

Fiscal Space for Social Protection: Options to Expand Social Investments in 187 Countries

By Isabel Ortiz

It is often argued that social protection is not affordable or that government expenditure cuts are inevitable during adjustment periods. But there are alternatives, even in the poorest countries.

The paper "Fiscal Space for Social Protection: Options to Expand Social Investments in 187 Countries" (see <http://www.social-protection.org/gimi/gess/RessourcePDF.action?ressource.ressourceId=51537>), published by the ILO Social Protection Department, offers an array of options that can be explored to expand fiscal space and generate resources for social investments. These include: (i) re-allocating public expenditures; (ii) increasing tax revenues; (iii) expanding social security coverage and contributory revenues; (iv) lobbying for aid and transfers; (v) eliminating illicit financial flows; (vi) using fiscal and foreign exchange reserves; (vii) borrowing or restructuring existing debt and; (viii) adopting a more accommodative macroeconomic framework. To serve as a general advocacy resource, Annex 1 of the paper provides a summary of the latest fiscal space indicators for 187 countries.

A matter of fiscal choice: an overview of countries and their financing options

All of the financing options described are supported by policy statements of the United Nations and international financial institutions. Governments around the world have been applying them for decades, showing a wide variety of revenue choices. As this paper demonstrates, examples abound, did you know that:

- A large number of countries are increasing taxes for social investments – not only on consumption (generally regressive) but also on income, corporate profit, property, natural resource extraction. Bolivia, Mongolia and Zambia are financing universal pensions, child benefits and other schemes from taxes on mining and gas.
- The Thai government, during the first decade of the 21st century, reallocated substantial military expenditures towards universal health care.
- During the Arab spring, Egypt created an Economic Justice Unit in the Ministry of Finance to review expenditure priorities.
- Brazil used a financial transaction tax to expand social protection coverage.
- Argentina, Brazil, Tunisia, Uruguay, and many others

expanded social security coverage and contributory revenues.

- A number of low-income countries are receiving North-South and South-South transfers while other countries are fighting illicit financial flows by cracking down on tax evasion.
- Chile, Norway and Venezuela, among others, are using fiscal reserves to support social development.
- South Africa issued municipal bonds to finance basic services and urban infrastructure.
- More than 60 countries have successfully renegotiated debts, and more than 20 defaulted/repudiated debts, such as Ecuador, Iceland and Iraq, using savings from debt servicing for social programs.
- A significant number of developing countries have used deficit spending and more accommodative macroeconomic frameworks during the global recession to attend to pressing demands at a time of low growth, and to support socio-economic recovery.

Each country is unique, and all options should be carefully examined, including the potential risks and trade-offs associated with each opportunity, and considered in national social dialogue. Given the importance of public investments for human rights and inclusive development, it is imperative that governments explore all possible alternatives to expand fiscal space in order to promote national socio-economic development with jobs and social protection.

The intricacies of the fiscal space options

Each section of the paper gives a quick review of the issues, presents advantages and disadvantages, and examples of each fiscal space option. You can check different fiscal space indicators for your country in the Annex and identify the country specific essential questions *for transparent public debate and social dialogue*:

- **Re-allocating public expenditures:** this is the most orthodox option, which includes assessing on-going budget allocations through Public Expenditure Reviews (PERs), and other types of thematic budget analyses, replacing

- high-cost, low-impact investments with those with larger socio-economic impacts, eliminating spending inefficiencies and/or tackling corruption. *Can government expenditures be re-allocated to support social investments that empower vulnerable households? Are current military, infrastructure or commercial sector expenditures justified in light of existing poverty rates? Has a recent study been conducted to identify measures to enhance the efficiency of current investments, including steps to tackle and prevent corruption and the mismanagement of public funds?*
- ii. **Increasing tax revenues:** this is a main channel achieved by altering different types of tax rates - e.g. on consumption, corporate profits, financial activities, personal income, property, imports or exports, natural resource extraction, etc. - or by strengthening the efficiency of tax collection methods and overall compliance. *Have all tax codes been considered to maximise public revenue without jeopardising private investment? Are personal income and corporate tax rates designed to support equitable outcomes? What specific collection methods could be strengthened to improve overall revenue streams? Could minor tariff adjustments increase the availability of resources for social investments? Is natural resource extraction adequately taxed? Can tax policies better respond to "boom" and "bust" cycles? Have financial sector taxes been considered to support productive and social sector investments? Has there been any attempt to earmark an existing tax or introduce a new one to finance specific social investments - taxes on property, inheritances, tourism, tobacco, etc.?*
 - iii. **Expanding social security coverage and contributory revenues:** in existing social security systems, increasing coverage (and therefore collection of contributions) is a reliable way to finance social protection, freeing fiscal space for other social expenditures; social protection benefits linked to employment-based contributions also encourage formalisation of the informal economy. *Can contributions to social security be extended to more workers? Are current contribution rates adequate? Is there scope to introduce innovations like the Monotax to encourage the formalisation of workers in the informal sector?*
 - iv. **Lobbying for aid and transfers:** this requires either engaging with different donor governments or international organisations in order to ramp up North-South or South-South transfers. *Has there been any formal or informal attempt to lobby friendly governments for increased aid or transfers?*
 - v. **Eliminating illicit financial flows:** Given the vast amount of resources that illegally escape developing countries each year, estimated at ten times total aid received, policymakers should crack down on money laundering, bribery, tax evasion, trade mispricing and other financial crimes that are illegal and deprive governments of revenues needed for social and economic development. *What can be done to curb tax evasion, money laundering, bribery, trade mispricing and other financial crimes that are illegal and deprive governments of revenues needed for social and economic development?*
 - vi. **Using fiscal and central bank foreign exchange reserves:** this includes drawing down fiscal savings and other state revenues stored in special funds, such as sovereign wealth funds, and/or using excess foreign exchange reserves in the central bank for domestic and regional development. *Are there fiscal reserves, for example, sitting in sovereign wealth funds that could be invested in vulnerable households today? Are excess foreign exchange reserves being maximised and used to foster local and regional development?*
 - vii. **Borrowing or restructuring existing debt:** this involves active exploration of domestic and foreign borrowing options at low cost, including concessional, following a careful assessment of debt sustainability. For countries under high debt distress, restructuring existing debt may be possible and justifiable if the legitimacy of the debt is questionable and/or the opportunity cost in terms of worsening deprivations of vulnerable groups is high. *Have all debt options been thoroughly examined to ramp up social investments? What are the distributional impacts of financing government expenditures by additional borrowing? Have different maturity and repayment terms been discussed with creditors? Has a public audit been carried out to examine the legitimacy of existing debts?*
 - viii. **Adopting a more accommodating macroeconomic framework:** this entails allowing for higher budget deficit paths and higher levels of inflation without jeopardising macroeconomic stability. *Is the macroeconomic framework too constrictive for national development? If so, at what cost mac-*

roeconomic stability? Could increasing the fiscal deficit by a percentage point or two create resources that could support essential investments for the population? Are current inflation levels unduly restricting employment growth and socioeconomic development?

Examples of fiscal space strategies, selected countries

Strategy	Bo- livi a	Bot- swan a	Bra- zil	Costa Rica	Le- sot ho	Ice- lan d	Na- mib ia	South Africa	Thai land
Re-allocating public expenditures				X	X	X		X	X
Increasing tax revenues	X	X	X		X	X	X		X
Expanding social security contributions			X	X	X		X	X	X
Reducing debt/debt service	X	X	X	X	X	X		X	X
Curtailling illicit financial flows						X			
Increasing aid							X		
Tapping into fiscal reserves	X	X	X						
More accommodative macroeconomic framework	X		X						X

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Reference:

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The importance of social dialogue

National social dialogue is best to articulate optimal solutions in macroeconomic and fiscal policy, the need for job and income security and human rights. While in some countries, national development strategies and their financing sources have been shaped through social dialogue; in many other countries this has not been the case. Public policy decisions have often been taken behind closed doors, as technocratic solutions with limited or no consultation, resulting in reduced social investments, in lack of public ownership, adverse socio-economic impacts and, frequently, civil unrest.

Transparent national tripartite dialogue, with government, employers and workers as well as civil society, academics, UN agencies and others, is fundamental to generate political will to exploit all possible fiscal space options in a country, and adopt the optimal mix of public policies for inclusive growth and social justice.