a year (around 4% of GDP) due to illicit flows through trade mispricing alone.[86] It urgently needs to update its tax code to reinforce aspects such as treatment of "thin capitalisation" (where companies misdeclare profits as dividends or interest payments to avoid taxes).
4. A final reason is the influence of **tax treaties,** which set low rates for the taxes Burkina Faso can deduct up front from companies headquartered in other countries (withholding taxes) before they can start shifting profits out of Burkina Faso, and therefore reduce Burkina Faso's tax revenue. This is a less important issue in Burkina Faso, because the government has signed such treaties only with France, Tunisia and other WAEMU member states. Even so, the withholding taxes permitted by the treaties are lower for dividends among UEMOA states, and for interest payments and royalties for all three, with the Tunisia treaty having particularly low rates of 5-8% compared with the national rates of 12.5-25%, though the treaty with France gives priority to payment of taxes in Burkina Faso. As a result, Burkina Faso should be aiming to renegotiate especially the treaty with Tunisia.

2.2. Is Burkina Faso designing its tax system with an intent to be progressive?

To assess the "structural" or intended progressivity of Burkina Faso's tax system, it is necessary to look in turn at each of its major taxes:

- **Personal Income Tax:** Burkina Faso's top rates of PIT are well below African and LMIC averages at only 25%; though its lowest rate of 12% is relatively average. However, this divergence means that it has a very narrow range of income tax rates (only 13% compared to typical 20-25% ranges). Its minimum threshold for paying personal income tax is around the same level as per capita GDP, which means that most poor taxpayers are excluded: however, its top tax threshold is 8 times as high, a wider range than in most countries, implying that some high earners may not be paying their fair share.
- **Value Added Tax**: Burkina Faso has a VAT rate of 18% (in line with other members of WAEMU), which is among the highest rates in developing countries, well above LIC, Africa and global averages. It has no minimum VAT threshold, meaning that smaller traders and their (poorer) customers have been paying VAT, making it much more regressive. On the other hand, it has a considerable range of exemptions, some of which are for pro-poor products such as basic foodstuffs, and medical products, but others of which are for sectors or less "pro-poor" goods such as telecoms/ICT and finance, and which are in the process of being rationalised.
- **Corporate Income Tax**: Burkina Faso has reduced its CIT rate from 30% to 27.5%, participating to a limited degree in the regional "race to the bottom" of recent years, and encouraged by higher resulting scores in the World Bank's Doing Business Index. This puts its rate at an average level for West Africa where rates range from 15% to 35%. Recently, other countries such as Cote d'Ivoire have justified greater CIT cuts on similar grounds – even though the WAEMU has tried to combat this by setting a minimum CIT rate of 30% (Action Aid 2014).
- **Other Progressive Taxes:** Burkina Faso has long had the same capital gains tax and corporate income tax rates. However, until recently only half of any capital gains were taxed, and many categories such as mergers and asset transfers were not taxed (the Government is in the process of updating its CGT legislation). Burkina Faso taxes income from land at 18% for small amounts and 25% for larger,

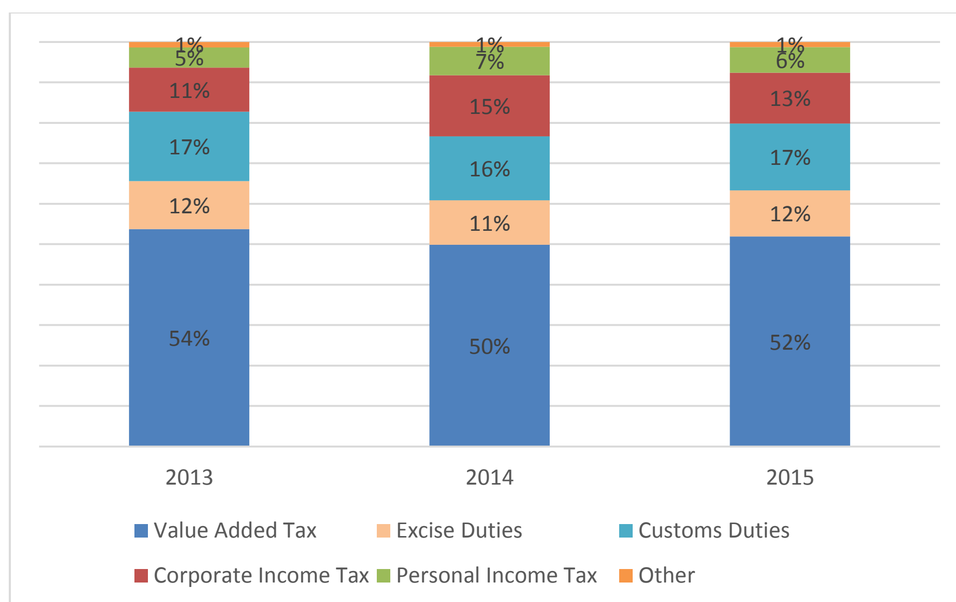
broadly comparable with CIT/PIT rates; it also has duties on property sales and rental income ranging from 3% to 7%: these property taxes are considerably higher than those in Ghana. Its inheritance and gift taxes are similar to those in most WAEMU countries, with rates which vary with the closeness of relationship: a top rate comparable to PIT and lower rates down to zero for very close relatives.

- **Other Regressive Taxes:** Burkina Faso, like many Francophone countries, has very high social security contribution rates (16.5% for the employer and 5.5% for the employee), giving a total of 22%, somewhat above global and LIC averages, and well above the African average. Its excise duty rates have historically been relatively low, but have been raised in the 2016 budget. Customs duties are set in line with the common external tariff of the WAEMU zone, varying between 0% and 20% and therefore not very progressive.

2.3. Is Burkina Faso collecting progressive or regressive taxes ?

As shown in chart 7, Burkina Faso collects 80% of its taxes from indirect taxes (VAT, excise duties and customs duties), which have been found globally to be regressive, and more than 50% from VAT (data are not available on collections for social security, which can be even more regressive than VAT).

Chart 7. Breakdown of Burkina Faso's total tax collection by type of tax



Based on incidence coefficients derived from Martinez-Vazquez et al, Burkina Faso's tax system is almost certainly significantly regressive, increasing the Gini by around 0.04. There is no country-specific incidence analysis for Burkina Faso, though it may benefit from such a study in future years due to the partnership between the World Bank and the CEQ initiative. This result would place it among the more regressive tax systems worldwide, ranking 125th on the DFI tax progressivity database, and well below Ghana or Sierra Leone.

What explains these results?

The relatively small progressive effect of direct taxes reflects their relative lack of progressivity (compared to other countries) and large problems with collection (the productivity of PIT in Burkina Faso – the extra amount collected for each $ of GDP – is extremely low at only 4 cents; and that of CIT is only 7 cents) due to exemptions, deductions and dodging. VAT is likely to be substantially regressive due to a relative lack of pro-poor exemptions, and is also very productive at 83 cents per $

of consumption due to a relative lack of other exemptions, meaning that it has a major impact on making the overall system more regressive.

3. Government spending in Burkina Faso: is it combatting inequality?

3.1. How much is Burkina Faso spending on key inequality busting social sectors?

When non-contributory social protection spending only is taken account of, as an overall proportion of the budget social sector spending is allocated around one-third of the budget (at 28%). This has slightly improved in recent years with increase allocations of 2-3% of budget to social spending.

Overall, across the three social sectors, including both contributory and non-contributory social protection, Burkina Faso spends around the mid-way mark of the sample of 41 sub-Saharan countries – ranking 24th from the bottom. When compared to other Low-Income Countries (LICs) on sector specific spending, Burkina Faso tends to fare relatively well: they come second to top in health spending, in the top ten for social protection, but is rather let down by a lower than average spending level on education. See charts 14 to 17 in annex 2.

In particular, by the standards of LICs they have a fairly large social protection spending, when contributory schemes are taken account of, with spending standing at 8% of budget, or 1.8% of GDP.[87] However, it should be noted that Burkina Faso's overall spending levels are pulled down when non-contributory social protection spending is taken into account, when this reaches low levels of below 1% of budgets and 0.3% of GDP. This suggests that Burkina Faso is spending a larger amount on contributory schemes than other countries of a similar income level. However, given this tends to have a more regressive impact in a country with such large poverty/inequality, while higher levels of social protection supported by tax-financed non-contributory social protection tends to be the most redistributive, this suggests that social protection spending in Burkina Faso is less progressive than could be. In other words, social protection spending could almost certainly work harder to address poverty and inequality in Burkina Faso.

In education, overall spending has increased in recent years, from 14% to 17% of the budget during 2013-15, and from 3.8% to 4.9% of GDP, and the government should be commended for this – especially as this now has ensured they are meeting the Incheon Declaration for Education 2030 commitment. While it is clear that Burkina Faso is moving in the right direction in terms of increasing spending on education, and the country is currently meeting (the lower end) of the Incheon benchmarks for spending on education, it should also be noted that Burkina Faso has a tendency for fairly large changes to be observed year-on-year. For instance, in 2009, Burkina Faso was spending 16.67%; in 2010 15.9%; 17.21% in 2011; and, 14.9% in 2012. This does add a cautionary tale to assuming any increases are part of a longer term trajectory. Burkina Faso must make a much longer term commitment to increasing spending for education as part of a longer term plan to improve their quality and outcomes.

On health spending this is fairly steady at around 10-11% over the last few years. However, this is still from the Abuja commitments, and, moreover, spending is just $18 per capita in 2015, well below the recommended Chatham house US$86 per capita to provide essential health services for all.

While health spending is the highest among the 3 countries in this study – and relatively high overall compared to other similar regional or income country groups, it is assumed that increases are required to meet the new commitment to provide free healthcare to children and pregnant mothers. In April 2016 the government brought in a new law means healthcare is now free for children under five, for pregnant women, for deliveries and caesareans, and for breast and uterine cancer screening. Building on a pilot in three districts and at the first two levels of the health system, the government plans to roll this out nationally. When tested through the above pilot scheme in the

Sahel health region in the North-East, this was seen to have an immediate, substantial effect of increasing access to care and reducing expenses and the benefits of the exemption were not monopolised by the better-off families.[88] Seeing this roll out nationally with similar results – especially this not being monopolised by better off families as the pilot showed - could have a very large impact on inequality and poverty. If implemented fully, this policy could save the lives of 30,000 children each year.[89]

This almost certainly means this is likely to have a strongly progressive impact on health spending. But this needs to also be part of a stronger push to move away over the longer term to relying on regressive, out-of-pocket payments, increasing funding to deliver on the (larger) law in Burkina Faso of Universal Health Coverage for all. The removal of user fees for women and children is a just the first step for Burkina Faso, which has also passed a law on Universal Health Coverage to guarantees access to essential health services for all. This is a large scale up when it is considered that only 37% of the population are currently covered with nearly 90% of this being paid for by out-of-pocket spending. Such distortions tend to hit women disproportionally, and 92.5% of women reported paying health user fees.[90]

Delivering on this commitment will entail large increases in health spending, as well ensuring it is spent equitably and efficiently. Certainly, recent moves suggest this could have a large impact on inequality if well implemented – and advocating for increased financing is required to support the government on this.

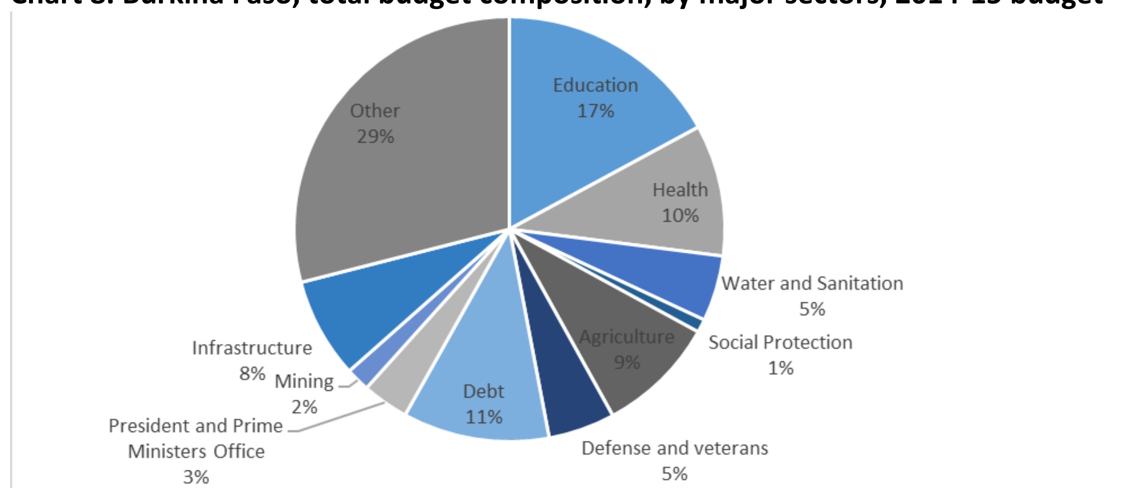
What else is the budget spent on?

Given debt is relatively low at 11% and defence at 5%, less is being swallowed up by such spending than, say, Ghana. What is the overall budget being spent on? A relatively large amount is being spent on agriculture in 2015 (8.9%), and WASH (5%). However, there are large parts of the budgets which are divided between multiple ministries serving small areas which have been classified as "other" in the budget breakdown below (these are multiple other small ministries covering areas such as judiciary, tourism etc) and which account for a large amount of overall budget. Given this diverse spending, and classification, it is sometimes difficult to assess the true poverty and inequality impact of some of this spending. Given the importance of Burkina Faso addressing pro-poor spending, such a cross budget analysis may help to better define future programmes.

Table 2. Burkina Faso overall breakdown of budget, 2015

Sector/programme	Percentage of budget spent on area
Education	17%
Health	10%
Water and Sanitation	5%
Social Protection	1%
Agriculture	9%
Defence and veterans	5%
Debt	11%
President and Prime Ministers Office	3.5%
Mining	1.8%
Infrastructure	7.6%
Other	29%

Chart 8. Burkina Faso, total budget composition, by major sectors, 2014-15 budget



3.2 What do we know about sector spending, and its inequality effect in Burkina Faso?

By applying the benefit incidence coefficients derived from Martinez-Vazquez et al, to Burkina Faso's social spending, it is possible to conclude that overall this is likely to be progressive. In other words, it helps to reduce inequality, bringing down the Gini coefficient by 0.03. Of a sample of 16 West Africa countries, Burkina Faso was found to have the third most likely progressive spending patterns. Of the 3 countries in this study Burkina Faso is likely to have the largest inequality impact; this reflects above all the higher proportions of health spending, because its impact on inequality is likely to be greater. Such spending can help to explain why Burkina Faso keeping their inequality relatively low.

One area of spending which has been noted as being not being as progressive as possible – and possibly marginally regressive – in Burkina Faso is spending on education. This analysis seems slightly counter-intuitive when compared to the overall mix of spending on education, and the fact that Burkina Faso GSW analysis shows they spend close to 65% of their total resources on education on primary schooling – this is significantly higher than the other countries in this study (see table below). This is also higher than an average for a sample of 27 LICs.[91]

Table 3. Breakdown of spending by different levels in the 3 country studies

	Ghana (UIS data 2013)	Burkina Faso (2014 UIS data)	Sierra Leone, (UIS data 2014)
Pre-primary allocation of total education budget	6.6%	0.03%	No data
Primary schooling allocation of total education budget	25%	65%	43%
Secondary schooling allocation of total education budget	48%	17%	23%
Tertiary education allocation of total education budget	20%	13%	31%

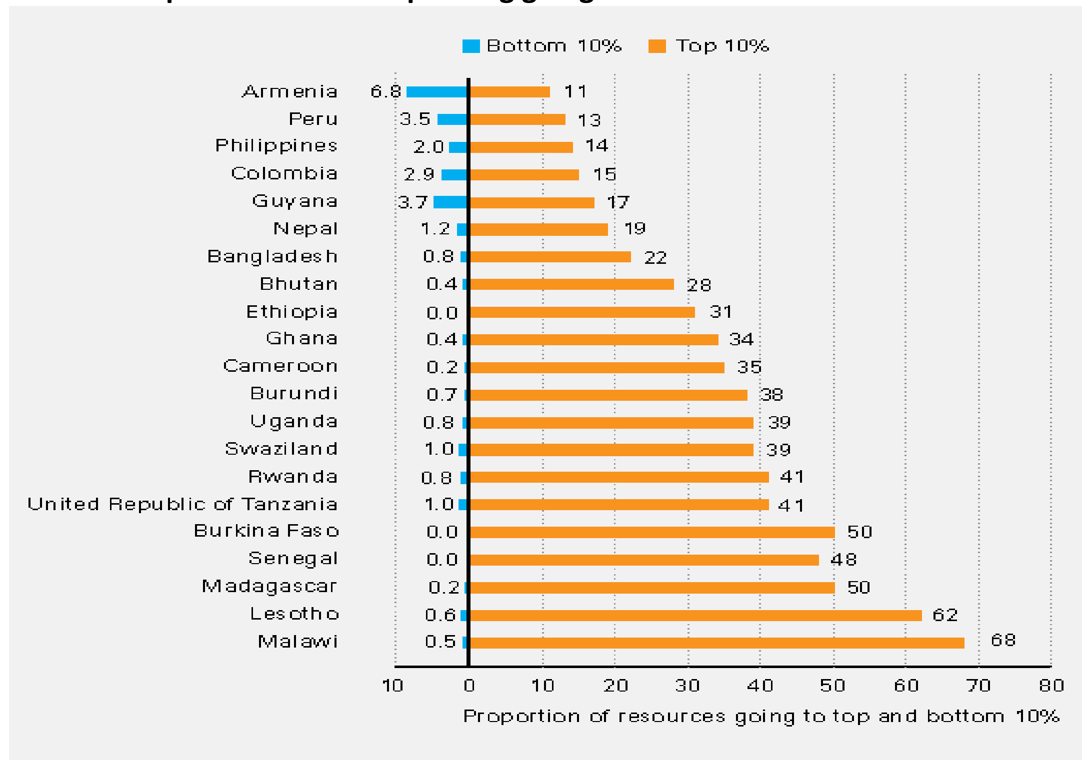
**note some budget are allocated to areas such as administration or adult education not captured above as a category and thus the above does not make up 100% of spending.*

However, this is explained by the fact that Burkina Faso has very low completion and retention rates. For instance, Chart 9 shows the percentage of public funds used for the education of the most educated 10% and the least educated 10% of students in 18 countries. At the top of the figure is a group of countries where education resources are distributed relatively equally across children. Burkina Faso, sits towards end, where the top 10% consume 50% of public expenditure for the budget and the bottom 10% less than 1%. This is a highly regressive spending pattern. While Pôle de Dakar has used information from household surveys to analyse the ratio of expenditures for children from the wealthiest 20% of households compared with children from the poorest 20% households. In Burkina Faso, the wealthiest use 8 times more public education resources than the poorest.[92]

In many respects, this is not a fault of the government which, through large allocations to primary education, is committed to scaling up universal completion. But there are two areas which the government could focus on to better tailor their spending to be more progressive. Firstly, spending on pre-primary is very important to addressing inequality, and is low in Burkina Faso (less than 0.05%).

Secondly, in a country where vast geographical inequalities in education exist, and very few of the poorest make it through education, certainly in rural and marginalised regions - it is understandable that the poorest are consuming very little budget, and increase should be channelled to supporting poorer areas. For instance, 73% of the Sahel region have never been to school versus 11% of the centre, and 65% of the poorest have never been to school versus only 13% of the wealthiest.[93] This also plays out in great geographical inequalities in terms of teachers and very large urban and rural differences, in terms of teacher ratios which tends to equate to different school sizes and number of teachers employed. In Burkina Faso in schools with just one teacher, the pupil-teacher ratio ranges from a few to nearly 150. In schools with three teachers, the pupil teacher ratio ranges from a few to approximately 100.[94]

Chart 9. % of public education spending going to 10% most or least educated students



Source. Taken from UNICEF, 2015, The Investment Case for Education and Equity. http://www.unicef.org/publications/files/Investment_Case_for_Education_and_Equity_FINAL.pdf

Burkina Faso has already done work on addressing this in the areas of health. After data revealed huge geographic inequities in health spending the government and development agencies allocated more resources to poorer regions.[95] Previously, poorer regions received less than more affluent areas. Boucle du Mouhoun and Nord – two of the poorest regions in Burkina Faso – received a combined 11% total of all health care spending; this is in spite of poverty incidences being 60% and 69%, respectively, in each these regions, while the wealthier Centre region which received 29% of total health care spending in spite of having 22% incidence of poverty. Similar approaches and analysis are needed to channel support to help the poorest and most marginalised in deprived regions and rural areas to attend school. International evidence shows that this often requires additional resources channelled to each pupil in those regions, and extra support with programmes such as school meals and conditional transfers for school attendance.[96] Burkina Faso has made some good inroads into beginning to bring in school meals but more can be done to expand this and make this sustainable in the budget (as opposed to supported largely by donors).[97]

4. Conclusions and Recommendations

Given lower levels of inequality than Ghana, and reductions in this in recent years Burkina Faso needs to work hard at continuing on this. However, with such large poverty, especially by region and rurality – it is important for all spending to be both pro-poor and inequality reducing.

Overall, according to the DFI/OI tax structural progressivity index, Burkina Faso comes in the bottom third of countries, due to a combination of high VAT and relatively low personal and corporate income tax rates. This places it above Ghana but below Sierra Leone, and 11th in West Africa. To make its tax structure more progressive, and able to play a better role in redistribution to reduce poverty and inequality, it could increase its Personal Income Taxes (PIT) and Corporate Income rates slightly, reduce its top PIT threshold, introduce a minimum threshold for VAT, and reduce social security contributions.

Overall, according to the DFI/OI tax incidence indicator, Burkina Faso is very low, 125th of 155, with a tax system which is *substantially* regressive. This reflects its very high dependence on collection of VAT and other indirect taxes on consumption and trade, set against its poor record of collecting direct corporate and personal taxes which are more progressive. These findings emphasise the strong need for it to increase the progressivity of the tax structure, and the collection of progressive taxes, in order to make the tax system much more progressive.

For Burkina Faso to increase the role tax can play in tackling inequality and redistribution within the economy it must work much harder at placing less burden on the poor, and ensuring the rich, especially corporations, pay more.

Burkina Faso's social spending is likely to be progressive, helping to reduce inequality. It is also important for Burkina Faso to focus on how pro poor their social spending is and make sure this is focused more on those at the bottom. Spending must address the wide disparities in terms of access to services and outcomes for users. This is most apparent in education where, in spite of good allocations to spending on primary schooling very low retention rates in many regions means the poorest still get a very small slither of the education financing pie. Allocations to education need to give greater emphasis to spending more per pupil in areas with low participation or retention on primary, as well as focus on supporting pre-primary and areas such as social protection focused on helping children go and stay in school.

The recent commitment to provide free health services to women and children is a very welcome breakthrough in a country with over 92.5% of women reported paying health user fees. This has to

be met with increased financing though to be successful and scaling up health spending should be a major priority for the government.

Finally, as with all counties in this study, low levels of spending on non-contributory, tax-supported social protection needs addressing.

The Burkina Faso government should focus on the following recommendations:

1. Tax

- **Enhance tax effort** by: reducing exemptions and deductions; fighting tax dodging more effectively on corporate and personal income tax; and renegotiating tax treaties to allow higher withholding taxes, capital gains taxes and taxes on dividends.
- **Make the design of its tax system more progressive** by: increasing taxes on capital gains, inheritance and gifts to match income tax rates; increasing corporate and especially top personal income tax rates to match regional levels, while reducing its maximum PIT thresholds to ensure that wealthy citizens pay their fair share; and introducing a minimum threshold for VAT to exempt small traders and their customers from VAT payment.
- **Make its tax collection more progressive** by: sharply increasing the proportion of taxes coming from personal and corporate income tax (by reducing exemptions, deductions and dodging), and capital gains/property/wealth taxes, introducing a minimum VAT threshold; and carrying out a detailed tax incidence study to measure the actual impact of taxes on inequality.

2. Spending

- **Make education spending more progressive,** by carrying out a detailed incidence analysis of education to identify how to make it more progressive, including by region and rurality; reorienting spending to be more progressive according to its findings;, and providing complementary support including school meals and cash transfers.
- **Boost health spending to deliver on the new policy of dropping user fees for children and women,** working towards universalizing free health care over the medium term.
- **Scale-up non-contributory spending on social protection,** with the long-term aim of achieving a universal social protection floor.
- **Address geographical inequalities through better constructed financing formulae**, to address continuing urban-rural and North-South divides.

***

Country Case study 3. Sierra Leone country profile

1. Inequality in Sierra Leone

Since the end of the internal conflict in 2002, Sierra Leone has made remarkable progress in consolidating political stability and rebuilding its economy. Its GDP growth rate increased significantly - ranging between 6% and 20% - higher than most other fragile countries like Sierra Leone.

However, that success, mainly driven by the mining industry, remains vulnerable and poorly distributed due to weak human and institutional capacity, inadequate mechanisms of economic governance and the persistence of social inequalities.[98] Moreover, progress has been seriously compromised by the Ebola outbreak that shook the country from May 2014 to February 2016.

Sierra Leone does quite well in terms of inequality. From a sample of 41 sub-Saharan African countries, Sierra Leone had 8th most equal Palma score and the 7th most equal Gini. It is also the most equal country in this study.[99] The Palma ratio, measured over the period 2005-2013 indicates that the richest 10% earn 1.5 times the income of the poorest 40% of the population, and the Gini is 34% (in 2011). Thus, economic inequality seems to be less prevalent (as is often the case in fragile countries because there is less scope for extreme wealth). However, Sierra Leone does have very large poverty levels, and other forms of inequality, especially in terms of access to and outcomes of services, is very prevalent. As the Human Development Index (HDI) shows sierra Leone has improved their score, from 0.252 in 2000 to 0.413 - 181st out of 188 countries - in 2015. Despite this 38% rise, it is still below average HDI in Sub-Saharan Africa (0.518). The Inequality-adjusted HDI (IHDI) is 0.241, representing a loss of 41.7% caused by social inequalities. Inequality is more pronounced in life expectancy (51.2 % in 2010-15) and education (49.6 % in 2014).

The relatively high level of different forms of inequality in terms of human development in Sierra Leone is associated with the prevailing post-conflict situation. Sierra Leone is still recovering from a bloodshed of decade in civil war that resulted in the death of over 50,000 people and the displacement of two million – and access to infrastructure and services continues to be a problem. While the relatively low levels of *economic* inequality are a result of very high poverty levels, and low GDP, giving very little space for inequality to grow, and only a small elite currently capturing more of the economic pie, while most citizens remain trapped in poverty.

2. Tax policy in Sierra Leone – how well is it doing in combatting inequality?

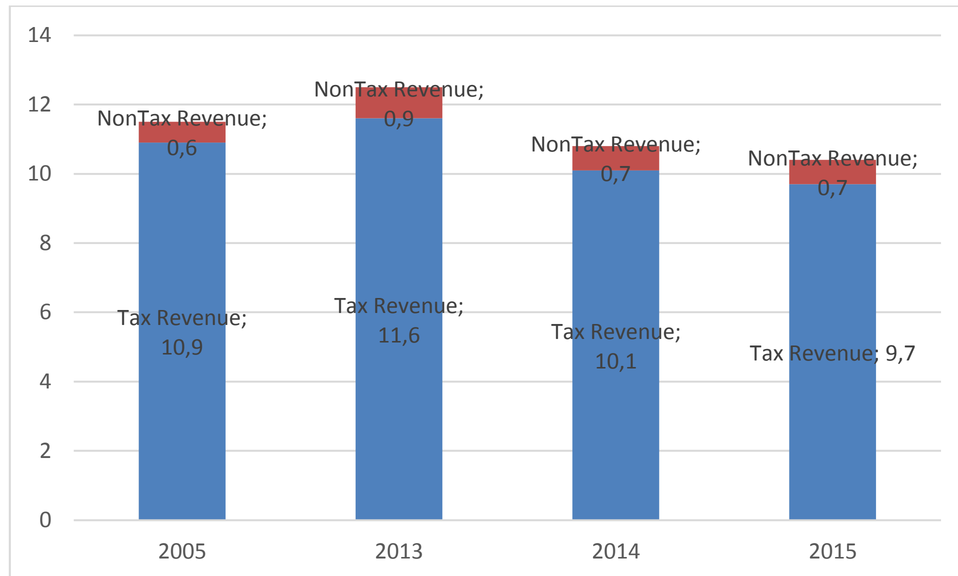
2.1. Is Sierra Leone collecting enough tax ?

As shown in Chart 10, Sierra Leone performs very poorly in terms of revenue collection, with total revenue at only 10.4% of GDP and tax revenue at only 9.7%. This makes it the second worst ECOWAS member on both measures, with only Nigeria performing less well, which has one of the lowest revenue and tax collections in the world (as shown in Annex Chart 26).[100]

During 2000-2011 Sierra Leone's tax collection has varied dramatically, as chart 11 shows. Two major tax reforms managed to increase the ratio by 3% (due to improved administrative performance with the creation of a National Revenue Authority, and renewed economic growth) in 2000-2005 and 4% (including the introduction of a General Sales Tax similar to a VAT) in 2007-11. In 2012-13 GDP grew dramatically due to iron ore production, but without producing much extra tax revenue – so GDP

growth outstripped the potential collection of taxes from that growth, especially from mineral extraction. In 2013-14 renegotiation of revenue agreements with the iron ore company again increased revenue, but in 2014-15 Sierra Leone was hit by Ebola which reduced non-mining revenue, and in 2015 iron ore prices and revenue have collapsed, leaving it 1% below 2005 levels.

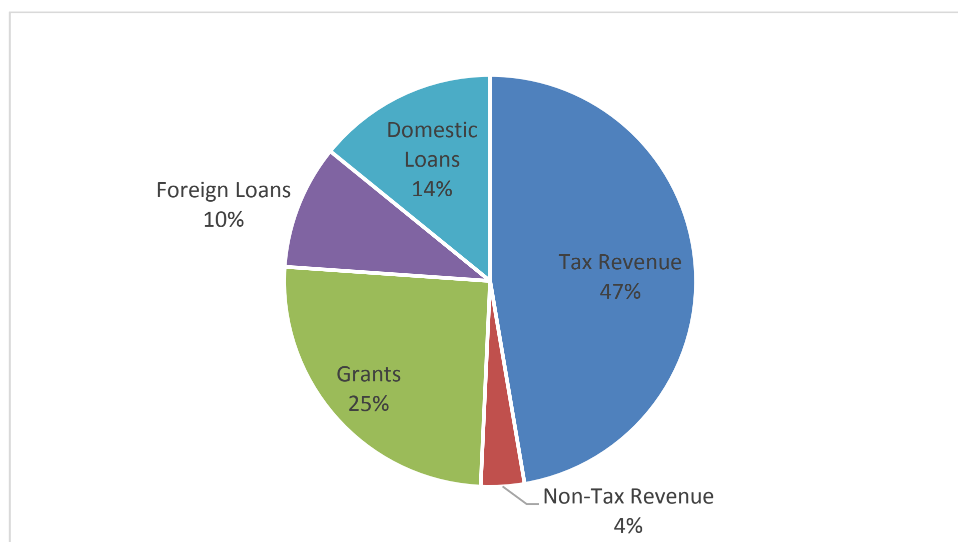
Chart 10. Sierra Leone revenue trends as % of GDP (2005, 2013-15)



Source: IMF WEO database April 2016

Chart 11 shows the overall financing sources for Sierra Leone's budget. Due to its low levels of tax collection, revenue represents a relatively low share (only 51%) of total budget financing as of 2015. Of this, 95% is tax revenue. As almost all foreign borrowing by Sierra Leone is concessional (keeping its debt burden low), over one third of the budget is funded by aid (foreign loans + grants), partly due to the increase in aid flows to fight Ebola. Nevertheless, it represents a fall compared to the postwar period when grants were 9-10% of GDP, almost as high as budget revenue.

Chart 11. Sierra Leone Budget Financing Sources, 2015



Source: IMF Country Documents 2016

Sierra Leone has a very low per capita GDP compared even to most of its neighbours, but a relatively large extractives sector, which makes its "tax collection potential" higher according to the IMF, at 18.2% of GDP. In other words, Sierra Leone is collecting only half of its potential amount of tax revenues. This means Sierra Leone is not collecting enough tax to play a fully re-distributive and equalising role. As a result, it is performing very poorly in terms of tax "effort" compared to this potential, at only 50%: this places it third last among ECOWAS countries and 104th globally.

The reasons why Sierra Leone falls short of its tax potential are similar to Ghana and Burkina Faso:

1. massive **tax exemptions and deductions** have historically been the main problem in Sierra Leone's tax system. In addition to a list of multiple rates and special regimes for foreign investors, sectors, and other reasons, Sierra Leone granted special ad hoc deals to major investors in the mining, agribusiness and tourism sectors. The Sierra Leone government has not yet published any report on tax exemptions, but an analysis conducted by civil society organizations the Tax Justice Network-Africa and the Budget Advocacy Network in 2014 showed that exemptions on the General Sales Tax (GST), customs duties and Corporate Income Tax alone, cost an average of 11.5% of GDP in 2011-12. This is around 20% more than the tax actually collected, and 8 times the health and 7 times the education budget[101] These revelations resulted in some renegotiation in 2014-15 of ad hoc deals with mining companies (which avoided further losses of 2% of GDP), and more scrutiny of new contracts by parliament, but much more remains to do.
2. **failure to tax extractives sufficiently**. For many years the government was criticised for insufficient taxation of the extractives sector, notably diamonds. In 2014 it introduced a new mining code and renegotiated the tax agreement with the iron ore company, producing a major increase in tax revenues.
3. **tax dodging** – through evasion, avoidance and illicit flows by corporations and individuals. These are very hard to quantify, but Global Financial Integrity data have suggested that Sierra Leone has been especially vulnerable to illicit financial flows (IFFs) through trade mispricing, losing US$558 million a year on average, more than 10% of its GDP.[102]
4. **tax treaties**, which set low rates for the taxes Sierra Leone can deduct up front from companies headquartered in other countries (withholding taxes) before they can start shifting profits out of Sierra Leone, and therefore reduce Sierra Leone's tax revenue. Sierra Leone has relatively few tax treaties – with only Norway, South Africa and the UK. Nevertheless, these treaties do contain lower withholding tax rates (especially on royalties and natural resource payments) than in the tax code, reducing tax collection by Sierra Leone. It should be a priority for the country to renegotiate such treaties.

2.2. Is Sierra Leone designing its tax system with an intent to be progressive?

To assess the "structural" or intended progressivity of Sierra Leone's tax system, it is necessary to look in turn at each of its major taxes:

- **Personal Income Tax:** Sierra Leone has a PIT top rate which matches African and LIC averages at 30%; but a lowest rate which is relatively high at 15%. This divergence means that it has a relatively narrow range of income tax rates (only 15% compared to typical 20-25% ranges). Its minimum threshold for paying personal income tax is around the same level as per capita GDP, which means that most poor taxpayers are excluded: and its top tax threshold is only 3 times as high, a slightly lower difference than in most countries. implying that high earners are intended to be paying their fair share.
- **Value Added Tax**: Sierra Leone has a General Sales Tax (GST) instead of a VAT, set at a rate of 15% (slightly below WAEMU but above other ECOWAS members and broadly in line with LIC and SSA averages). However, it has a very high minimum turnover threshold for paying GST, at more than 100 times per capita GDP, meaning that many relatively large traders may not be paying GST and making it slightly more regressive. It also continues to have a wide range of

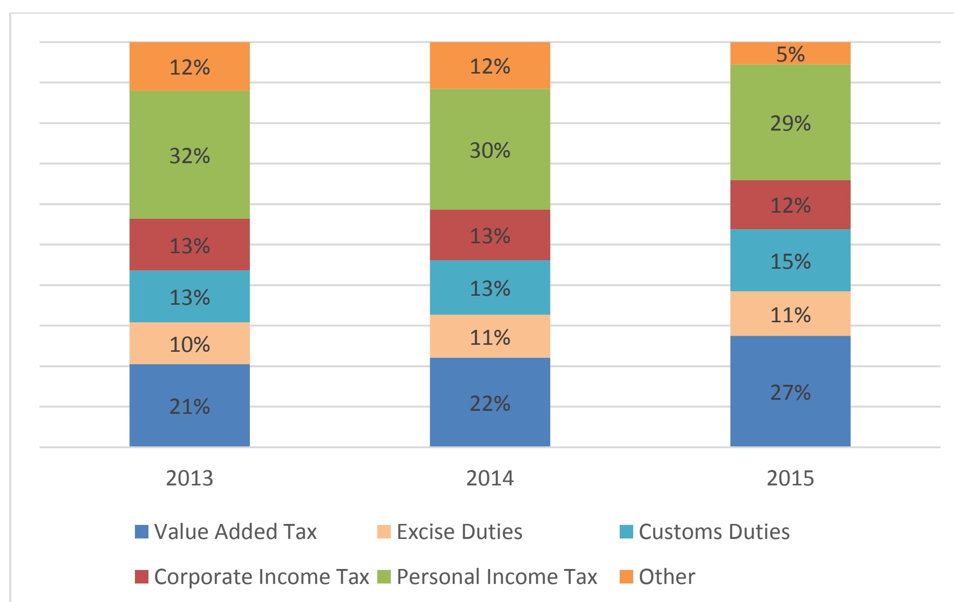
exemptions on GST: while a few of these (on education, health and public transport) might be relatively neutral or even progressive, many others (for sectors such as agriculture, financial services and mining) are highly regressive and should be eliminated – and bizarrely basic foodstuffs are not exempt. There is need for a fundamental reform of the GST system and its replacement by a VAT which covers all sectors with more rational thresholds and exemptions for a few basic goods.

- **Corporate Income Tax**: Sierra Leone has kept its CIT rate at 30%, although some neighbouring countries have been cutting theirs, and has therefore avoided the race to the bottom. This puts its rate at an above average level for West Africa where rates range from 15% to 35% - but one which is in line with WAEMU efforts to combat harmful tax competition by setting a minimum CIT rate of 30% across the region.
- **Other Progressive Taxes:** Sierra Leone has no separate capital gains tax – and applies corporate income tax only to complete disposal of businesses or assets, leaving major scope for avoidance. Its other taxes on income from wealth (rent, dividends, interest) are well below the CIT rate, ranging between 0% and 15% for residents, and 10% and 25% for non-residents. It does have small stamp duties on property transfers. Information on inheritance and gift taxes was not obtainable for this draft.
- **Other Regressive Taxes:** Sierra Leone has a social security rate of 15% (10% employer and 5% employee), significantly below global, LIC and African averages. Its customs system remains relatively progressive, with rates between 3% (on basic goods) and 40% (on luxuries), but this will soon be ended by the ECOWAS common external tariff. Information on excise duty rates was not available for this draft.

2.3. Is Sierra Leone collecting progressive or regressive taxes ?

As shown in chart 12, Sierra Leone collects only 53% of its taxes from indirect taxes (VAT, excise duties and customs duties), which have been found globally to be regressive - 30% of which is from VAT. It also collects virtually no revenue from social security contributions, which can be even more regressive than VAT. Collection of direct tax has increased considerably since 2005, reaching 40% of the total, due largely to increased taxation of extractives. and improved collection of PIT.

Chart 12. Breakdown of Sierra Leone's total tax collection by type of tax



Based on incidence coefficients derived from Martinez-Vazquez et al, Sierra Leone's tax system is almost certainly slightly regressive, increasing the Gini by 0.01 (results similar to Ghana). There is no

country-specific incidence analysis for Sierra Leone, though it may benefit from such a study in future years due to the partnership between the World Bank and the CEQ initiative. This result would place it at an average level globally, ranking 71st worldwide and above Burkina Faso but similar to Ghana.

What explains these results? Though direct taxes are relatively progressive in their structure (compared to other countries) there are large problems with collection, The amount of personal income tax collected for each extra dollar of GDP - is very low at only 10 cents – and the amount of corporate income tax is even lower at only 4 cents. These low levels reflect exemptions, deductions and dodging. VAT is likely to be substantially regressive due to a relative lack of pro-poor exemptions, but is also relatively unproductive at only around 30 cents per $ of consumption due to major non-progressive exemptions, and a very high minimum threshold, so it has less impact on making the overall system regressive.

3. Government spending in Sierra Leone: is it combatting inequality?

3.1. How much is Sierra Leone spending on key inequality busting social sectors?

Overall, across the social sectors, including both contributory and non-contributory social protection, Sierra Leone was spending 32% of budget on these three sectors (as charts 16 and 17 in annex 2 show).

When non-contributory social protection spending only is taken account of, as an overall proportion of the budget, social sector spending is allocated at 30.5% in 2015. This has slightly improved in recent years with increased allocations from 28% in 2013.

Spending has increased considerably in Sierra Leone over the last few years on education, only to fall away in the planned in the 2016-17 budget. It moved from 15% of government budgets in 2011 to 20% in 2015, and 2.6% to 4% of GDP, respectively. However, in 2016 it declined to around 18% (17.8%). This means that Sierra Leone is now spending within the levels recommended by the Incheon Declaration, but has some rather large movements over time. It should be noted that in 2015, when spending was 20%, Sierra Leone was spending the fourth highest amount of budget allocation on education among LICs (see chart 14 in annex), which is commendable. However, spending per capita is very low still at US$14.5 in 2015, rising from US$9.63 in 2011.

Meanwhile health spending has gone from 6.5% to 11% of total government budget between 2011 and 2016 – also a good rise but below the levels required for Abuja commitment. While per capita US$22 in 2016 – very far below the required US86$ Chatham house recommendations but up considerably from the previous year when this stood at US$15 per capita. At least some of this increase is explained by new funds being allocated from donors being channelled through government systems (i.e. “on budget aid) as a result of the fall-out from the Ebola crisis. In fact, donor support to the government’s own health sector plans doubled from nearly 2% to 4% of the total budget from the 2014-15 to 2016-17 budget cycles. It is vital that the Ebola crisis doesn’t just lead to a short term boost in strengthening the fragile health system in Sierra Leone, supported by donors, but that sustainable solutions are found to boost the whole system towards better financing and coverage that can help can help the realisation of Universal Health Coverage.

Moreover, given the reductions in 2016-17 planned spending were observed in education at the same time as health was boosted, it is very important that any increases in one sector (health) are not coming at the price of another (education). “Robbing Peter to pay Paul” is not a long term solution: that must come from sustainable increases to scaling up quality fee-free services for all

across both health and education, supported mainly by tax revenues (which are too low), in the long term, and donors bridging any short term gaps.

Finally, social protection spending also remains *very low*, when both contributory and non-contributory spending is taken account of Sierra Leone has the 11th from the bottom in spending across a sample of 41 countries- with spending at only 3% of total budget and less than 1% of GDP. When non-contributory spending is taken account of this drops even further to below 1%. Presumably, there are large "off budget" social protection schemes administered by CSOs/NGOs. However, increases in spending on social protection, aimed at ensuring these are designed with inequality and inclusive growth in mind, should be a priority in a country with such low development indicators and such widespread poverty.

Table 4 and Chart 13 break down the latest available budget year in more detail. This shows, that while debt levels remain relatively low at present this has risen from 8% to 11% in the last few years. So certainly debt is on the increase, but is firmly within the boundaries of acceptable spending levels. Most surprising, is the large spending tag attached to road and infrastructure related projects at around one quarter. This is part of a growing trend in countries like Sierra Leone to spend money (and usually borrow to fund such spending) on infrastructure which is intended to promote growth, without analyzing its potential impact on poverty or inequality. Overall it is vital that Sierra Leone ensures a robust analysis of the poverty and inequality impact of their spending, and reconfigures accordingly.

Chart 13. 2015 budgets for priority sectors in the "Agenda for Prosperity" development plan

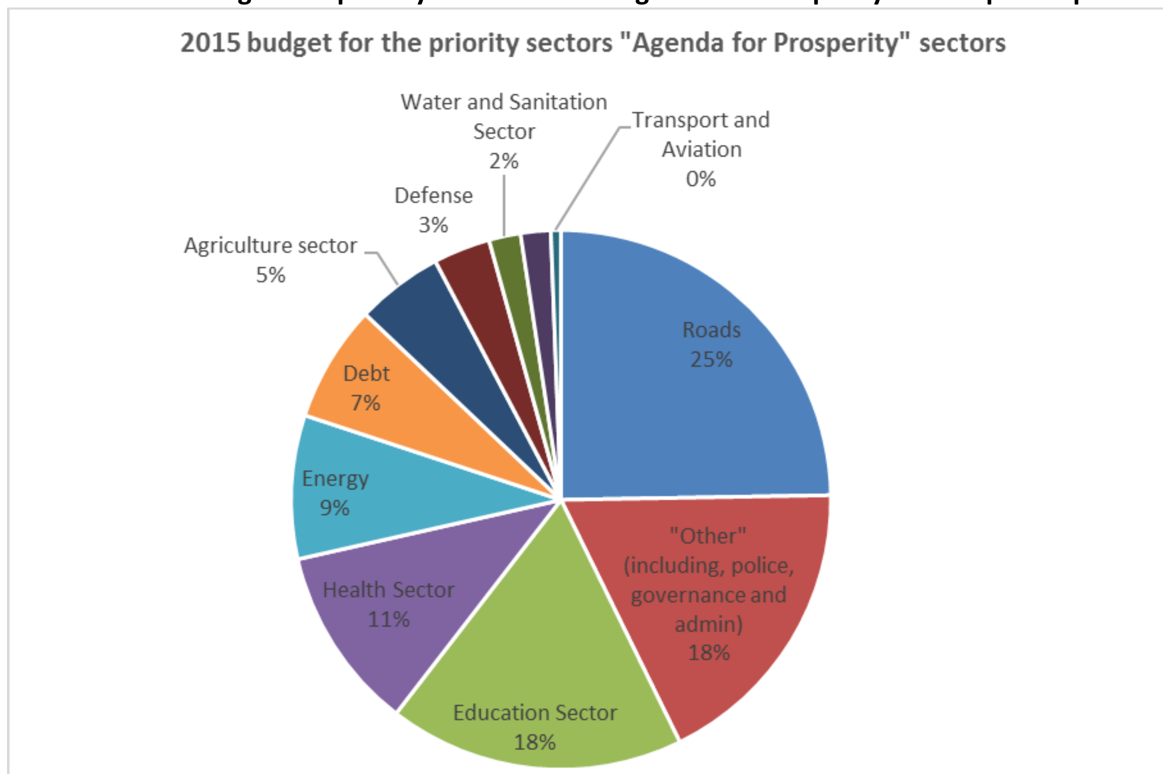


Table 4. Sierra Leone overall breakdown of budget, 2015

2015 budget for the priority sectors in "Agenda for Prosperity"	
Sector/Programme	**percentage of total budget**
Roads	24.7%
Other, including, police, governance and admin	18%
Education Sector	17.7%
Health Sector	11%
Energy	8.6%
Debt	7.0%
Agriculture sector	5.2%
Defence	3.4%
Water and Sanitation Sector	1.9%
Social Protection, minus pensions etc	1.8%
Transport and Aviation	0.6%

3.2 What do we know about sector spending, and its inequality effect in Sierra Leone?

By applying the benefit incidence coefficients derived from Martinez-Vazquez et al global study to Sierra Leone, it is possible to see that social spending is likely to be marginally progressive, bringing down the Gini coefficient by 0.01%. Of the 3 countries in this study social spending in Sierra Leone was found to have the (relatively) least impact on inequality impact, however, they remain about in the middle of a larger data-set of 16 West African countries. With increases in health spending in the latest year's budgets this could well also improve future scores of spending on inequality.

In particular, education spending is very skewed towards tertiary; and spending on tertiary and secondary schooling consumes 56% of the total spending. This is likely to have a regressive impact in a country where wealth appears to be the largest factor explaining a lack of schooling (either entry, progression or completion through levels). For instance, the wealthiest quintile had a completion rate of 84% in primary school, compared to only 34% for poorest. Meanwhile only 1% of the poorest quintile and 3% of the next poorest quintile completes secondary schooling, yet 41% of the richest do. This means that the richest are consuming the vast majority or resources, which is likely to be very regressive.

Health spending, while improving in quantity terms, which is also likely to be matched by renewed vigour behind old commitments as a result of the Ebola crisis, has been historically low, in spite of pledges to make the system more progressive. In 2010 the Government of Sierra Leone removed user fees for pregnant women, lactating mothers and children under five, under the Free Health Care Initiative (FHCI). But, in spite of this commitment, per capita costs have remained very low in health, as noted above, in fact, in 2014, this was around one-quarter of the per capita amount needed estimated by the Chatham House recommendation to finance a basic essential health package for all. Moreover, Sierra Leone has continued to have very low levels of spending on health workers – leading to some of the worst ratios of midwives to patients in the world. So that, even

with this commitment, many went without or sought out private care due to very overstretched workers

Moreover, according to data compiled by the ILO World Social protection report (see chart 1 in introduction), currently in Sierra Leone 75% of the population access healthcare but this is virtually *all* covered by out of pocket payments!

This has disastrous impacts on the poor, pushing millions into poverty when a health crisis occurs, or leaving the poorest unable to access urgent health services. Nowhere is the impact been more urgently and dangerously felt than in the rampant spread of Ebola in 2014 Therefore, it is vital that new and substantial increases to spending, boosted by progressive financing, are found. One such suggestion has recently been mooted through a Withholding Tax earmarked for funding the FHCI. While it is true that the Sierra Leone governments has a responsibility to ensure that their citizens are benefiting, and not simply the multinational companies who are extracting the mineral wealth, some caution is required in terms of earmarked funds – they must be part of an overall plan to ensure that new resources are not only allocated to one sector but are part of sustainable long term solution to scale up social sector spending. Even with such a tax, large financing gaps exist which, one DFID-commissioned financing gap analysis concluded would require donor funding to support.[103]

The very low per capita spending levels across health, and education, as well as low budget commitment to social protection, suggests that the government may have to work even harder, or boost their overall budget levels through larger revenues, in order to scale up all social sector services, quality and reach. And without quality there can be no equity. If patients cannot be seen be a doctor, or access essential medicines, while children are in school but quality is so low to ensure learning, then equity is not well served. Indeed, very low levels of revenue raising in Sierra Leone leave budget availability very constrained, and total revenue has been consistently lower than expenditure revenue.

Finally, geographical inequalities remain stark in Sierra Leone, and need to be addressed - which has been further exacerbated by Ebola. Beyond the loss of life, the restriction of movement inside and outside the country, and the closure of food products markets have led to disruptions in supply, causing a drastic drop in household income and at the same time surging basic food prices. Thus the crisis of Ebola has further widened social inequality in Sierra Leone. The spatial nexus in Sierra Leone is essentially rural and urban, further exacerbated by the long period of instability in the civil way when the ruling elite systemised privileged rent-seeking at the expense of the public interest. This behaviour has contributed to the continuation of regional disparities in health and education inherited from the British colonial system. Currently, the urban population has the lion's share of services. The country needs to address these disparities so they do not add to further inequalities in the future, notably through a detailed analysis of financing and spending formula.

4.Conclusions and Recommendations

In Sierra Leone, economic inequality remains relatively low, but geographical inequality remains stark, while extremely low levels of human development and high levels of extreme poverty persist throughout the country.

According to the DFI/OI tax structural progressivity index, Sierra Leone performs well, coming 60th worldwide and 7th among ECOWAS countries, due to a combination of low VAT and relatively high personal and corporate income tax rates. This places it above Burkina Faso and Ghana. However, it

could reform its GST and replace it with a VAT, and do a great deal more to tax capital gains, property and wealth. Overall, according to the DFI/OI tax incidence indicator, Sierra Leone is average, ranking 71st globally and 5th regionally, with a tax system which is only marginally regressive. This reflects its relatively low dependence on VAT and other indirect taxes on consumption and trade, reflecting its high minimum VAT registration threshold. This is somewhat offset by the very poor record of collecting direct corporate and personal taxes which are more progressive. These findings emphasise the need for it to increase the collection of progressive taxes, and reform the VAT/GST system, to make the tax system more progressive.

In spite of a (relatively) good revenue raising record, Sierra Leone has not committed enough funds to sustainably scaling up social sectors. Recent increases in health are being offset by lower spending in education- and rather large spending on non-social sectors may limit the equality busting impact of budget allocations. The Ebola crisis should have been a wake-up call that it is time for the natural resource wealth that Sierra Leone is endowed with, to be better translated into quality services for all. To promote inclusive growth and an economy more resilient to external shocks, the Government has made the reduction of inequality a key pillar of its strategy to build a prosperous economy by 2035 – it is now time to truly invest in this agenda.

The Sierra Leone government should focus on the following recommendations:

1. Tax

- **Enhance tax effort** by: reducing exemptions and deductions; fighting tax dodging more effectively on corporate and personal income tax; changing its GST into a VAT; and renegotiating tax treaties to allow higher withholding taxes, capital gains taxes and taxes on dividends.
- **Make the design of its tax system more progressive** by: increasing taxes on capital gains, inheritance and gifts to match income tax rates; perhaps reducing the bottom rate of personal income tax; replacing the GST with a pro-poor VAT including exemptions on basic goods but eliminating other exemptions; and reducing the minimum GST/VAT threshold to ensure middle-income businesses pay tax.
- **Make tax collection more progressive** by: increasing the proportion of taxes from personal and corporate income tax (by reducing exemptions, deductions and dodging), and capital gains/ property/wealth taxes; making the GST/VAT more progressive and reducing regressive exemptions; and carrying out an incidence study to measure actual impact on inequality.

2. Spending

- **Invest more in lower levels of education to increase impact on inequality, and reverse the overall education spending decline in 2016 budgets.** Based on a comprehensive analysis of education spending incidence, reconfigure spending to be more pro-poor and inequality busting, moving spending from higher levels to lower levels where most of the poor access education.
- **Sustainably increase financing for education to scale up fee-free health services**, firstly for women and children, as committed to in the Free Health Care Initiative (FHCI), with the long term ambition of achieving free Universal Health Coverage.
- **Scale up spending on social protection dramatically from current very low levels,** through non-contributory cash transfer programmes which can be gradually scaled up into a universal floor.
- **Address large scale spatial inequalities** through better targeted financing aimed at targeting geographical inequality.

Annex 1. Snapshot of data findings on tax and spending for each country

Below are data snapshots for the three countries in this study showing core data findings.

The inequality data are shown for the two indicators chosen to measure inequality, Gini and Palma, the methodology for which is explained in section 1.

The tax data are presented in terms of the three indicators, as outlined in section one. This also gives the ranking of the country in the global DFI/OI tax database. The three areas are:

1. Tax effort compared to potential (percentage of actual/potential tax revenue)
2. Intended progressivity (the country's rank in the DFI database)
3. Actual progressivity (actual or estimated impact on the Gini coefficient)

The spending data are presented in units which enable comparison with other countries: the share of budget or GDP going to these areas (as a proxy for government commitment), and US$ per capita. It also compares then counties to how close they are to meeting international spending benchmarks.:

1. On health, the Abuja commitment to spend 15% of budget on health, and the "Chatham house recommendation" US$86 dollars to meet the basic and essential healthcare needs of all;
2. On education, the Incheon framework recommendation to spend between 15-20% of budget allocations or 4-6% of GDP.
3. On social protection, the AU Windhoek Conference commitment by African governments to fund a basic Social Protection Floor, the cost of which was determined at 4.5% of GDP.

Data snapshot – Ghana (latest years' available data)			
Inequality data			
Palma ratio (2015)		**Gini (2011)**	
2.2		46	
Tax data, 2015			
Tax effort (% of potential, rank)	**Intended progressivity (Rank of 155)**	**Actual progressivity (impact on Gini, rank)**	**Overall progressivity (Rank of 155)**
52%, 101	110	-0.01 to +0.01, 50-68	113
Social spending data 2015-16			
Education spending (as % of budget)	Health spending (as % of budget)	Social protection spend (as % of budget)	Total social spending (as % of budget)
17%	8%	>1%	27%
Education spending (as % of GDP)	Health spending Per Capita spending (international min US$87)	Social protection spend, including contributory, (as % of GDP), *2011*	Total social spending (as % of GDP)
5%	US$32	2.3%	10% GDP
Meeting Incheon international commitments? *Yes (lower end)*	**Meeting regional/international commitments?** *No*	**Meeting Windhoek social protection commitment?** *No – far off*	**Likely impact on inequality** *Average*

Data snapshot – Burkina Faso (latest years available data)			
Inequality data			
Palma ratio (2015)		**Gini (2011)**	
1.84		39.8	
Tax data, 2015			
Tax effort (% of potential, rank)	**Intended progressivity (Rank of 155)**	**Actual progressivity (impact on Gini, rank)**	**Overall progressivity (Rank of 155)**
73%, 42nd	103	+0.04, 125	85
Social spending data 2015			
Education spending (as % of budget)	Health spending (as % of budget)	Social protection spend (as % of budget)	Total social spending (% of budget)
16.6%	10%	>1%	28%
Education spending (as % of GDP)	Health spending Per Capita spending (international minimum spend US$87)	Social protection spend, including contributory, (as % of GDP), 2011	Total social spending (as % of GDP)
4.92%	US$18.3	1.8%	9.7%
Meeting Incheon international commitments? *Yes (lower end)*	**Meeting regional/international commitments?** *No*	**Meeting Windhoek social protection commitment?** *No – far off*	**Likely impact on inequality** *Slightly above average*

Data snapshot – Sierra Leone (latest years' available data)			
Inequality data			
Palma ratio (2015)		**Gini (2011)**	
1.5		34	
Tax data, 2015			
Tax effort (% of potential, rank)	**Intended progressivity (Rank of 155)**	**Actual progressivity (impact on Gini, rank)**	**Overall progressivity (Rank of 155)**
50%, 104th	60th	+0.01, 71st	99
Social spending data 2016			
Education spending (as % of budget)	Health spending (as % of budget)	Social protection spend (% of budget)	Total social spending (% of budget)
18%	11%	>1%	29%
Education spending (as % of GDP)	Health spending Per Capita spending (international minimum spend US$87)	Social protection spend, including contributory, (as % of GDP), 2011	Total social spending (as % of GDP)
4%	US$21	>1%	7%
Meeting Incheon international commitments? *Yes (lower end)*	**Meeting regional/international commitments?** *No*	**Meeting Windhoek social protection commitment?** *No – far off*	**Likely impact on inequality** *Slightly above average*

ANNEX 2. PRESENTING CROSS COUNTRY COMPARABLE DATA

This annex presents the cross country spending and tax figures, for a larger data-set for comparisons referred to in the above case studies in one place for ease of reference.

Below is spending data broken down into two clusters for cross-country comparison:

1. Different income groups for the three countries in this study (i.e. Low-Income Countries for Burkina Faso and Sierra Leone and Lower-Middle Income Countries' for Ghana),
2. Comparisons to sub-Saharan African Countries, as two clusters of possible comparison.

This is because spending on social sectors tends to be most comparable to country income group spending. There are also common trends across Africa, compared to other regions.

This looks at the spending on the three core social sectors, namely education, health and social protection, for 2015 budget (planned) spending as a percentage of total government expenditure, although social protection data dates vary. It also looks at the spending on these three sectors together to compare social with primary spending. This is complemented by country specific data in the country profiles. Data on social protection includes both contributory and non-contributory, where we have compiled a larger cross county sample for 2015; however, in individual country examples we use only non-contributory data as well.

Chart 14. Education spending as a percentage of total budget, Low-Income countries, 2015

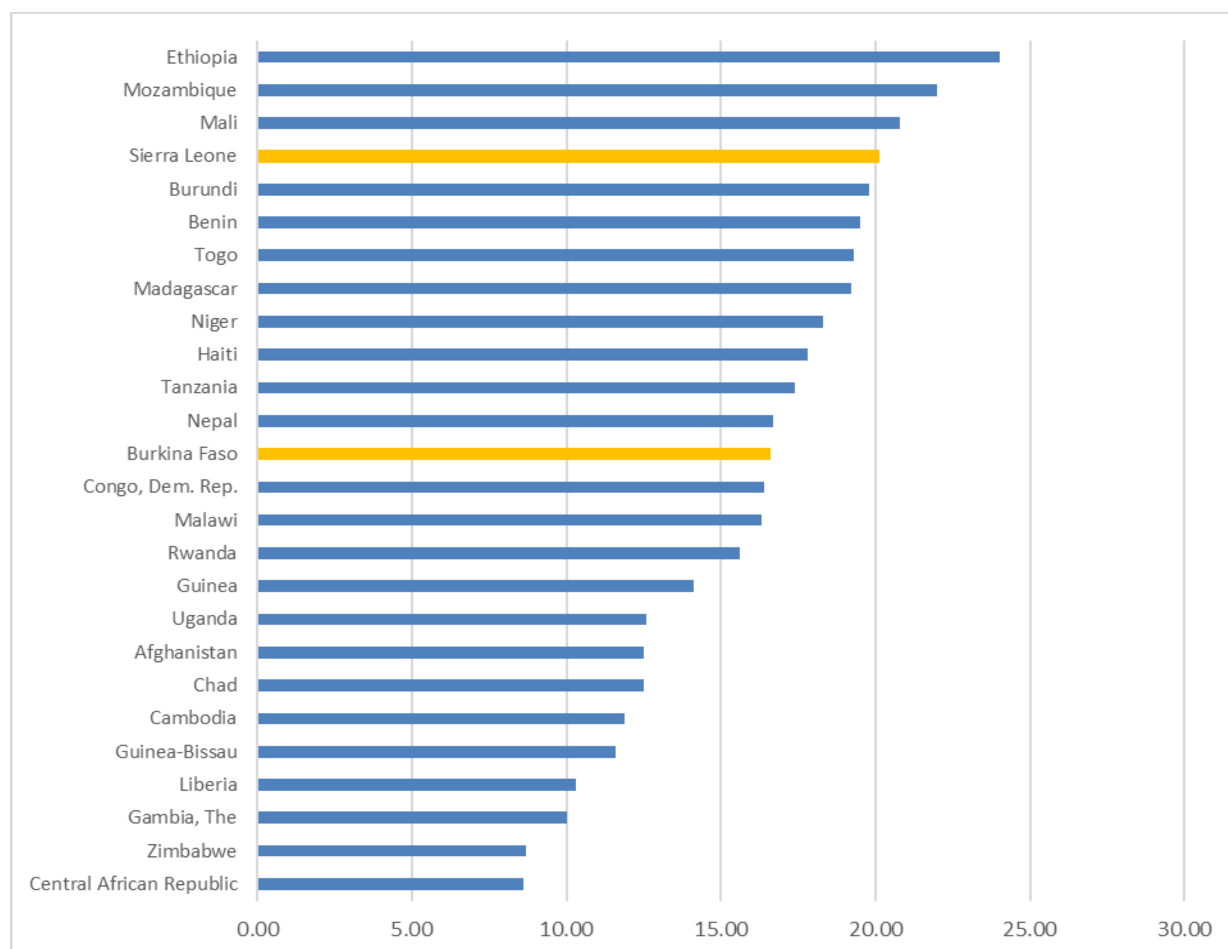


Chart 15. Low-Income Countries, health spending as % of total budget, 2015

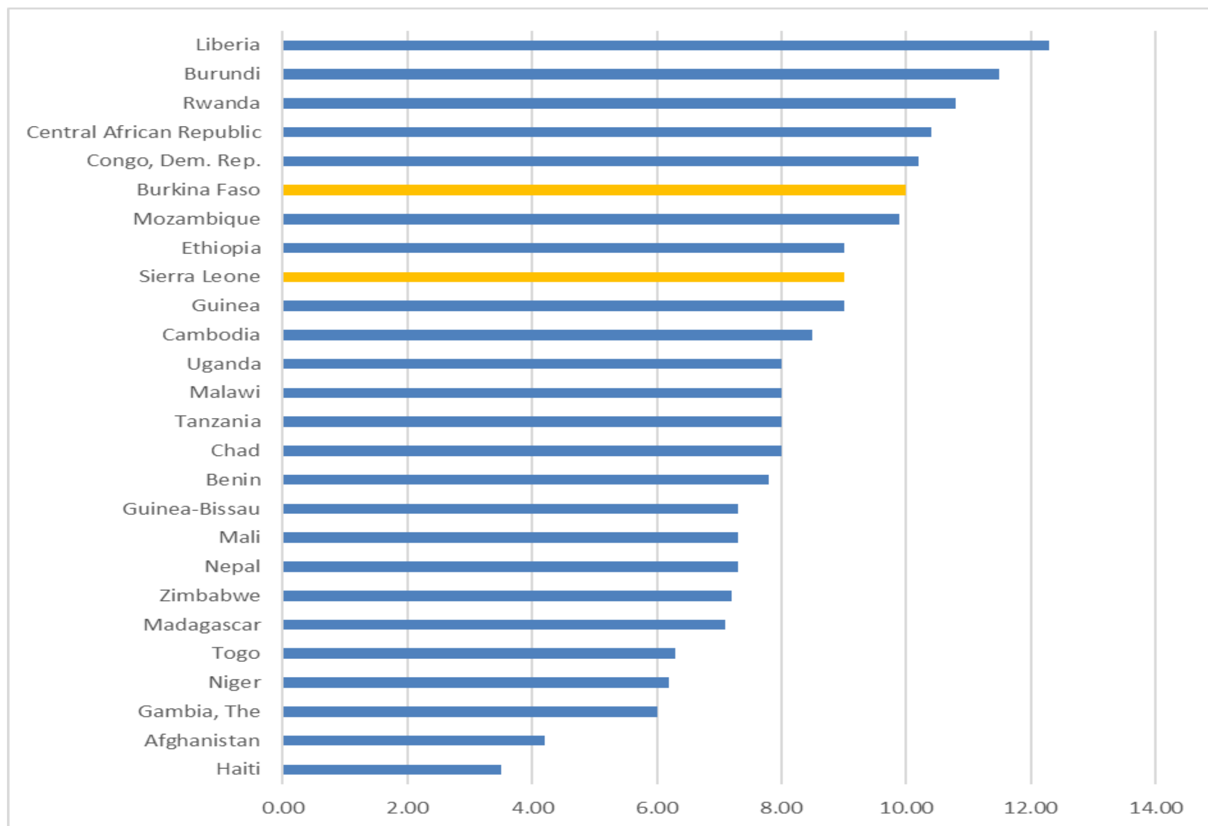
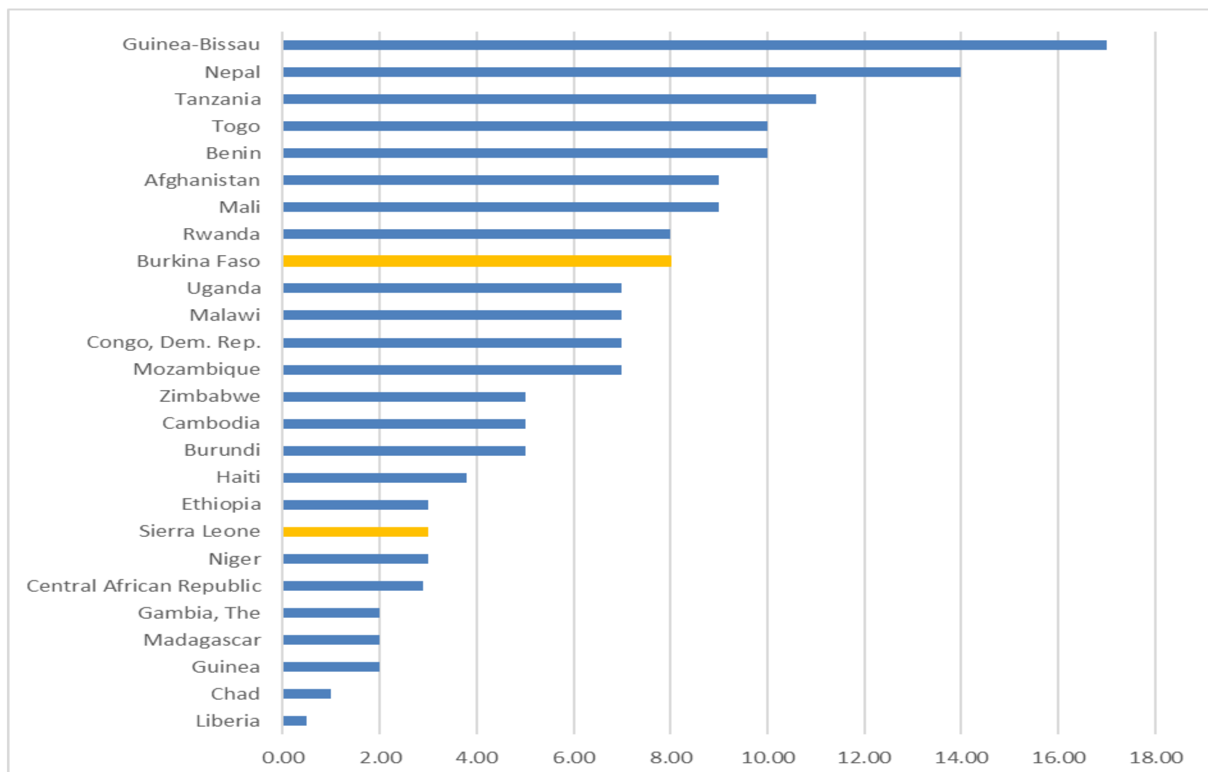


Chart 16. Social protection spending as % of total budget, Low-Income countries, 2010-2014*



** Note social protection uses the ILO latest data - so years are not strictly comparable with other sectors*

Chart 17. All social sector spending as % of total budget, Low-Income countries, 2015

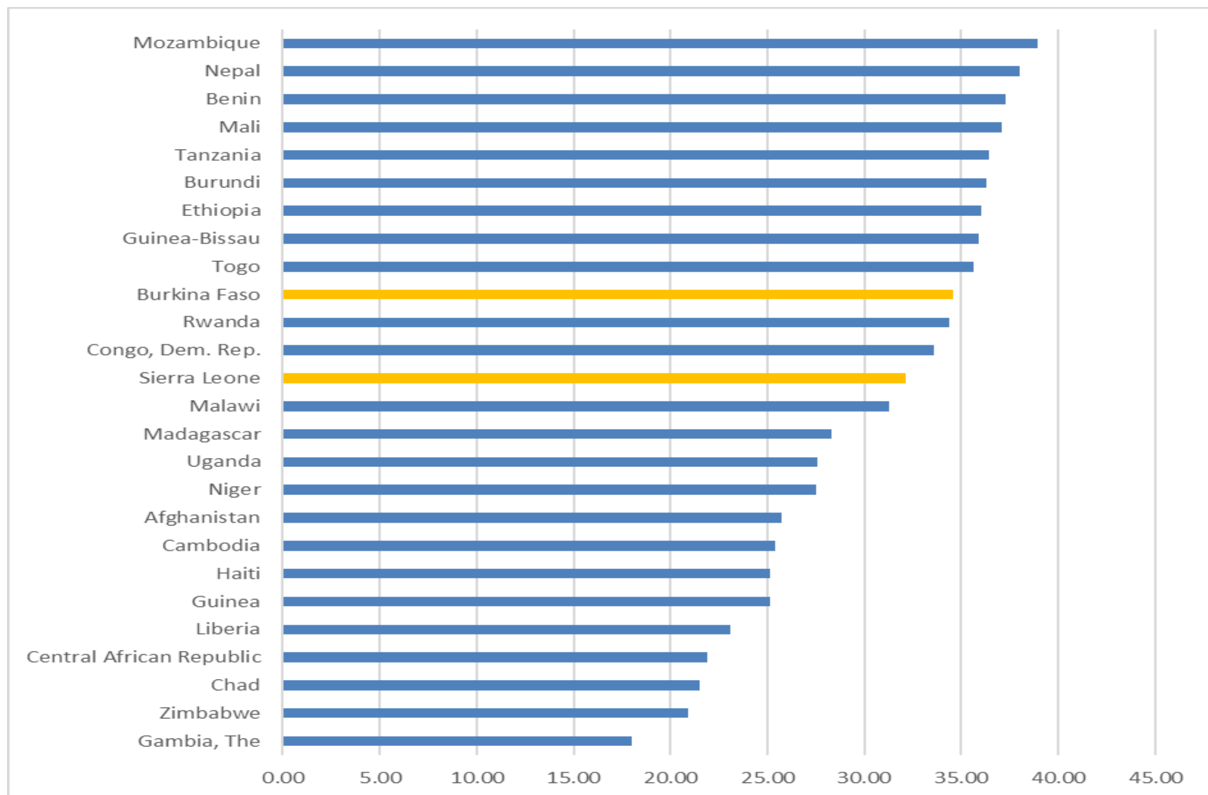


Chart 18. Education spending as % of total budget, sub-Saharan African Countries, 2015

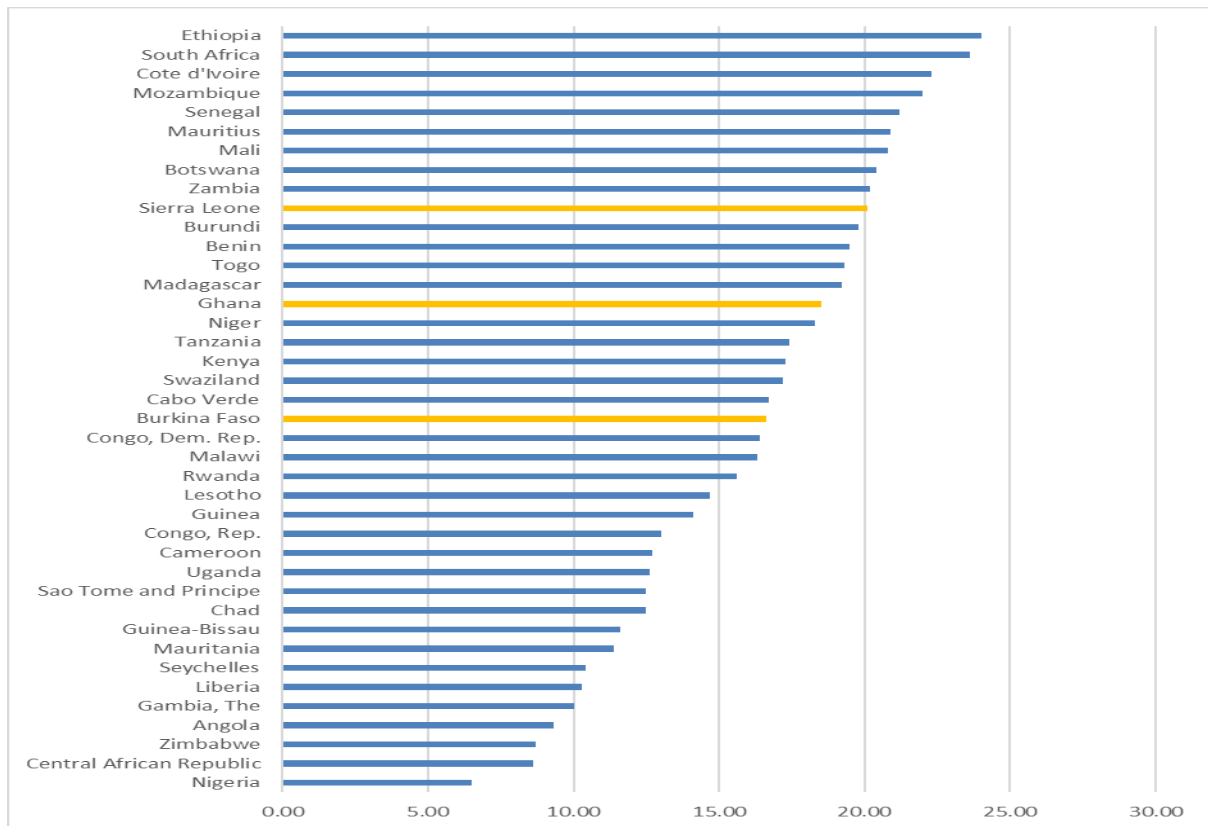


Chart 19. Health spending as a percentage of total budget, sub-Saharan African Countries, 2015

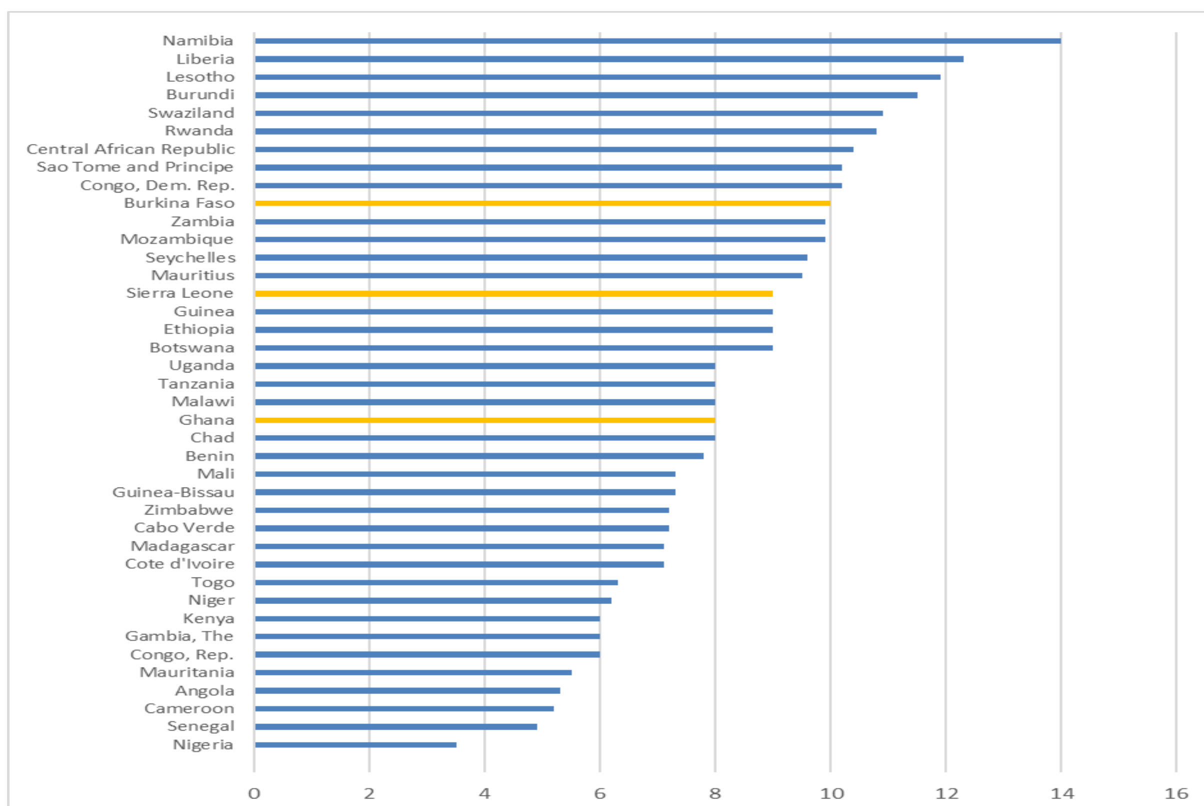
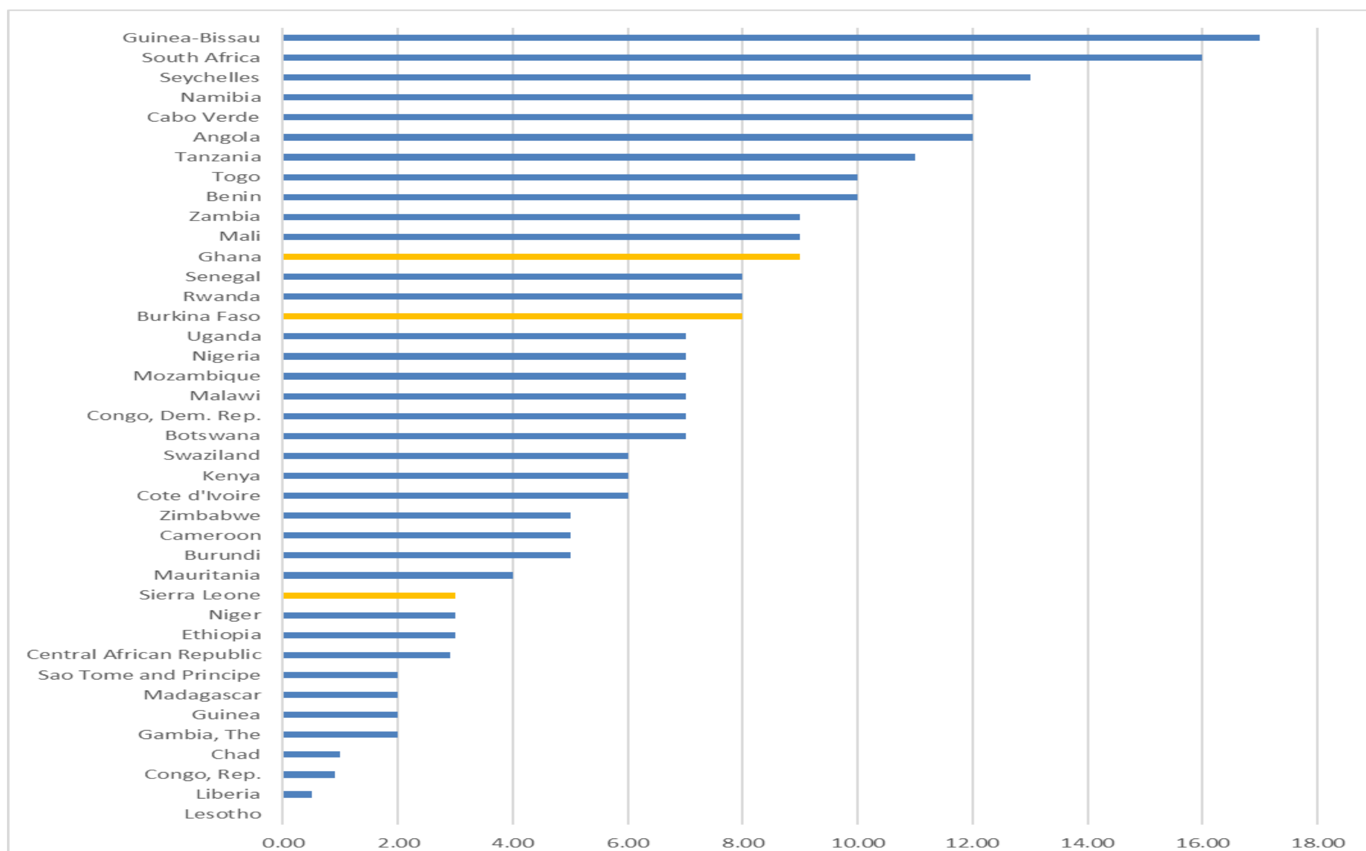


Chart 20. Social protection spending as % of total budget, Sub-Saharan Africa, 2011-2014*



** Note social protection uses the ILO latest data - so years are not strictly comparable with other sectors*

Chart 21. Spending on all three social sectors, as % of total budget, Sub-Saharan Africa, 2015

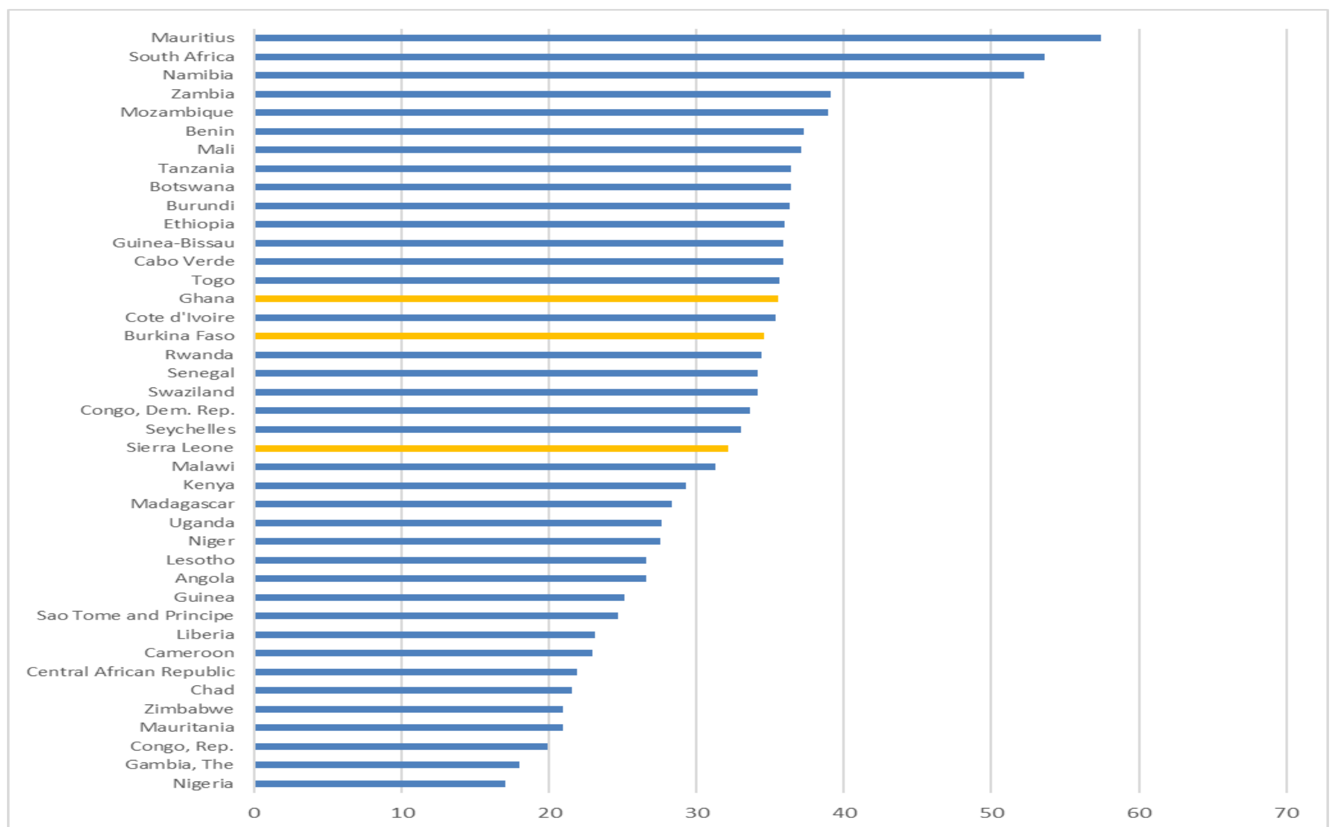


Chart 22. Education spending as % of total budget, Lower-Middle Income Countries, 2015

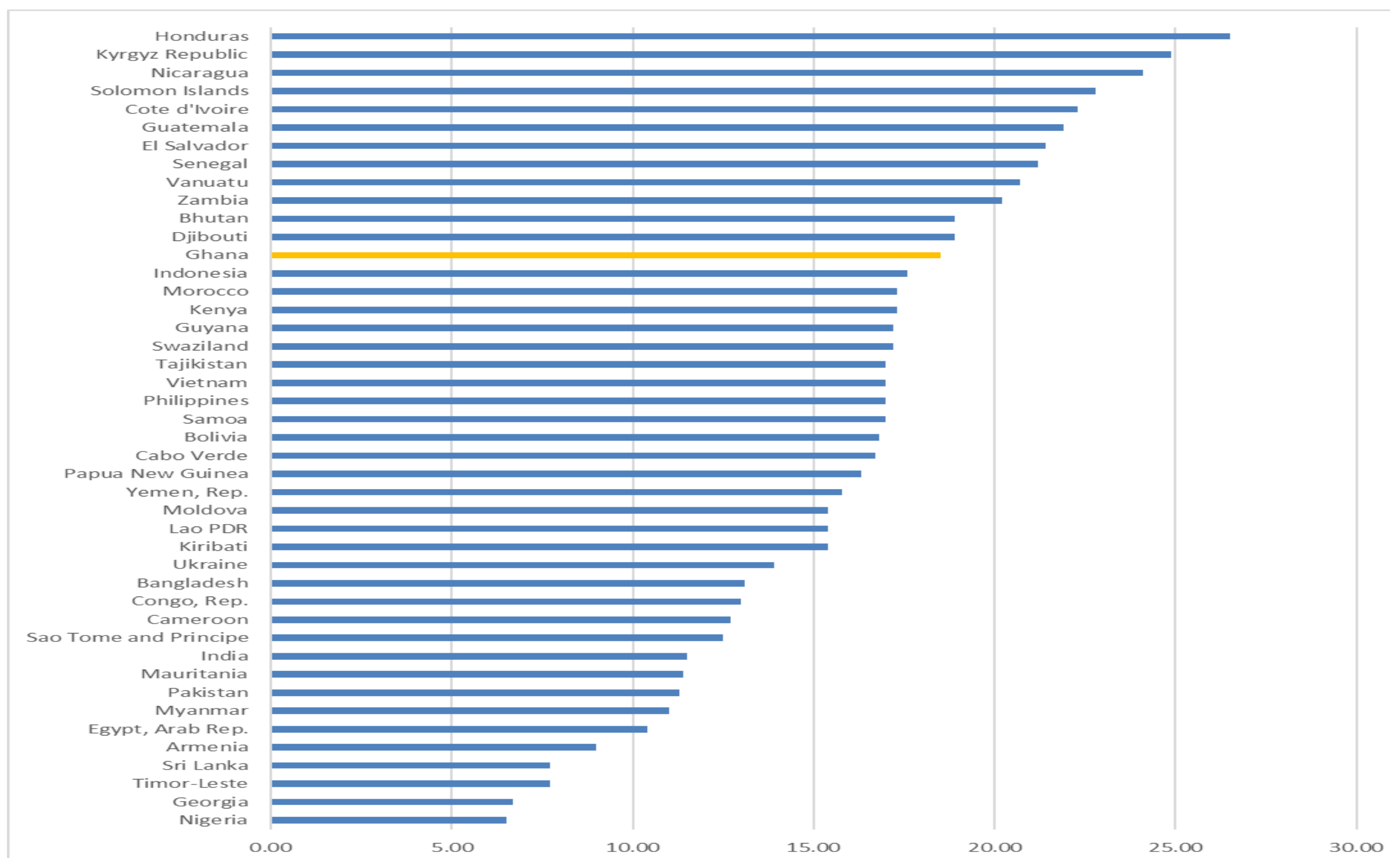


Chart 23. Health spending as % of total budget, Lower-Middle Income Countries, 2015

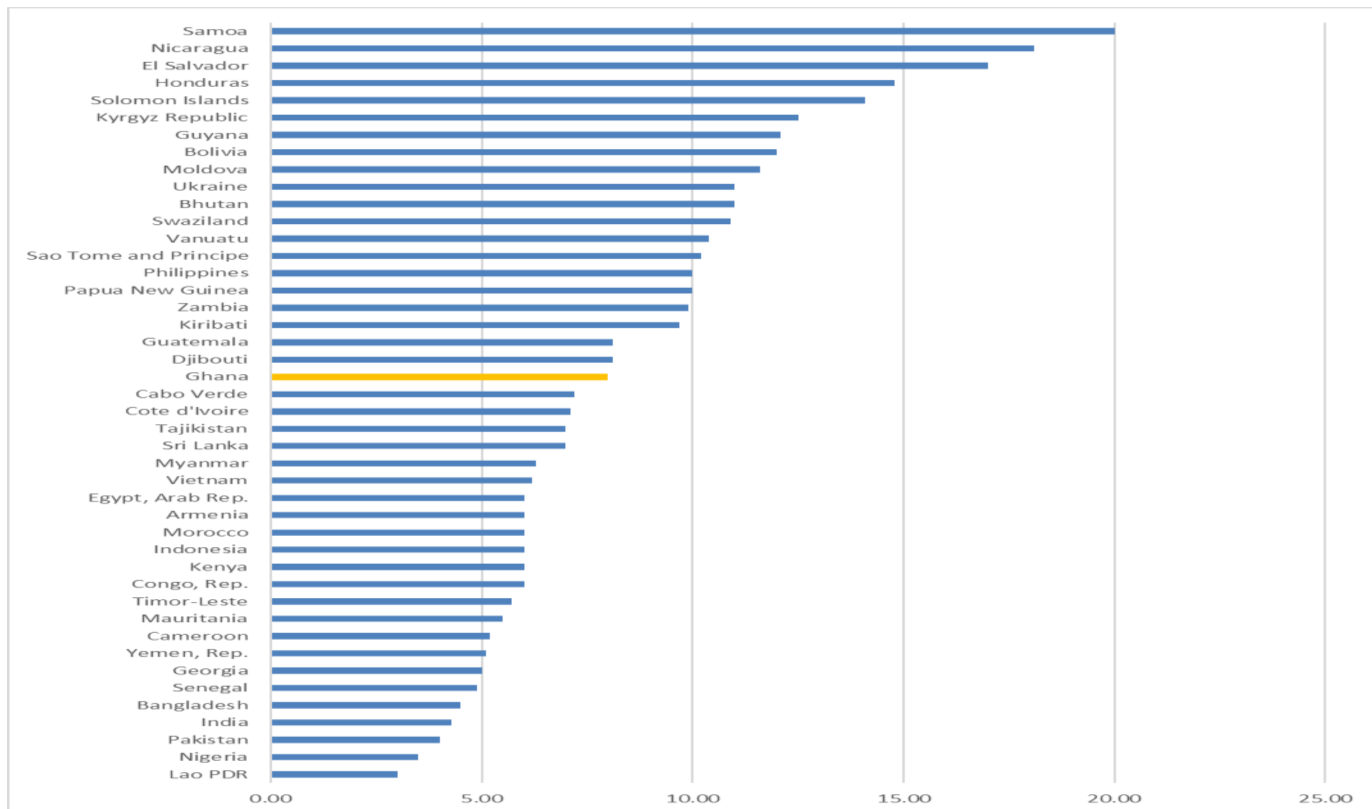
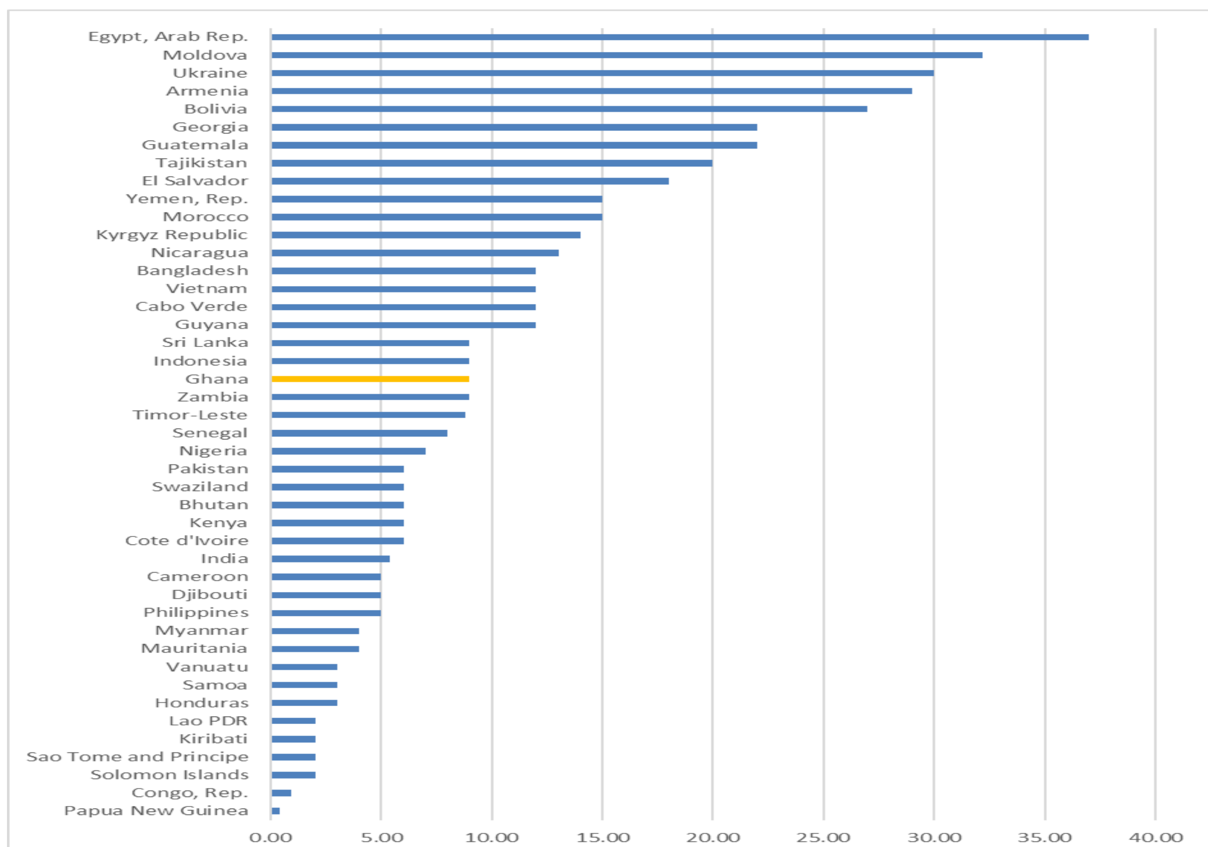
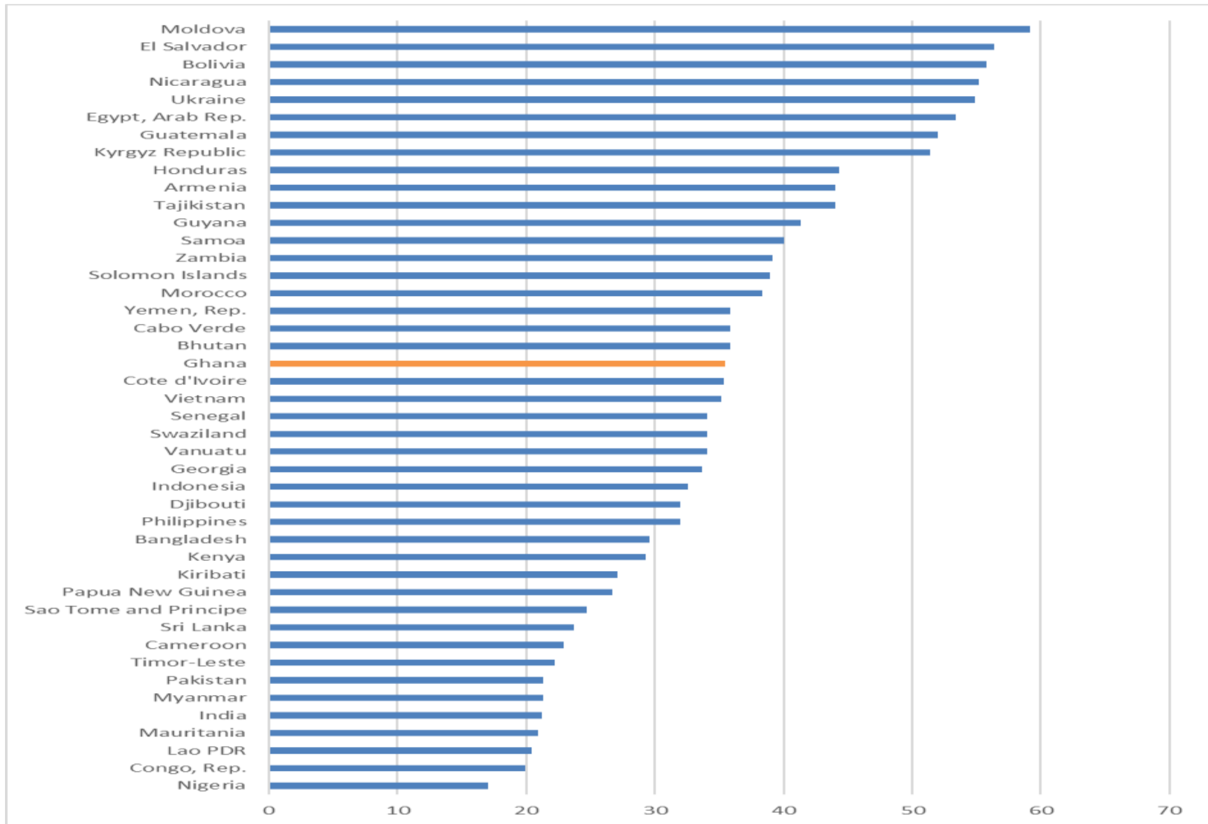


Chart 24. Social Protection spending as % of budget, Lower-Middle Income Countries, 2010-2014*



** Note social protection uses the ILO latest data - so years are not strictly comparable with other sectors*

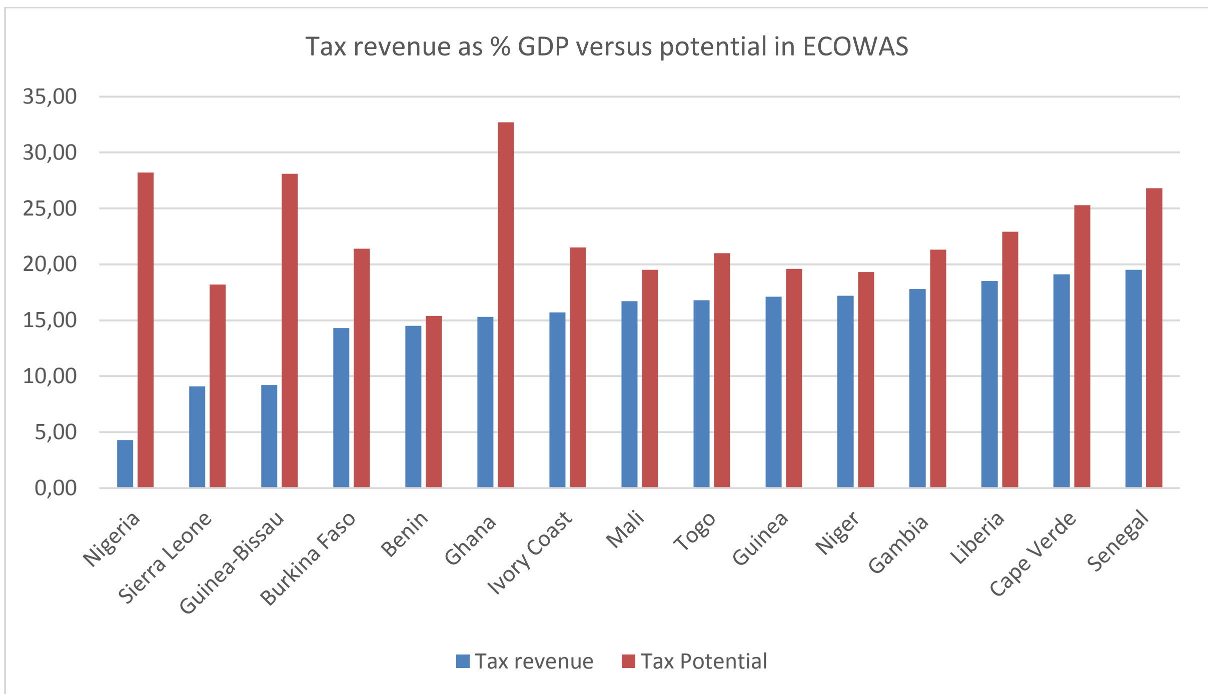
Chart 25. Spending on all three sectors, as % of total budget, Low-Middle Income Countries, 2015



Tax data

Tax data is compared to West Africa as tax policies tend to be more regionally focused.

Chart 26. Tax revenue as % GDP versus potential in ECOWAS



Source: DFI tax database using IMF figures.

[1] See OECD 2015, In It Together: Why Less Inequality Benefits All; and http://www.imf.org/external/pubs/ft/survey/so/2014/RES041214A.htm?utm_source=feedburner&utm_medium=feed&utm_campaign=Feed%3A+devj%2Fimf+(IMF)

[2] World Bank (2016). Poverty in a Rising Africa. http://www.worldbank.org/en/region/afr/publication/poverty-rising-africa-poverty-report

[3] Oxfam (2015). A Dangerous Divide: The State of Inequality in Malawi. http://policypractice.oxfam.org.uk/publications/a-dangerous-divide-the-state-of-inequality-in-malawi-582678

[4] Web article accessed September 2016, http://www.uneca.org/stories/southern-africa-most-unequal-region-africa

[5] This comparison is known as the "Palma ratio". See box 1 in main report for explanations of different measurements

[6] To be precise Ghana was ranked the 20th most unequal, Burkina the 29th, and Sierra Leone the 34th (based on authors own calculations and rankings Using Palma - see box 1 in main report for explanations of different measurements

[7] World Health Organization (WHO) data. Based on web article accessed September 2016 https://www.yahoo.com/news/ebola-lessons-spur-sierra-leones-fight-against-maternal-013341411.html

[8] See, http://blogs.savethechildren.org.uk/2016/05/burkina-faso-takes-a-step-closer-to-universal-health-coverage/ . Accessed September 2016

[9] For instance, See OECD 2015, In It Together: Why Less Inequality Benefits All: Or the global panel study by Martinez-Vazquez and Moreno-Dodson of incidence studies covering 150 countries over a 30 year period.

[10] Oxfam International, 2016, The Time is Now: Building a Human Economy for Africa, http://policy-practice.oxfam.org.uk/publications/the-time-is-now-building-a-human-economy-for-africa-608510

[11] See http://www.oecdobserver.org/news/fullstory.php/aid/3782/How_tax_can_reduce_inequality.html

[12] See http://repositorio.cepal.org/bitstream/handle/11362/36693/6/LCG2586SES353e_en.pdf for example, page 37.

[13] Oxfam International, 2016, The Time is Now: Building a Human Economy for Africa, http://policy-practice.oxfam.org.uk/publications/the-time-is-now-building-a-human-economy-for-africa-608510

[14] It should however be noted that Ghana's GDP was revised upwards in 2008 by 40%, to take account of estimates of the informal sector. Before that, Ghana had a tax/GDP ratio well over 20%.

[15] See Global Financial Integrity (2015), Illicit Financial Flows from Developing Countries 2004-13, at http://www.gfintegrity.org/wp-content/uploads/2015/12/IFF-Update_2015-Final-1.pdf

[16] This is not always the case: actual regressively or progressivity is strongly influenced by VAT rates and exemptions

[17] See Lustig, Nora. 2015. The Redistributive Impact of Government Spending on Education and Health: Evidence from Thirteen Developing Countries in the Commitment to Equity Project. CEQ Working Paper No. 30, Center for Inter-American Policy and Research and Department of Economics, Tulane University and Inter-American Dialogue, February, available at www.commitmentoequity.org/publications_files/Comparative/CEQWPNo30%20RedisImpactGovntSpendEducHealth%20March%202015.pdf. See also OECD 2015, In It Together: Why Less Inequality Benefits All

[18] Oxfam International, 2011. "Achieving a Shared Goal: Free Universal Health Care in Ghana". https://www.oxfam.org/sites/www.oxfam.org/files/rr-achieving-shared-goal-healthcare-ghana-090311-en.pdf

[19] Web article, accessed September 2016 http://blogs.savethechildren.org.uk/2016/05/burkina-faso-takes-a-step-closer-to-universal-health-coverage/

[20] ILO, 2014. World Social Protection Report 2014-2015. Page 105

[21] Rose, P. and Ilie, S. (2016), Funding widening participation in higher education: implications for the distribution of public financing in South Asia and sub-Saharan African counties.

[22] UNESCO-UIS (2016), Data Centre, United Nations Educational, Scientific and Cultural Organization, Montreal. http://www.uis.unesco.org/datacentre/pages/default.aspx

[23] http://www.education-inequalities.org/countries/burkina-faso#?dimension=all&group=all&year=latest

[24] MICS, 2006-2001

[25] https://www.oxfam.org/sites/www.oxfam.org/files/file_attachments/rr-food-secuity-burkina-faso-school-canteens-070415-fr.pdf

[26] UNESCO (2014), Education for All Global Monitoring Report 2013/14: Teaching and Learning – Achieving Quality for All, United Nations Educational, Scientific and Cultural Organization, Paris. http://unesdoc.unesco.org/images/0022/002256/225660e.pdf

[27] UNICEF (2015b), Simulations for Equity in Education (SEE), United Nations Children's Fund, New York. http://www.unicef.org/education/bege_SEE.html

[28] See K. Watkins and W. Alemayehu (2012) Financing for a Fairer, More Prosperous Kenya: A review of the public spending challenges and options for selected Arid and Semi-Arid counties, Brookings Institute, for a useful discussion of these models.

[29] An unpublished DFI report for IBP discusses this at length and can be shared if needed. .

[30] http://www.imf.org/en/News/Articles/2016/07/26/14/42/NA072816-New-IMF-Study-Data-Tool-Track-Fiscal-Policies

[31] For examples, see OECD 2015, In It Together: Why Less Inequality Benefits All, the global panel incidence study by Martinez-Vazquez and Moreno-Dodson covering 150 countries over 30 years, The Impact of Tax and Expenditure Policies on Income Distribution: Evidence from a Large Panel of Countries, and country-level analysis by CEPAL, CEQ, EU and OECD (In it Together: Why Less Inequality Benefits All). See also N. Lustig (2012) 'Taxes, Transfers, and Income Redistribution in Latin America', Inequality in Focus 1(2); Lustig, Nora. 2015,.

[32] http://pubdocs.worldbank.org/pubdocs/publicdoc/2015/10/503001444058224597/Global-Monitoring-Report-2015.pdf

[33] See Duncan, D, and Sabirianova, K.P. (2008), Tax Progressivity and Income Inequality, Georgia State University Andrew Young School of Policy Studies Working Paper 2008-6-5; TO ADD IMF, OECD, CEPAL, Asian Development Bank, etc.

[34] Duncan and Sabirianova Peter, 2008

[35] IMF. (2011, March). *Revenue Mobilization in Developing Countries*

[36]Keen, M., & Mansour, M. (2009, July). *Revenue Mobilization in Sub-Saharan Africa: Challenges from Globalization, IMF Working Paper 157.* http://www.imf.org/external/pubs/ft/wp/2009/wp09157.pdf

[37] IMF. (2011, March). *Revenue Mobilization in Developing Countries*

[38] The database and its methodology have benefited from inputs from tax experts from the IMF, World Bank and Tax Justice Network and CEQ Commitment to Equity programme. An adapted version of the DFI tax database is being used with Oxfam International to design the DFI/OI Commitment to reducing Inequality Index (upcoming publication).

[39] 3 We use a Kakwani index for progressivity of the personal income tax rate; the main corporate income tax rate; and the main VAT/general sales tax rate adjusted for exemptions/lower rates for pro-poor products and for a threshold excluding small companies.

[40] OECD, EU (2015), Wage and Income Inequality in the European Union, Study PE 536.294 for the EMPL Committee; the various individual and multi-country incidence studies available from the Commitment to Equity Institute at Tulane University, at http://www.commitmentoequity.org; CEPAL, Panorama Fiscal de América Latina y el Caribe 2016; and Martinez-Vazquez, J; Moreno-Dodson, B and Vulovic, V (2011), The Impact of Tax and Expenditure Policies on Income Distribution, Andrew Young School of Public Policy Studies, GSU.

[41] To calculate these assessments requires respectively: 1) tax to GDP collected and assessments of a country's "tax potential"; 2) data on individual tax rates/thresholds and a calculation of their relative progressivity; and 3) data on the composition of taxes collected and an assessment of likely incidence of each type of tax.

[42] For more details of these at country level see Development Finance International (2016), IMF Tax Policy Advice and TA: Is It Living Up To (Progressive) Expectations?, policy research report for Oxfam International, April; and at global level see IMF (2015), Options for Low Income Countries' Effective and Efficient Use of Tax Incentives for Investment, Staff Report, October, available at https://www.imf.org/external/np/g20/pdf/101515.pdf

[43] For statements by low-income countries opposing these practices, see the communiqués of Francophone country Finance Ministers available at www.development-finance.org

[44] ICRICT (2015), Declaration of the Independent Commission for the Reform of International Corporate Taxation, citing UNCTAD, available at http://www.icrict.org/declaration/ , The IMF has reached broadly similar conclusions in its 2014 tax spillovers report

[45] See Oxfam GB (2016), Ending the Era of Tax Havens, Briefing Paper, 14 March 2016, available at http://www.actionaid.org/2016/02/mistreated-how-shady-tax-treaties-are-fuelling-inequality-and-poverty .

[46] For instance, See OECD 2015, In It Together: Why Less Inequality Benefits All: Or the global panel study by Martinez-Vazquez and Moreno-Dodson of incidence studies covering 150 countries, over a 30 year period.

[47] This is 1970 to 2009. See Martinez-Vazquez & Blanca Moreno-Dodson: The Impact of Tax and Expenditure Policies on Income Distribution: Evidence from a Large Panel of Countries.

[48] See OECD 2015, In It Together: Why Less Inequality Benefits All: and Lustig, Nora. 2015. The Redistributive Impact of Government Spending on Education and Health: Evidence from Thirteen Developing Countries in the Commitment to Equity Project. CEQ Working Paper No. 30, Center for Inter-American Policy and Research and Department of Economics, Tulane University and Inter-American Dialogue, February.

[49] O"Donnell et al (2007) „The Incidence of Public Spending on Healthcare: Comparative Evidence from Asia", The World Bank Economic Review 21(1) (January 1): 93–123, http://wber.oxfordjournals.org/content/21/1/93 shows that health spending was found to be inequality reducing in 11 of 12 Asian countries.

[50] This may be different dependent on the level of completion and access in a country. For instance, the OECD has analysed policies in OECD countries and shown that investment in upper secondary promotes equal access to education which helps reduce inequality. See "Reducing income inequality while boosting economic growth: Can it be done?" https://www.oecd.org/eco/growth/49421421.pdf . See De Gregorio, J., and J-W Lee, 2002, "Education and Income Inequality: New Evidence from Cross Country Data," Review of Income and Wealth, Vol. 48, No. 3. Or UNESCO, 2010. Reaching the Marginalized. EFA Global Monitoring Report. UNESCO

[51] Social protection schemes which are based on some form of employee or employer contribution, especially civil servant pensions schemes which dominate in many low income and lower-middle income countries, rather than a straight tax transfer tend to be much less progressive.

[52] Government Spending Watch uses government budget documents to track spending across a number of sectors which have been shown to reduced poverty and inequality. To do the cross country comparison charts we have added some additional data in about 15-20% of cases.

[53] This is done by both doing in-depth analysis of the spending on different programmes and by applying a weighting for the likely "incidence of spending" by using "benefit incidence studies" which show the impact of spending on the Gini coefficient to calculate the likely "actual" impact of spending on inequality

[54] "Catastrophic" spending is when this is more than 25%: but it is important to note that catastrophic health expenditure does not necessarily lead to impoverishment in the sense of pushing a household below a poverty line. Rich households, or households with access to credit, for example, might be able to pay large medical bills that, while onerous, do not require them to forgo consumption of essentials or of key family investments such as for children's schooling. Impoverishing expenditure, on the other hand, is expenditure that pushes households into, or further into, poverty.

[55] http://www.who.int/bulletin/volumes/93/2/14-139287/en/#R1

[56] Upcoming publication from REAL Centre (2016) Background paper for the International Commission on Financing Global Education Opportunity. Should be published by the commission before the end of the year
[57] See OECD 2015 (Ibid), and http://www.oecd-ilibrary.org/docserver/download/0115391e.pdf?expires=1466589576&id=id&accname=guest&checksum=59FA5834E1E2192CDEF92F4807484562 Evidence on ECCE http://unesdoc.unesco.org/images/0023/002324/232456e.pdf
[58] UNICEF, 2015, The Investment Case for Education and Equity. http://www.unicef.org/publications/files/Investment_Case_for_Education_and_Equity_FINAL.pdf
[59] https://www.odi.org/sites/odi.org.uk/files/odi-assets/publications-opinion-files/9700.pdf
[60] This is done in two ways. Firstly, we assess the incidence of spending using a national incidence study in Ghana from CEQ, and using average global incidences of spending on different sectors have been used to calculate the likely impact of spending. The global study estimates are taken from: Martinez-Vazquez, J; Moreno-Dodson, B and Vulovic, V (2011), The Impact of Tax and Expenditure Policies on Income Distribution, Andrew Young School of Public Policy Studies, GSU. There are no studies of spending impact on Palma.
[61] OECD 2015, and Lustig 2011 and 2015, show there is strong evidence to suggest that both the amount spent and the composition of budgets also matters (the "primary spending" versus social spending)
[62] For instance, See OECD 2015, In It Together: Why Less Inequality Benefits All: Or the global panel study by Martinez-Vazquez and Moreno-Dodson of incidence studies covering 150 countries, over a 30 year period (The Impact of Tax and Expenditure Policies on Income Distribution: Evidence from a Large Panel of Countries). This shows that health spending reduces the Gini coefficient by 0.4-0.7, education by 0.13, and social protection by 0.12. They also show strong impact of social housing, but given a lack of cross country data on social housing spending, we have been unable to include this in the index. It should be a priority, given the strong results, to collect spending data on social housing for future reports. Country-level analysis by CEQ, the EU and the OECD finds similar results. Social housing includes WASH
[63] http://www.oxfam.org.uk/media-centre/press-releases/2016/03/women-spend-two-days-a-month-more-than-men-on-housework-and-childcare
[64] See http://www.afd.fr/jahia/webdav/site/afd/shared/PORTAILS/PAYS/GHANA/PDF/afd-ghana-va.pdf
[65] MDG World Bank World Development Indicators data- See http://mdgs.un.org/unsd/mdg/Data.aspx
[66] Wodon and Coulombe 2007 POVERTY, LIVELIHOODS, AND ACCESS TO BASIC SERVICES IN GHANA
[67] Based Multiple Indicator Cluster Survey 2006-2011. Inequality in Ghana: A Fundamental National Challenge Briefing Paper - April 2014. http://www.undp.org/content/dam/ghana/docs/Doc/Inclgro/Ghana-unicef%20Inequality%20Briefing%20Paper%20FINAL%20DRAFT%20Apr%202014.pdf
[68] It should however be noted that Ghana's GDP was revised upwards in 2008 by 40%, to take account of estimates of the informal sector. Before that, Ghana had a tax/GDP ratio well over 20%. For an analysis reflecting this, see Christian Aid (2009), Taxation and Development in Ghana, at http://www.christianaid.org.uk/images/taxation-and-development-in-ghana.pdf
[69] For a comprehensive analysis of tax exemptions in Ghana, see Action Aid 2014.
[70] For the tax lost, see Action Aid 2014. For spending data, see www.governmentspendingwatch.org
[71] See Global Financial Integrity (2015), Illicit Financial Flows from Developing Countries 2004-13, at http://www.gfintegrity.org/wp-content/uploads/2015/12/IFF-Update_2015-Final-1.pdf
[72] For a presentation on these results, see http://www.commitmentoequity.org/publications_files/Ghana/Fiscal%20Policy%20Inequality%20and%20Poverty%20-%20A%20CEQ%20Assessment%20for%20Ghana%20Oct%2029%202015.pdf
[73] This is taken from the latest ILO spending figures, for which data is only available from 2010, so this is slightly dated.
[74] http://commitmentoequity.org/publications/ghana.php,
[75] Rose, P. and Ilie, S. (2016), Funding widening participation in higher education: implications for the distribution of public financing in South Asia and sub-Saharan African counties.
[76] UNESCO-UIS (2016), Data Centre, United Nations Educational, Scientific and Cultural Organization, Montreal. http://www.uis.unesco.org/datacentre/pages/default.aspx
[77] Oxfam International, 2011. "Achieving a Shared Goal: Free Universal Health Care in Ghana". https://www.oxfam.org/sites/www.oxfam.org/files/rr-achieving-shared-goal-healthcare-ghana-090311-en.pdf
[78] World Health Organization, 2015, Tracking universal health coverage: first global monitoring report. http://apps.who.int/iris/bitstream/10665/174536/1/9789241564977_eng.pdf?ua=1
[79] : Commitment to Reducing Inequality, Fiscal Incidence in Ghana, 2015 http://www.commitmentoequity.org/publications_files/Ghana/CEQ%20WP35%20Fiscal%20Incidence%20in%20Ghana%20Dec%202015.pdf
[80] See budget speech 2016:
[81] UNICEF (2015b),Simulations for Equity in Education (SEE), United Nations Children's Fund, New York. http://www.unicef.org/education/bege_SEE.html
[82] Hoy, C. and Samman, E. (2015) 'What if growth had been as good for the poor as everyone else', Overseas Development Institute, http://www.odi.org/publications/9588-income-inequality-poverty-growth
[83] Data from World Bank and authors own calculations
[84] See, http://blogs.savethechildren.org.uk/2016/05/burkina-faso-takes-a-step-closer-to-universal-health-coverage/ . Accessed September, 2016

[85] For a comprehensive analysis of tax exemptions in Burkina Faso, see the presentation by government to an IMF seminar in 2015 on tax exemptions, available at https://www.imf.org/external/french/np/seminars/2014/waemu/pdf/dabre5.pdf
[86] See Global Financial Integrity (2015), Illicit Financial Flows from Developing Countries 2004-13, at http://www.gfintegrity.org/wp-content/uploads/2015/12/IFF-Update_2015-Final-1.pdf
[87] Do note, this is based on the latest available years from ILO World Social Protection data set, which is 2011, for social protection, and 2015 data from health/education from GSW (i.e. not entirely comparable years)
[88] http://www.ncbi.nlm.nih.gov/pmc/articles/PMC3756435/
[89] Web article, accessed September 2016 http://blogs.savethechildren.org.uk/2016/05/burkina-faso-takes-a-step-closer-to-universal-health-coverage/
[90] ILO, 2014. World Social Protection Report 2014-2015. Page 105
[91] Ibid, UNICEF
[92] UNICEF, 2015, The Investment Case for Education and Equity. http://www.unicef.org/publications/files/Investment_Case_for_Education_and_Equity_FINAL.pdf
[93] http://www.education-inequalities.org/countries/burkina-faso#?dimension=all&group=all&year=latest
[94] Ibid, Save
[95] Zida, A., Berone, P and Lorenzetti, L. (2010), Using National Health Accounts to Inform Policy Change in Burkina Faso, Health Systems 20/20, Abt Associates. http://pdf.usaid.gov/pdf_docs/pnaeb930.pdf
[96] UNESCO (2014), Education for All Global Monitoring Report 2013/14: Teaching and Learning – Achieving Quality for All, United Nations Educational, Scientific and Cultural Organization, Paris. http://unesdoc.unesco.org/images/0022/002256/225660e.pdf
[97] https://www.oxfam.org/sites/www.oxfam.org/files/file_attachments/rr-food-secuity-burkina-faso-school-canteens-070415-fr.pdf
[98] AfDB, 2013
[99] based on DFI calculations
[100] The earlier TJN-Africa/BAN study refers to revenue/GDP reaching
[101] For more details, see Losing Out: Sierra Leone's massive revenue losses from tax incentives, by the Sierra Leone Budget Advocacy Network (BAN), at http://www.christianaid.org.uk/images/Sierra-Leone-Report-tax-incentives-080414.pdf
[102] See Global Financial Integrity (2015), Illicit Financial Flows from Developing Countries 2004-13, at http://www.gfintegrity.org/wp-content/uploads/2015/12/IFF-Update_2015-Final-1.pdf
[103] http://www.opml.co.uk/sites/default/files/Fiscal_Space_Analysis_FHCI.pdf