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Dear Readers,

compared to other developing countries, fragile states suffer from extreme high child mortality, poverty and insufficient economic growth. They thus lag far behind when it comes to reaching the Millennium Development Goals. Weak state structures are a key obstacle for the state to fulfil its core functions. This jeopardises not only the stability of the country itself but also that of its neighbours.

By signing the Paris Declaration, Germany has - together with other donors - committed itself for an increased engagement in countries with fragile statehood. The development of state institutions, i.e. the support to (re)build legitimate state institutions and to strengthen the capacity of the state to restore a relation of trust between state and citizens lies at the centre of this endeavour. However, it has to be avoided that external actors substitute the state's functions.

The following contributions report about projects of German development assistance in the realm of institutional development in countries with fragile statehood. We concentrate especially on the importance of mobilizing state revenues and the importance of formulating a state budget that is both transparent and oriented towards reducing poverty.

I hope you enjoy your reading!

Yours sincerely,

Stefanie Harter

Public Finance Reform

What role does Good Financial Governance play in fragile states?

Public finance: key to sustainable state development

2015 is drawing near and the debate over the millennium development goals (MDGs), in which the importance of legitimate, efficient statehood is becoming ever more evident, is gathering pace. Only with legitimate, efficient state structures can political transformation processes be steered and securely anchored. In many partner countries, however, this is exactly what is lacking. As a result, the implementation of reform processes, which are essential if the MDGs are to be achieved, is either sluggish or simply peters out altogether. It is at this point that state development (or: statebuilding) is called for. State development aims to promote the development of constructive relations between state and society and thus establish resilient and legitimate state structures.

State development and fragility

Although the state development approach is relevant for all development contexts, it was first discussed with respect to countries with fragile statehood. Fragile states are characterized by a low level of governance. This may mean, for example, that their systems of public administration are in no position to allocate their public funds effectively and transparently. For this reason there is a much higher risk of corruption in countries with fragile statehood, which is an issue that has increasingly been a focus of attention given the growing importance of budget support. According to an OECD definition this group of countries, as different as Sierra Leone, Togo, Syria or Afghanistan, lack the

political and administrative capacity and/or the political will to fulfil their core state functions. For this reason capacity development has proved to be a particularly promising approach conducive to efficiency with regard to state development (see box).

Strengthening partner governments and enabling them to fulfil core state functions in accordance with their citizens' expectations is vital for the establishment of legitimate and resilient state structures. At the same time the participation of players from society must be promoted, in order to facilitate the dialogue between government and society. Processes including political discussion should be launched, for example of the transparent administration of revenues from natural resources

Public finance as key

Public finance constitutes an integral field of action for the promotion of constructive state-society relations. The example of taxation leaves no doubt: efficient tax collection can enlarge the government's scope for action and thus enable it to better meet its citizens' expectations. At the same time it can serve to tighten citizens' political ties with the state, as in return for their tax payments they expect provision of services and accountability. Transparent budget management and administration are therefore of major public interest. The government's democratic and financial accountability to its citizens both enhances its legitimacy and promotes good governance.

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Capacity Development (CD) is vital for sustainable state development in the sense of promoting constructive relations between state and society. Purposeful CD can provide a partner government with the support it needs in order to fulfil its key functions. It can also become possible for state and society players to engage in a dialogue over public issues, such as budget management and public investment. CD is vital especially in fragile situations in which the state lacks these capacities. Financial modalities such as budget support in particular involve high political and fiduciary risks in the countries concerned, in addition to which their capacity for absorption is limited.

More on the topic:



The U4 Anti-Corruption Resource Centre devotes much of its attention to the issue of corruption in fragile states:

[Corruption in fragile states](#)

Public Finance Reform

Steering of public funds in post-conflict situations

In its collaboration with countries in post-conflict phases the international community is operating in a highly complex political environment. Such countries are regarded as unstable, as their institutions are weak or have collapsed and they are no longer able to fulfil key state functions such as the provision of public goods. The legitimacy of the state has been severely undermined by its limited capacities and the preceding violent conflict. At the same time **substantial financial resources** are usually mobilised for these countries once a peace agreement has been signed.

Problems such as information deficits, unclear contact partners and a pressing need for action for humanitarian reasons are only a few of the challenges to which international collaboration must find answers. For this reason it has two prime objectives. Firstly, the current concrete situation must be mastered by providing emergency aid and undertaking peacekeeping measures. The second objective is to reconstruct legitimate public institutions.

Challenges to the budget process

Especially the capability of state institutions in fragile states to coordinate a high external inflow of capital is reduced. Crucial principles for a functioning and transparent budgetary system can be followed to a limited degree only. The high volatility and even more often, the allocation of funds at short notice complicate the recording of available revenues and expenditure. In addition, the preparation of a mid-term expenditure framework is made more difficult, since post-conflict states have to react fast and flexible to

changing conditions. A significant part of the allocated means is spent 'off-budget' for immediate aid and is thus not covered by the usual budget process. In the long term this procedure can give rise to a duplication of structures that undermines state institutions whose legitimacy has already been weakened and invalidates the democratic rules governing the budget circulation.

Avoiding duplicate structures

It is therefore vital for donors and their partners to reach an agreement on the timing of the transition from stabilisation and the initiation of necessary functions in progressing towards the development of legitimate statehood. In a further step the institutional, administrative and processual preconditions must be satisfied that are necessary in order to establish (or restore) the efficiency of core elements of the budget process. At the same time, in a rapidly changing and only partly comprehensible environment instruments must be established within the budget system to ensure that, if necessary, funds can be disbursed or reallocated promptly. Ideally, donors will engage in constant consultation within the context, will coordinate their actions with each other and from the very beginning draw up plans for an exit strategy.

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In July 2009 the **Afghan Ministry of Finance** evaluated current donor engagement and thereby identified budget-policy risk factors that are typical in post-conflict phases. Even today up to 80% of the donor funds provided are not disbursed through national structures. With the exception of military expenditures, 20% of these funds are allocated in such a way that at no time is the national government informed thereof. The report regrets that no adequate capacity development measures followed the initial emergency support that had to be provided by institutions other than Afghan institutions, which themselves lacked the necessary capacities.

[Study on donor engagement in Afghanistan](#)



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Public Finance Reform

Domestic resource mobilization in fragile states: The case of Pakistan

Reforms designed to mobilise domestic revenues in countries with fragile statehood are vital for the state development process. The direct strengthening of the state's fiscal basis enables it to fulfil its core functions – providing public goods and services to its citizens (fiscal objective). Moreover, supporting a legitimate, transparent and efficient system of public revenues contributes to the establishment of a trustful state-society relationship (governance objective).

The case of Pakistan

The constant potential for violence and conflict in Pakistan has substantially lowered its capacity to operate in central fields of public good provision. In particular, it is Pakistan's **low self-financing capacity** that severely constrains its ability to act as an efficient and reliable state. Whereas the average tax/GDP-ratio in OECD countries is at 35%, Pakistan's tax ratio is only about 11%. As a result, central state functions like the provision of public security, protection of private property, education and health remain largely unfulfilled: Soon after regaining independence in 1947 universal primary education was declared a national development goal, which is still far from being accomplished.

From a governance perspective the *fiscal social contract* particularly with respect to taxation has been permanently undermined and widespread corruption within state bodies has created a relationship of profound mistrust between citizens and tax authorities. Brief use of the army to collect

taxes and the associated *compliance by fear* proved to be just as detrimental to Pakistan's tax culture. As a result, as far as is possible citizens and business enterprises endeavour to circumvent the tax system and tax authorities, which is reflected in generally recognised and tolerated **tax evasion strategies** and the shift of economic activities towards the **informal sector**. Furthermore, tax exemptions as a result of lobbying activities have not only reduced the tax base, but also undermined citizens' trust in a strong state committed to overall welfare.

The continued illiquidity of the Pakistan budget reached a peak in 2008: in order to remain solvent Pakistan was obliged to turn to the IMF for financial support, which was provided only on strict conditions. One such condition was the implementation of the hitherto faltering **sales tax reform** by the end of the current fiscal year (30.06.2010). However, the political will to implement such tax reforms has been largely undermined by **protests from various interest groups** in parliament. Moreover, the scope for action is further constrained by lobby groups *outside* parliament. For example the threat of strike from the textile sector in reaction to the proposed sales tax reform. In the past, both factors have resulted in the failure of implementing reforms.

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Currently the **GTZ Public Finance, Administrative Reform and Decentralisation Project** is elaborating strategies for the mobilisation of domestic revenues in countries with fragile statehood. For this purpose various country studies were commissioned (e.g. Afghanistan, DR Congo, Madagascar, Nepal, Zimbabwe) to specify possible reform options. Furthermore, the issue will be discussed in a workshop, "Taxation in fragile states", at the **Public Policy Conference** in Berlin on June 17th and 18th.



In 2008 the IMF approved a stabilization loan of USD7.6bn for **Pakistan** to meet its foreign debt obligations. One pre-condition of this agreement was that Pakistan had to undertake major reforms of the tax system to enhance domestic revenues.

Public Finance Reform

Natural resources and development in West Africa's fragile states

Diamonds, iron ore, tropical woods and oil – given the fragile statehood of countries where civil war has raged and the high expectations of their citizens, the production of natural resources is a hazardous undertaking. For this reason the project “**Regional resource governance in West Africa's fragile states**” has been under way in partner countries Liberia und Sierra Leone since 2009. Guinea und Côte d'Ivoire are expected to join in the near future.

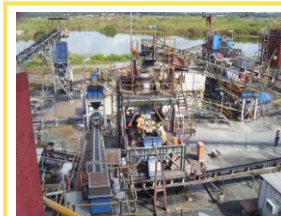
The starting point for the GTZ approach is the point in the fragile context at which political and economic incentive structures must be brought into accord with development goals. Organisational reforms can, for example, improve operational procedures within the administration and at the same time establish a foundation for transparency and accountability. Here the Extractive Industries Transparency Initiative (EITI) provides valuable stimuli for institutional reforms. Its aim is to disclose payment flows in the commodity sector. In comparison with other African countries Liberia has shown political will in this respect: all extractive contracts in the mining and forestry sectors must be approved by parliament and are therefore open to public debate. Liberia is the first and only African country to have satisfied the EITI implementation criteria since October 2009. Sierra Leone expects to do so in September.

In order to promote the exchange of regional experience, the GTZ provides support for cross-border EITI peer learning. The legal pre-conditions for achieving the project's goals (transparency, compensating payments to communities affected by the exploitation of resources, local development plans) have already been satisfied in both countries. Besides advising on

the political and legal anchoring of the **Natural Resource Governance Approach** the GTZ above provides support in its implementation, for in both post-conflict countries there is still a lack of capacities. West African countries are currently in no position to call on comprehensive quantitative analyses of the mining sector and on this basis to formulate their strategies and perform their political steering functions. Only in this way, however, will it be possible in the long term to enhance state control over the country's mining activities and to use its resource potential in the interest of its citizens. In this case effects could be expected on other **state-building** elements, such as the strengthening of local administration or improvements in the quality of public services at a local level.

All in all, mining investors in Liberia und Sierra Leone can be regarded as decisive drivers of change. Investors usually have a long-term investment horizon and therefore have a vested interest in sustained stable relations. Both citizens and NGOs make a vital contribution to enhancing the use of existing revenues (budget transparency, better management of expenditures). In accordance with the human rights approach partner countries are advised thereby on how to act in the best interest of their target groups. This means that in decision-making consideration must always be given to issues of human rights. This helps partners to establish development policy priorities in a fragile environment. The project supports Germany's political dialogue and contributes to the donors' political coherence by means of agreement with the World Bank, the UN and the EU.

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Kimberlite diamond mining by Koidu Holdings SA in **Sierra Leone**. The largest mining investor in the country offers good prospects for development approaches, but is located in a region plagued by civil war. Engagement by private enterprise highlights the effects of weak statehood. The triangle of interests between investor, government/local administration and local population in the mining area must be carefully balanced. Capacity development is necessary on all three sides if commodity production and development are to be complementary in the long run. With its long experience of programs in fragile contexts German development co-operation is highly valued as an “honest broker”.



Public Finance Reform

News from partner countries

Asia: Regional seminar „Human Resource Management in Supreme Audit Institutions“

In the discussion of possible approaches to the enhancement of governance attention has been focused increasingly on supreme audit institutions (SAIs). They have a vital role to play, in particular with regard to developing countries' autonomy, as they contribute significantly to the strengthening of national public financial management (PFM) systems. SAIs act here not only by auditing public expenditures, but in an advisory capacity they can also provide stimuli for reforms and prevent mismanagement.

However, **supreme audit institutions are only as good as their staff**. This was the essential message delivered by a regional seminar held by the Office of the Auditor General of Thailand (OAG) and the GTZ project EUROSAI – Co-operation with the German Federal Court of Audit (BRH) from March 29th to 31st in Bangkok. The seminar was opened by the Auditor General of Thailand, Khunying Jaruvan Maintaka, Stefan Duppel (German embassy) and Barbara Dutzler and brought together participants from **Cambodia, Indonesia, the Philippines, Thailand and Vietnam**.

Participants were supported by experts from the **German Federal Court of Audit**, the **Swedish Rikskrevisionen** and the **General Secretariat of the ASOSAI** (Asian Organisation of Supreme Audit Institutions). They suggested improvements with respect

to job specifications for auditors, train-

ing and further education, as well as incentive systems, engaged in a Q&A session and took part in a lively discussion. Issues of pay structure and competence profiles for prospective auditors were of particular interest. Gert Jönsson, vice-president of the Swedish Rikskrevisionen described the Swedish graduated pay system and provided some interesting insights into possible incentive systems. Participants were then given the opportunity to exchange experiences in specific fields and to discuss concrete issues in working groups, whereby it soon became clear that despite differing environments current challenges are everywhere very similar.

Regional exchange of experience and information to be taken further

The seminar was a great success and the regional exchange of experience and information that was initiated in the field of personnel management and development was regarded by participants as extremely constructive and positive.

Personnel management and development issues are of great interest and relevance for work in all SAIs, as well as in GTZ projects. There is, moreover, a widespread desire to deepen the exchange of information by means of a regional network. Enhanced engagement by the GTZ in collaboration with the ASOSAI could provide the necessary support. With this result the seminar has taken an important first step towards strengthening collaboration with Asian SAIs.

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Gert Jönsson (Rikskrevisionen), **Dr. Seongjun Kim** (ASOSAI), **Dr. Barbara Dutzler** (GTZ), **Stefan Duppel** (German embassy), **Khunying Jaruvan Maintaka** (OAG), **David Oberhuber** (GTZ), **Rutha Abraha** (GTZ), **Apichai Sunchindah** (GTZ) and **Dr. Lars Friege** (BRH) (from left to right) at the regional seminar in Bangkok.

24 participants from 5 South-East Asian SAIs exchanged opinions and experience with regard to personnel management and development.

Collaboration between the GTZ and the ASOSAI General Secretariat should be intensified in future in order to enhance the promotion of regional exchange.

Further information on ASOSAI is available under:

<http://www.asosai.org/>



Public Finance Reform

OECD recommends *better regulation* and reduction of bureaucracy

Interview with Rolf Alter and Leo Dirks¹

What are the advantages of a central unit for Better Regulation and how do other EU countries provide it with legitimacy?

Rolf Alter: The advantages of central units are the facilitation and encouragement of policy coherence for Better Regulation of policy implementation. These units can perform one or several key functions of regulatory quality oversight: oversight of the rule making process, assisting rule makers in their evidence-based analysis, challenging the quality of regulatory proposals and advocating for regulatory quality of better regulation.

EU countries have adopted different options in terms of institutional set up. The UK has a history of a well structured and powerful unit that has traditionally performed the first three functions. The Regulatory Reform Group in the Netherlands has had many of the functions of a core unit, located in the Ministry of Finance. However, functions remain disjointed in countries such as France, Italy or Denmark. The establishment of a National Regulatory Control Council as an independent watchdog in Germany mirrors trends in other EU Countries. Several EU countries are currently testing with a "networked" approach to institutional management of Better Regulation. However, this requires capacity for coordination and focus, which can often best be done at the center of government.

The OECD fosters culture change inside public administration, and speaks about quality controls, necessary incentive mechanisms and sanctions. This is also for the joint work on development an important issue: what could these mechanisms look like?

Rolf Alter: Implementing Better Regulation policies requires policy drivers, often external, that can help modify internal behaviours and bring about culture change among regulators. However, the implementation into governmental processes needs to reflect national traditions. In Westminster style governments, such as Australia or the UK, implementation is in a system that reflects strong conventions, where processes are not necessarily codified in specific rules. In France, there was a need to change the Constitution, and implement an Organic Law, to bring the necessary discipline for impact assessment within public administration. In the US, the Presidential Office for Information and Regulatory Affairs gives guidance to agencies on how to improve the quality of their impact assessment. In order to work effectively, these mechanisms need to be embedded in an administrative and regulatory culture. Culture change is required to pay attention to the compliance costs and regulatory burdens created by new regulations, which often are unintended consequences.

Continued on the next page

On 28 April, 2010 the [OECD Review of Better Regulation in Germany](#) was delivered to the German government in Berlin. This report is part of a joint project for **better regulation in 15 EU countries** initiated in 2008 in collaboration with the EU. With the establishment of the Standards Control Council within the **Office for the Elimination of Bureaucracy in the Federal Chancellery** substantial institutional progress has already been achieved towards improving the quality of legislation in Germany and lowering the costs imposed by bureaucracy on both companies and citizens. Attention was also drawn to the program „Elimination of Bureaucracy and better Regulation“. The OECD's main recommendations are that in the elaboration of new legislation consideration should be given to both the **expected impact of legislation** and **ex-post evaluation** of existing regulation. A more transparent consultation process can be established by increased use of **e-government** and **e-participation** instruments.

¹ The Interviews have had to be shortened due to the format of the newsletter. The full text is available upon request.

Public Finance Reform

E-Participation is an issue of great significance for the German government. What systems exist already and how high are their estimated costs?

Leo Dirks: Ministries already place much draft legislation on their websites in order to inform the public at an early stage. These can be accessed either directly or over the central internet pages www.bund.de and www.bundesregierung.de. On its internet page www.e-konsultation.de/ the Ministry of the Interior has already presented some procedures and invited consultation on, for example, secure online communication with respect to the Citizens' Portal Law. The Environment Ministry also invited consultation on sustainability over the internet page www.mitreden-u.de/ and the Ministry of Justice has conducted chats on the subject of copyright. The cost per system is roughly between €30,000 and €50,000 without internal staff.

In its e-government reforms is the German government benefiting from the experience of other EU countries?

Leo Dirks: The experience of our European neighbours confirms that e-government offers a great potential for the modernisation of administration and the reduction of bureaucracy. Nevertheless, given Germany's federal structure, e-government solutions that have proved successful in other countries cannot be adopted automatically on a one-to-one basis. However, we want to transfer positive experience: the „open data“ concept offers free access to public administration data, in order to provide enterprises with support in fulfilling their functions and at the same time to enhance their

competitiveness. A further project is the spatial data infrastructure (GDI-DE), whereby spatial data can be used by means of web technology by interactively connected organisations. 166 million data items can be freely accessed via the online database of the German Federal Statistical Office. However, we are still lagging some way behind the open-data portal in Great Britain.

The OECD has stressed the significance of ex-post evaluation of measures. How can we ensure that new findings are adopted?

Leo Dirks: The common code of procedure for federal ministries stipulates that in the case of draft legislation all possibilities of evaluation must be examined. Currently parliament is discussing the draft of a law that is designed to extend the powers of the National Standards Control Council: in future it will also be expected to examine drafts in order to verify whether existing possibilities of evaluation have been given due consideration. Even when a draft has become law, changed circumstances may, if necessary, call for changes in the law. It is conceivable that the National Standards Control Council might impose a combination of evaluation and limitations on those responsible for drafting the law. Timely evaluation will help decide whether the law is still necessary or whether something needs to be changed.

*The interviews with Rolf Alter and Leo Dirks were conducted by Dr. Stefanie Harter in May 2010
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Leo Dirks has been head of the Department for the Reduction of Bureaucracy in the German Chancellery since 2007. His department supports the government co-ordinator for the reduction of bureaucracy and better regulation. The federal government aims to lower significantly the costs imposed by bureaucracy on business enterprises, citizens and administrations. The National Standards Control Council supports the government in lowering existing costs and avoiding new costs of bureaucracy in fulfilling information duties. For more:

[Bürokratieabbau](#)

BürokratieAbbau
Zeit für das Wesentliche

Public Finance Reform

Public Finance issues

Equity in taxation

This year's UN summit on the Millennium Development Goals (MDGs) will bring up the question of how international development co-operation can enhance its contribution to poverty alleviation. The first successful results of the undertaken efforts are now becoming apparent. Above all, many Latin American and Asian countries are well on track to achieve MDG 1, namely halving absolute poverty. However, the developing countries have been less successful in reducing relative income inequalities. Examinations of Gini coefficients show that in recent years inequalities in income distribution have increased in many countries, despite the reduction of absolute poverty. Empirical studies have shown that unequal income distribution constrains growth. Additionally, income inequalities bear the risk of social tensions and may well result in a destabilisation of societies. It is therefore necessary to face these developments with the appropriate instruments.

Inequalities in income distribution are on the increase

In the field of public finance the international development co-operation has in the past primarily supported partner countries in formulating a pro-poor budget. Additionally, the revenue side can contribute to reducing inequalities in income distribution by establishing an **equity-oriented tax system**. One possible instrument is a reduction of the value added tax (VAT) rate on basic foodstuffs, or their complete exemption from value added tax.

Another possible tax measure is, a more comprehensive use of progressive income taxation, which aims to implement a tax burden that is oriented at the taxpayers ability to pay and therefore might be regarded as more equitable. In the same way, the abolition of tax exemptions and the removal of tax loopholes, which are primarily of benefit to higher income groups, can also contribute to a more equitable distribution of the tax burden.

Taxation and equity in Latin America

These issues are also discussed in a study on equitable taxation carried out by the UN Economic Commission for Latin America and the Caribbean (CEPAL) in cooperation with GTZ, which will be published soon. Particularly in Latin America, income distribution is extremely unequal and income taxation has always played a minor role in the region's tax systems. Revenues are predominately generated by indirect taxation, which means that tax systems are all too often regressive. Consequently poorer households bear a tax burden that is relatively higher than that of wealthier income groups. Hardly any Latin American tax system has responded to demands for more equitable and redistributive taxation. As a consequence, the discussion of equity and fairness in tax systems is bound to become even more intensive.

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NACIONES UNIDAS



The current **GTZ program with CEPAL** (UN Economic Commission for Latin America and the Caribbean), „**Opportunities and sustainability in globalisation**“ provides support for Latin American governments in their efforts to implement more equitable tax systems, in particular through a stronger use of direct taxes. At the GTZ Public Policy Conference in Berlin on June 17th and 18th, the study on equitable taxation will be presented and discussed by a panel of experts. The main author, Juan Pablo Jiménez, will attend the conference. This discussion will be held on **June 17th between 14.00 and 15.30.**

For further information on CEPAL see:

<http://www.eclac.org/>

Public Finance Reform

A green, equitable system of taxation to combat climate problems and public debt

The federal government has undertaken to reduce the public deficit and to limit new debt. Against the background of the current financial and economic crisis this will be no mean achievement. This issue was therefore chosen by the Forum for Ecological Market Economy (Forum Ökologische Marktwirtschaft - FÖS) as the main topic for discussion at its annual conference in Berlin on April 23rd. Discussion by representatives from the finance, economic and environment ministries, as well as from civil society, science and parliament focused on how, for example, the levying of environmental taxes and the gradual elimination of environmentally harmful subsidies could contribute not only to achieving climate goals but also to enhancing public revenues. This question was examined in greater depth at two workshops at which discussion centred on the taxation of company and official cars and a financial transaction tax.

Is a financial transaction tax internationally feasible?

At the workshop on a financial transaction tax representatives from the Federal Ministry for the Economy and Technology (BMWi), the German Institute for Economic Research (DIW) and the international Attac network, together with Prof. Dr. Paul Bernd Spahn discussed the financing potential of such a tax as well as that of the bank levy currently planned by the German federal government. Most critical comment centred primarily on the level of such a tax and its international feasibility. If the rate of taxation were low, the chances of its being accepted internationally were judged to be substantially higher. In this case, however, the tax would be of little use as a steering instrument and would

generate little revenue. As early as 2002 Prof. Spahn prepared a report for the Federal Ministry for Economic Cooperation (BMZ) which favoured a two-level model that would not only serve as a steering instrument but would also provide financing for development cooperation. (see: [BMZ Meldung innovative Finanzierung](#)).

Climate-friendly car fleets

The second workshop examined the issue of tax instruments that could be used to create incentives for a climate-friendlier composition of car fleets in Germany. 60% of all cars registered in Germany are company or official cars, most of which are fuel-guzzling, high-emission limousines. Two „adjustment screws“ were identified: on the employee’s side monetary advantage and on the employer’s side possibilities for depreciation. In both cases a grading scheme was suggested according to CO² emissions. As representative of the federal government the head of the tax department in the Federal Ministry of Finance (BMF) pointed to conflicting goals: a limitation of depreciation possibilities for company and official cars would violate the “objective net principle”, according to which all business expenditures are tax deductible. The special regulations introduced would stand in direct contradiction to the declared goal of simplifying taxation as laid down in the coalition agreement. There was general agreement among participants that the regulation of monetary advantage with respect to fuel costs would create particularly strong disincentives – only the remedy was left open.

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This year’s Annual Conference of the Forum for Ecological Market Economy (Forum Ökologische Marktwirtschaft - FÖS) was held in Berlin in April under the motto “A greener and more equitable system of taxation to combat climate problems and public debt” [FÖS Conference 2010](#)

The **introduction of a financial transaction tax** is currently a subject of much controversy in Germany. The degree to which experts disagree, especially over the question of the concrete form of the tax, was revealed at a **hearing in the financial committee** of the German Bundestag on Monday, May 5th. The experts’ opinions can be accessed under (only available in German): [Anhörung Finanztransaktionssteuer](#)

Public Finance Reform

The 12th EITI board meeting sets accent on commodity transparency

The anxiously awaited 12th EITI board meeting, at which decisions were taken with respect to the validation status of 19 candidate countries, was held in Berlin from April 15th to 16th. **Validation** is regarded as a litmus test for the Initiative and is used to monitor the EITI's two-year implementation. To date only Azerbaijan and Liberia have completed validation on schedule and thus qualified as „EITI compliant“. Another 17 countries were granted 6-to-12-month extensions of their deadlines. Mongolia was the only country classified as „close to compliant“. Sao Tomé e Príncipe and Equatorial Guinea on the other hand were excluded from the Initiative on grounds of their lack of political will. The Republic of Chad was accepted as new member.

The conclusion to be drawn from the board meeting in Berlin is that, despite binding rules, the EITI must display a degree of pragmatism in order to be able to react to the different capacities and general conditions prevailing in candidate countries. In recent months all the countries involved have made strenuous efforts to meet the validation pre-conditions. Here the **multi-stakeholder process** has proved to be invaluable as a **governance dialogue platform**.

The German representative on the board was Mrs. Dr. Ulla Mikota, Deputy Head of Department at the Federal Ministry for Economic Co-operation (BMZ). The GTZ, which has been advising the BMZ for many years on implementation of the Initiative and strategic positioning with respect to commodity transparency, participated at the Berlin meeting within the German delegation. The BMZ maintains a strong interest in increased support for EITI within the framework of bilateral cooperation and recruiting

new member countries for the Initiative as well as in closer examination of more wide-reaching issues of transparent commodity revenues. All players are aware that the **EITI is a key factor contributing to the sustained enhancement of good governance** and in particular to the promotion of efficient public finance systems.

At the federal government's evening reception on April 14th it was officially announced that, as the first DAX enterprise, the RWE energy group and the KfW banking group (the DEG will take over responsibility for implementation) have both agreed to join with immediate effect the international bodies supporting the EITI. The GTZ has been advising the BMZ since 2008 in its endeavours to persuade German companies to support the Initiative.

At the 12th EITI board meeting the GTZ was able to present its achievements in this area to a wide audience of experts and decision-makers from the worlds of politics, business and civil society. InWEnt's EITI Program is another significant and internationally esteemed contribution for implementing the EITI and strengthening the capacity of state and non-state stakeholders. Germany is in a very good position to help structure the next decisive phase of the EITI's overall development, whether this involves validation, institutionalizing the EITI processes, evaluation and assessment of effects, or wider-ranging issues of the reform agenda with respect to transparent revenues from commodities.

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Gudrun Kopp, Secretary of State at the BMZ (Federal Ministry of Economic Cooperation and Development) and **Peter Eigen** (r.), EITI Chairman, at the evening reception on April 15th.

The considerable attention focused on the EIT Initiative and the issue of transparent revenues from commodities as a result of the board meeting and declarations to the press by the BMZ and BMWi (Federal Ministry of Economics) facilitated a side event „The impact of transparency initiatives in the commodity sector“. Representatives from the World Bank and BMZ Evaluation Departments, the community of donors and civil society together discussed what effects can realistically be expected from the EITI and how they may be verified. The discussion of effects will be continued by a work group, in which the GTZ Public Finance Team is actively participating.

Public Finance Reform

Upcoming events

Public Policy Conference at the GTZ-Haus in Berlin June 17/18 2010

„State institutions between steering functions and diversity – Who determines whom?“ The Public Policy Conference will this year focus on the challenges facing state institutions in their endeavours to structure political and administrative processes in a very heterogeneous environment.

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66th Annual Conference of the International Institute of Public Finance (IIPF)

The GTZ will again support the Annual Conference of the International Institute of Public Finance (IIPF), which will be held in Uppsala, Sweden from **August 23rd to 26th 2010** (<http://www-conference.slu.se/IIPF2010/>) on the theme „**Tax Evasion, Tax Avoidance and Shadow Economy**“. A public policy award will be offered by the GTZ for the best contribution with regard to development co-operation.

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Preview next issue

Public procurement: between donor interest and development efficiency

A large part of government activity consists of the procurement of goods and services that are required for the fulfilment of public functions. This also means that a substantial proportion of public expenditures are accounted for by procurement processes, which are therefore an important field for action if government efficiency and legitimacy are to be enhanced. Ever since the Paris Declaration in 2005 and the Accra Agenda for Action in 2008 the reform of public procurement has been regarded as a top priority.

In reforms of public procurement technical and administrative aspects are often in the foreground. In its advisory capacity, however, the GTZ endeavours at the same time to include political aspects and societal control, in order to ensure a contribution to good governance and government legitimacy. As a result, issues relating to institutional frameworks and capacity development are in the foreground.

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New arrivals:

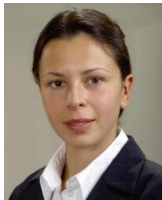


Dr. Hyun-Ju Koh has been working with the team since April 2010 as a project assistant in the field of public revenues. Previously she worked as research assistant in the Public Finance Department at the University of Munich and completed a doctoral thesis on tax competition and the taxation of industrial agglomerations.



Rebecca Kik is the newly appointed adviser for the BMZ in Bonn for the field of public finance, administrative reform and decentralisation. After her legal studies she joined the GTZ, where she worked as a junior assistant and consultant in Berlin and India before taking up a post as legal consultant in the Economic and Social Division of the FAO in Rome.

New arrival:



Yanina Oleksiyenko joined the Public Policy Team in June 2010 to work in the field of tax reforms, especially in collaboration with the IMF. Yanina Oleksiyenko studied international economic relations in Kyiv and economics in Konstanz. After her studies she worked for several years in the field of international corporate taxation.

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