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**Innovative Sources for Development Finance**  
- Global Public Economics
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Global Public Economics

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Introduction: Innovative Sources to Meet a Global Challenge

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3 Leaky Bucket or Positive Sum Game?
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Conclusion: Sober Analysis and Moral Commitment

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1 I am grateful to two anonymous reviewers for helpful comments on the first version of this paper, which have led me to make significant changes.
Abstract

This paper is concerned with issues of global public finance, and specifically the potential for new sources of funding for world development and poverty eradication. At this time of international tension, there is a need for new ideas to resolve longstanding world problems. A UN General Assembly resolution has called for “a rigorous analysis of the advantages, disadvantages and other implications of proposals for developing new and innovative sources of funding, both public and private, for dedication to social development and poverty eradication programmes”. Possible innovative sources include a tax on short-term capital and currency flows (“Tobin tax”), global environmental taxes (carbon-use tax or air transport tax), a global lottery, creation of new Special Drawing Rights, increased private donations for development, increased remittances from emigrants, and the International Finance Facility recently proposed by the UK Government.

The paper examines four major issues that arise if we are to devise realistic, feasible ways of achieving a substantial increase in the flow of resources for development and the framework that can be provided for the analysis. It seeks to bring to bear accumulated knowledge in the field of national public finance and more generally public economics.

The first question that has to be asked concerns the role of new sources. Some of the proponents of global taxation see it as an alternative to Official Development Assistance (ODA), but opponents see as an objection to new sources the idea that they could weaken the resolve of rich countries to increase ODA. Evaluations of the new ideas must therefore make clear whether they envisage a net addition to development resources or see new sources as an alternative to increased ODA.

The second question concerns the institutional architecture. Multilateral actions to introduce new sources of development resources involve inter-governmental co-operation. In today’s international climate, one has to ask how far this requires unanimity. Can new sources be introduced even if some significant rich countries opt out? The answer is likely to depend on the form of the new source, and this consideration may push some ideas to the top of the agenda. What are the institutional arrangements under which multilateral action takes place? Here one can learn from other arenas in which governments have learned to co-operate. The paper suggests for instance that the principle of subsidiarity, which has proved its value in the European Union, may allow a balance of national and global concerns.

The third question deals with the economics of transfers. Are these new sources examples of Arthur Okun’s “leaky bucket”, where the total available for development falls short of the total collected? Or can new taxes be devised that create a “double dividend”, where for example a global carbon tax both collects new revenue and reduces carbon emissions?

The introduction of new sources is a matter not only of economics but also of politics. The final question concerns the political economy of new sources. Is it best to link new revenue with another objective such as reducing currency speculation? Or does such a linking increase the size of the hostile coalition?
Introduction: Innovative Sources to Meet a Global Challenge

Two powerful and divergent forces grip the world at present. On the one hand, the effectiveness of international organisations has been called into question. There is in some countries a sense of frustration with multilateral co-operation and increasing resort to unilateral action. On the other hand, a global economy requires global institutions. International organisations are viewed by many as the key to the free movement of goods, services and capital. We have seen the adoption of ambitious development targets in the form of the Millennium Development Goals.

The tension between these two forces pervades discussion of resources for world development. On the one hand, there is talk of “donor fatigue”, and Official Development Assistance (ODA) has stagnated. Proposals for any form of global taxation meet immediate opposition from the US Congress. On the other hand, there is widespread recognition of the need for new flows to allow the Millennium Development Goals to be achieved. There are interesting proposals for new sources of revenue such as a global lottery or the International Finance Facility. Individual US billionaires are personally funding activities of the UN.

The direction taken at this juncture will depend largely on political events and political decisions. This paper is written in the hope that sober economic analysis will also contribute. Its aim is to set out a number of the key questions that arise in considering sources of new revenue for development finance. It does so on the assumption that international organisations will play a continuing, indeed growing, role, and that the agenda will be framed by the goals that have received international support, notably the Millennium Development Goals adopted by the UN General Assembly. Indeed, as a result of the Five Year Review of the World Summit for Social Development, the UN General Assembly adopted a resolution calling for “a
rigorous analysis of the advantages, disadvantages and other implications of proposals for developing new and innovative sources of funding, both public and private, for dedication to social development and poverty eradication programmes”. As the UN Secretary-General has observed, there has been a great deal of innovation in private financial markets, but less in the sphere of public finances. In order to carry out this analysis, the World Institute for Development Economics (WIDER) in Helsinki has been asked to carry out a study of “Innovative Sources of Development Finance” and I am co-ordinating a team preparing papers on this subject. Since the project is at an early stage, the present paper does not attempt to reach firm conclusions. Its aim is to raise questions and to provide a checklist of the issues that need to be addressed.

The paper is concerned with new sources of development funding in general. It is however useful to have some example in mind, and seven such proposals are set out in the Box. As this makes clear, possible new sources include both private and public sources of funding. We are not just concerned here with global taxes and official flows of development assistance. If, for instance, there are ways of increasing the remittances sent home by workers abroad, and these can be channelled into development purposes (such as the construction of schools), then this increases the flow of resources available for development. The same applies to charitable contributions by the citizens of rich countries. It should also be noted at the outset that I am concerned largely with the sources of funding, and rather than the use of funds. The two sides cannot of course be completely separated. It is easier to raise finance for specific purposes. We need to address the issue of earmarking. But the use of funds and their effectiveness is not the focus here.

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2 The authors are Tony Addison, Ernest Aryeetey, Tony Atkinson, Robin Boadway, Abdur Chowdhury, Ilene Grabel, George Mavrotas, John Micklewright, James Mirrlees, Machiko Nissanke, Agnar Sandmo, Andres Solimano, and Anna Wright.
One purpose of the present paper is to bring to bear on *global public finance* the accumulated knowledge in the field of national public finance, and more generally public economics. Although public economics has had an international dimension, and there has been a close link between public economics and development planning (the opening sentences of the article on optimum taxation by Diamond and Mirrlees 1971 refer to planning and investment criteria), there has been less impact on global development. As was observed a decade ago by Mendez, “a critical element lacking in the fields of finance and international relations is a theory and system of international public finance” (1992, page 11). The paper examines the contribution of the classical theories of incidence and excess burden; it asks how far one can learn from experience at a national level with optimal tax design. In line with recent developments in public finance, we need to consider the political economy of world resource flows, and the relation between fiscal and non-fiscal sources of funding.

This approach leads one to ask a number of questions. Those considered here are set out in the titles of Sections 1-4. The aim is not to provide definitive answers, but to clarify the questions being asked and to suggest possible answers that are not immediately apparent. To illustrate the issues, I refer at different points to the seven schemes listed in the Box. These schemes differ considerably. They include actions close to existing ODA (the International Finance Facility), and sovereign actions of governments (SDR allocation); they include measures to increase the benefits in terms of development funding from flows of private funds (remittances and charitable contributions); they include totally new departures such as global taxation and a global lottery. There is of course a risk that by considering together such disparate measures we may be confounding the issues. The different instruments raise different concerns. However, one of the key lessons of modern public economics is that it is
often valuable – indeed necessary - to consider within a common framework different forms of government policy.

1 What is the Role of New Sources?

It is widely recognised that we need to develop new and innovative sources of funding, both public and private, for dedication to social development and global poverty eradication. The present level of ODA is not sufficient to achieve the Millennium Development Goals. The Zedillo Report concluded, “the inescapable bottom line is that much more funding is needed for official development assistance” (United Nations 2001, page 10). “Meeting the International Development Goals alone would require almost double the current ODA total of more than $50 billion per year” (United Nations 2001, page 16). The UK Government (HM Treasury and Department for International Development 2003, para 1.11) estimate that to achieve primary schooling for all needs some $10 billion more each year, that to reduce infant and maternal mortality requires an extra $12 billion a year, and that halving world poverty requires an investment of up to $20 billion a year. The most straightforward resolution is to increase ODA: the UK Government referring to a doubling to $100 billion a year as part of its proposed new International Finance Facility. In this respect, donor countries at the Monterrey Summit made useful progress. However, the announced increases, such as that by the European Union, still fall well short of the amounts just mentioned.

The gap between current ODA and the amounts required to meet the Millennium Development Goals is one of the motivations for looking at innovative sources of development funding. Moreover, the research to date suggests that new
sources could raise sums to fill the gap. The conclusions of Clunies-Ross (2003) may be summarised as follows (figures for all annual amounts, rounded):

- Arms-trade taxes: modest revenue-earner $5 billion;
- Tax on international air transport: revenue less than $20 billion;
- Carbon tax: $60 billion if levied on high-income countries;
- Tobin tax at rate 0.02%: revenue $50 billion.

If these estimates are broadly correct, then there appear to be several ways in which a sum could be raised equal or exceeding existing ODA.

The first question we need to address is the relation between new sources of development finance and an expansion of ODA. Are these to be seen as alternatives? Many proponents of new sources view them as a way achieving an increased flow of development resources at a time when increased ODA seems unlikely to materialise. Global taxation is an alternative to trying to persuade rich counties to take seriously their unfulfilled pledge to meet the UN target of giving aid equal to 0.7% of GNP. Others see this as a reason for opposing the exploration of new sources: Tobin taxes or other new schemes would weaken the resolve of rich countries to meet the UN ODA target.

Or are the new sources a net addition to the total of development resources? This is clearly a different proposition. One of the key lessons from public finance is that the incidence of taxation depends on what else is being varied at the same time. As Musgrave set out in his classic *Theory of Public Finance* (1959), one possibility is “tax/expenditure incidence”, where revenue is increased and spending goes up by the same amount: As illustrated in Figure 1, the introduction of new sources involves moving vertically. ODA remains unchanged and the benefit from the additional revenue is seen in the contribution to development goals. Alternatively, we could contrast the two sources. As indicated in Figure 1, we could move along a line
holding development-spending constant, while varying the sources of funding. In Musgrave’s terminology, this is “differential tax incidence”: the differential implications of different means of securing a given flow of resources. For example, if a global lottery raises new revenue, then this reduces the need for increased ODA, and hence avoids an increase in domestic taxation. This is a different situation.

The distinction between two different types of incidence is drawn from the taxation literature, but similar questions arise with other proposals for new sources. In the case of the International Finance Facility, we have to ask how far the guarantee of funding by donor countries increases the net value of ODA. How much net additional resources are generated by the certainty of underwritten flows rather than annual allocations by donor governments?

**Conclusion**

When considering innovative sources, we need to be clear whether they are seen as a complement to expanding ODA or as an alternative. In the former situation, the case has to be made in terms of enhanced funding for development; in the latter situation, the case is being made that the innovative sources are a better way of funding a given development effort. Put bluntly, is the case for a carbon tax that it will fund the Millennium Development Goals or that it is a better way of funding those goals than ODA?

**2 What Architecture?**

In some cases new sources could be introduced by a country acting unilaterally: for example, a country could provide matching funds for private funding of development. But in most cases it is envisaged that there would be a multilateral
agreement. Indeed, in the case of the creation of new Special Drawing Rights, the constitution of the IMF requires a (super) majority of members to ratify the agreement before it can be put into effect. Where the source involves multilateral action, then two questions arise under the general heading of “architecture”. In discussing this, I am presupposing that the participating countries have agreed on the form and scale of the action to be undertaken. What we are considering is the shape of the necessary institutions.

First, does the success and effectiveness of the scheme depend on complete adhesion of all countries or all donor countries? Can we have a “flexible geometry”, where it is viable to go ahead with a subset of countries? The European Union for example has in the past faced situations where one Member State chose to “opt out” of collective decisions, and there has been flexibility in the resulting institutions. The likely answer to this question varies from one proposal to another. With the International Finance Facility, or the Global Lottery, failure of countries to participate means that the scale of the operation is reduced, but it is not undermined. With a carbon tax, any significant opting out may erode the tax base, as producers relocate, and expose participating countries to intense lobbying from domestic interests. In the present political climate, this may be a significant reason for choosing one route over another (I return to political economy arguments in Section 4).

The second question concerns the institutional arrangements under which multilateral action takes place. Where countries are acting in concert, then the organisational structure is important, as is illustrated in this section by reference to global taxation. A flow chart for national taxation is shown schematically in Figure 2. National governments determine the rates of taxation and the tax base. Individual taxpayers pay the taxes to the government, which both enforces payment and is in
Many taxes involve intermediary agents. The individual taxpayer, for example, pays the aircraft departure tax to the airline, which then accounts for the revenue to the government. Employers collect payroll taxes. Retailers or wholesalers collect excise taxes.

One evidently cannot apply exactly the same process to global taxation. We have both global institutions and national governments, and it is the latter which have to agree to the taxes being levied and which are accountable to their electorates. It could indeed be that the global tax is treated as simply a glorified domestic tax, with the revenue being forwarded by national governments to a global spending body (the heavy lines in Figure 3). But there are more possibilities, as shown by the dashed and dotted lines in Figure 3. If there were an international air transport tax determined at the global level, then the airline could transfer the money, not to the national government, but to a global tax authority, in which case the new source of finance would bring a new actor into play. This is shown by the dashed lines in Figure 3. Whether or not such a World Tax Authority is envisaged is one of the questions that have to be considered. (This may be different from an international tax organisation – see Tanzi 1999.) The feasibility of creating such a tax authority depends on the universe of taxpayers. In the case of airlines, there is already an international organisation (IATA) and the international air travel tax could be seen as part of a membership subscription. The formation of an international body conveys certain privileges and the tax could be seen as a rent for the use of global air space. A World Tax Authority could not deal with taxes paid by individual households, but one could envisage it operating a tax levied on multi-national corporations, which would have to be registered where their cross-border activity exceeded a certain amount (just as there is an exemption level for VAT registration in national systems). In the literature
on the corporation tax, one of the arguments for such a tax base is that the status of incorporation confers benefits on organisations adopting this legal form. It is normally agreed that this does not justify present levels of corporate income taxation, but a more modest rate of global corporation tax could be seen as a form of benefit taxation for engaging in cross-border economic activity.

Moving in the opposite direction from the introduction of a World Tax Authority is the case shown by dotted lines in Figure 3, where national governments retain not only control over the administration of the tax process but also discretion over the tax rates. In this case, participating governments would agree on their national tax liability but retain freedom to decide how the revenue is to be raised. This would in effect be applying the principle of subsidiarity adopted by the European Union. To be concrete, suppose that the participating governments agree that each country should pay a tax related to national carbon emissions. This determines the amount that each participating country has to pay, but the national government would be free to raise the revenue in whatever manner it thought fit. It might consider for example that a tax on air journeys was unfair on those living in remote rural areas, and choose for domestic reasons a different tax base. We would then have a two tier structure, with the national tax obligation requirement being agreed multilaterally, but the tax implementation being chosen locally.

Conclusions

Proposals for new forms of development funding raise important issues of institutional shape. In designing the architecture of global fiscal system, there is considerable scope for choice. As the references to “flexible geometry” and to
“subsidiarity” illustrate, we can learn usefully about the range of alternatives from the experience of supra-national groupings such as the European Union.

3 Leaky Bucket or Positive Sum?

$10 billion tax revenue does not mean that $10 billion is available for new development purposes. As Arthur Okun expressed it in his book *Equality and Efficiency* (1975), transfers are made using a leaky bucket. Put another way, the marginal cost of $1 extra public funds for development may be more than $1. On the other hand, there are arguments, usually put under the banner of “double dividend”, that there may be efficiency gains, so that the amount in the bucket is actually increased. And the literature on the marginal cost of public funds has shown that there are circumstances when the marginal cost of $1 is less than $1 (see Atkinson and Stern 1974, Fullerton 1991 and Sandmo 1998). In this section, I consider these two different perspectives.

Why are buckets leaky? The first source of leakage is the cost of administration. Currency transactors may pay $X billion but $(X-A) billion is the net revenue, where A is the cost of operating the tax collection and enforcement agencies. The second source of leakage is that a new revenue source may crowd out other sources of development funding. One of the lessons of public finance is that in calculating the change in revenue resulting from an increase in one tax, one has to take account of the possible impact on the revenue from other taxes. A good example is the international tourist tax. As Clunies-Ross (1999) points out, tourism is an important source of government revenue for a number of poor countries. To the extent that visiting tourists have less to spend after they have paid the tourist tax, these countries will be receiving less sales tax on the purchases made by tourists and would
have to be compensated before the tax yields net additional revenue. Similarly the introduction of a global lottery will affect national budgets. Part of the customer base will be drawn from existing national state lotteries, reducing their revenue. Part will be drawn from spending on private gambling subject to national taxes, so that fiscal revenue will fall.

But these are not the only potential leakages. Most taxes have an impact on the decisions of taxpayers apart from the pure effect of reducing their incomes. In the conventional public finance format, there is a deadweight loss, or excess burden associated with taxation. The currency transactions tax causes people to avoid activities that attract the tax. They will, for example, be inhibited from switching their investment portfolio away from domestic securities towards those denominated in other currencies. This has an efficiency cost, since they are not allocating their investments according to the return at the margin. Moreover, there is a presumption that the distortionary cost increases with the tax rate. The distortion is much more significant with a transactions tax rate of 0.1% than for one with a rate of 0.02%.

**A Double Dividend?**

The standard analysis of tax incidence is based on a world of perfectly competitive, perfectly functioning markets. In such a “first-best” context, government intervention – whatever its distributional advantages – has an efficiency cost. In the currency transactions tax example, if it were not for the tax the market would be efficient. The economies of the world are not however well characterised by perfectly competitive, perfectly functioning markets, and one of the major contributions of modern public economics has been to explore the implications of market failure. This has led to arguments that taxes may serve a corrective function: that the excess burden
may become a benefit. The classic example is a corrective tax on environmental external diseconomies. A tax on the consumption of goods that harm the environment has a positive allocational effect, switching spending away from polluting goods towards those causing less or no environmental damage. In these circumstances, switching behaviour is desirable. Moreover, if the revenue is used to reduce other taxes that have a negative allocational effect, we have a “double dividend” (for overviews, see Goulder, 1995, and Sandmo, 2000).

The double dividend can arise in the present case in two ways. If the new source is seen as an alternative to ODA, then it can both make its own efficiency contribution and allow a reduction in the taxes presently used to finance ODA. This is a good example of the differential incidence argument in operation. Taxing air transport will not only reduce the environmental damage of tourism but also allow the income tax to be reduced, so making staying in the office financially more attractive at the margin. Taxing carbon may allow payroll taxes to be reduced, leading to a fall in unemployment. There is an “employment dividend” as well as an “environmental dividend”. The second possibility is that the new source is a net addition to development resources. In this case, the double dividend consists of the reduced environmental damage and the benefit from achieving the development goals.

*Questioning the Double Dividend Argument*

The double dividend idea appeals to the imagination. However one has to ask why, if a new revenue source can generate a positive sum outcome, have national governments not already adopted such a policy? Why do OECD countries not operate lotteries to raise funds to finance their ODA? If a carbon use tax would reduce external diseconomies, why is this not already reflected in domestic taxes? If
governments could reduce unemployment by a switch in taxation, why have they not already done so? To this central question there are several responses. Here I consider two. First, it may be that the dividend is global rather than national. Secondly, it may be due to the political economy of taxation and government finance (Section 4).

National governments may not impose corrective taxes because the benefits accrue disproportionately outside their boundaries. The switch from general taxation to carbon use taxation may be positive sum globally but negative sum nationally. The revenue calculations of governments take account only of receipts and payments to the national treasury. The impact of spillovers from one state to another is a staple of fiscal federalism. Under certain circumstances, local governments may under-supply public goods that benefit people living outside their borders; and they may over-tax where taxpayers come from outside. There are fiscal externalities. In the present case, there is a possible undersupply of fiscal correction to external diseconomies because the costs spill over to others.

How is this potential argument for additional environmental taxation affected by the fiscal architecture? We are presupposing that the tax is indeed levied on individuals and firms in the form of a carbon levy (or other environmental tax base). Suppose however that we have subsidiarity, where the burden on national governments is determined by their carbon emissions but the national governments are free to decide how to raise the revenue. As noted above, they may for political or other reasons choose another tax base. It is still however the case that the government faces a financial incentive to reduce its emissions by other policies, such as auctioning emission permits or regulation.

Finally, global spillovers apply at the macro-economic as well as the micro-economic level. One of the arguments for the creation of SDRs is that they would
provide a macro-economic stimulus to the world economy. The macro-economic literature has extensively discussed the problem of international policy co-ordination failure. The existence of failure does not mean that policy co-ordination necessarily leads to efficiency gains, but it is possible that there may be a global positive sum outcome to a creation of additional liquidity. Whether this is so depends on the view taken of the working of the macro-economy. It also depends on the extent to which the transfers of SDR allocations from rich to poor countries lead the latter to increase spending. Clark and Polak (2002) argue that a regular allocation will not lead to a rise in spending, most countries adding to their reserves (which in itself has a development benefit), but this may not apply where there are substantial transfers of SDRs to poor countries.

Conclusion

The calculation of the leakage, or extra dividend, is a complex matter. There may be a double dividend, when we recognise departures of real-world economies from the assumptions of perfectly competitive, perfectly clearing markets with full information. The double dividend may be global in character, reflecting the pervasive problems of international co-ordination, but securing the dividend depends on policy design and on the working of the world economy.

4 What is the Political Economy of Development Finance?

One reason why, under the subsidiarity architecture described in Section 2, a national government may choose a different tax base is that it faces political opposition to a particular form of taxation. The fuel tax protests of 2000 in Europe provide a good illustration. All politicians are aware that the operation of a tax system
requires a degree of social acceptance. A democratically elected government may have a mandate at the ballot box to introduce a new tax, but if the population decide in sufficiently large numbers that the tax is not acceptable, then its collection becomes, at best, prohibitively expensive and, at worst, impossible. The attempt by Mrs Thatcher to apply the poll tax in the UK is an example of the limits to government action, and UK taxpayers are normally a passive group. In the US there was a major tax strike from 1930-1933 in Chicago, and there is the more recent history of Proposition 13 in California (see for example Kaufman and Rosen 1981). The fact that both of these reactions were localised reflects the fact that tax acceptability is a social and not a purely individual phenomenon. There is contagion of individual attitudes and people are influenced by social pressure. Social pressure can operate in both directions; it may support honesty in tax paying, not least where tax payments are public information, as in certain Scandinavian countries.

The behaviour of the state, and its interactions with citizens, has long been an important part of the subject matter of public economics. The title of the landmark book in the field of public choice theory by Buchanan and Tullock (1962) is The Calculus of Consent. Analysis of public policy has to take account of the process by which policy is made and administered. In this respect a false dichotomy has been created between public choice theory and welfare economics. The purpose of the literature on optimum taxation, for example, was to illuminate the structure of arguments that took place within a political context (see for example Atkinson, 1995). It sought to test those arguments and see whether the policies proposed in the political debate followed from the professed objectives of the protagonists.

Political economy considerations are important in the present context. To give an example, let us consider the proposition that the double dividend argument
strengthens the case for a tax on carbon use as a source of development funding. This is described by Clunies-Ross as the “two birds” test: “the collection of revenue is itself linked to the achievement of some widely desired end, such as a recognized global public good, so that two birds can be killed with one stone” (2003, page 5). This related to the classic model of “logrolling” where two politicians agree to support each other’s pet projects. However this assumes a particular distribution of benefits and losses from the projects, the former being concentrated and the latter diffuse (Drazen, 2000, page 330). In the present case the reverse may be true: the costs may be largely borne by a small interest group, and the benefits widely dispersed. To be more concrete, opening up two fronts also invites attack from both directions, particularly if the two objectives require taxes at very different levels. In several of the proposals considered here, the tax required for allocational reasons is likely to be considerably higher than that needed to add significantly to development funding. The Tobin tax required to raise US$50 billion is a much lower rate than that suggested in terms of stabilising exchange rates. (Taking this argument to the limit, we may note that a carbon tax that reduced emissions to zero would be an environmental success but a revenue failure.) The double dividend case risks attracting the hostility of those who oppose the exchange stabilising level of taxation, who would not necessarily oppose the much lower rate envisaged here. In deciding whether or not there are dangers in linking the two arguments, we need to consider the motives and power of different pressure groups and lobbies. As has been pointed out by Sandmo (2000, Chapter 7), we can apply to environmental taxes the analysis made by Grossman and Helpman (1994) of the influence of lobby groups on foreign trade policy.
What is required is a more nuanced political analysis of the coalitions likely to form in support or opposition of different proposals. Moreover, it is again clear that the counterfactual is important. The case may be easier to make if the unpopular corrective taxes are being used as a substitute for other taxes (differential incidence). Alternatively, people may accept the need to pay corrective taxes if the revenue is being used for an approved purpose. Political economy arguments may mean that it is not possible to separate raising revenue from the use to which it is put. The literature on development assistance has extensively discussed conditionality and its impact on aid effectiveness. These may take the form of tying aid to particular uses. A good example has been debt for nature swaps, where environmental NGOs like the Worldwide Fund for Nature have cancelled developing country debt in exchange for agreed conservation projects. It may take the form of tying aid to the adoption of particular policies. Much of the literature is sceptical about conditionality (see for example Kanbur, 2000), but this does not mean that conditionality cannot affect the willingness of taxpayers to pay taxes, or donors to make transfers. People may be more willing to pay a tax on international travel if they believe that the proceeds will be used to supply fresh water in regions without a safe supply. Here it is useful to separate the perceived effectiveness and the actual effectiveness of the funds. We have to ask whether earmarked taxes can be more acceptable on account of their professed objectives, or whether it is the actual effectiveness of the use that determines the degree of acceptance.
Conclusions

The political economy of different proposals is an important part of the story, requiring a nuanced political analysis of the likely coalitions of support and opposition, as well as a careful specification of the exact nature of the proposals.

Conclusions: Sober Analysis and Moral Commitment

To summarise the broad answers given to the four questions posed above:

• We need to specify clearly the role of new sources of finance, which may be additional to, or an alternative to, increased ODA; in the former situation, the case has to be made in terms of enhanced funding for development; in the latter situation, the case is being made that the innovative sources are a better way of funding a given development effort;

• In designing the architecture of global fiscal system, there is considerable scope for choice; we can learn usefully about the range of alternatives from the experience of supra-national groupings such as the European Union;

• The calculation of the leakage, or extra dividend, is a complex matter. When we recognise departures of real-world economies from the assumptions of perfectly competitive, perfectly clearing markets with full information, there may be a double dividend. The double dividend may be global in character, reflecting the pervasive problems of international co-ordination, but securing the dividend depends on policy design and on the working of the world economy;

• The political economy of different proposals is an important part of the story, requiring a nuanced political analysis of the likely coalitions of support and
opposition, as well as a careful specification of the exact nature of the proposals.

If we are to generate the additional flow of resources required to meet the Millennium Development Goals, then we need both sober analysis of the alternatives and moral commitment. This paper has sought to apply the lessons of public economics to these key issues of global public policy. It has been concerned with the grammar of argument, seeking to elucidate the key issues. Opposition often arises as much from misunderstanding as from genuine differences. Clear identification of the alternatives allows us to separate those that are promising from those that are unlikely to be acceptable. But no progress will be made without moral commitment. Here too the intellectual debate has an evident role to play. The flowering of literature on cosmopolitan justice in the fields of political theory and philosophy may well influence global public finance in the same way that utilitarianism influenced national public finance a century ago.
### Box: Possible Innovative Sources of Development Funding

<table>
<thead>
<tr>
<th>Source</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Currency Transactions Tax (“Tobin tax”)</td>
<td>Tax on short-term capital and currency flows at a uniform rate payable by all banks and foreign exchange dealers, collected on a national or a market basis, covering a range of transactions to be defined (spot, forward, future, swaps and other derivatives). See Haq, Kaul and Grunberg 1996, Spahn 1996, Mendez, 1997, Patomäki and Denys 2002</td>
</tr>
<tr>
<td>Global environmental taxes</td>
<td>Tax on commercial use of hydrocarbon fuels according to their carbon content; tax on international air passenger mileage and freight transport. See Pearce 1991, Poterba 1991 and Cooper 1998.</td>
</tr>
<tr>
<td>Global lottery</td>
<td>Global lottery operated through national state-operated and state-licensed lotteries, with proceeds shared between national participants and an independent foundation established in conjunction with UN. See Ahde, Pentikäinen and Seppänen 2002.</td>
</tr>
<tr>
<td>Creation of new Special Drawing Rights (SDRs)</td>
<td>New round of creation of SDRs as approved in 1997 but not yet ratified, with donor countries making their share available for development purposes. See Soros 2002.</td>
</tr>
<tr>
<td>Increased private donations for development</td>
<td>Measures to encourage private funding of development through UN agencies. Global funds. Corporate sponsorship. Internet.</td>
</tr>
<tr>
<td>International Finance Facility (IFF)</td>
<td>Long-term, but conditional, funding guaranteed to the poorest countries by the donor countries. Long-term pledges of a flow of annual payments to the IFF would leverage additional money from the international capital markets. See HM Treasury and Department for International Development. 2003.</td>
</tr>
<tr>
<td>Increased remittances from emigrants</td>
<td>Logistics (reducing cost of remittances), financial institutions (encouraging repatriation) and citizenship rather than residence basis for taxation. See Bhagwati and Hamada 1982, Mirrlees 1982, Bhagwati and Wilson 1989, and Solimano 2001</td>
</tr>
</tbody>
</table>
Figure 1  Net Addition to Development Resources or Alternative Source?

New Sources

Starting Point

Increased ODA

Differential Incidence

Equal Revenue

Tax/Spending incidence
Figure 2  Fiscal Architecture: National Taxation
Figure 3  Fiscal Architecture in Global Setting

Figure 2  Fiscal Architecture: NationalTaxation

World Tax Authority

Global development institution

Member governments agree national tax burden

National Government

National Tax Decision Process

Agent (e.g. airline)

Individual taxpayer

Tax collection process

Figure 3  Fiscal Architecture in Global Setting
Figure 2  Fiscal Architecture: National Taxation
References


