

# Innovative financing methods for social protection

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## Question

*Review innovative financing methods for social protection around the world*

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## 1. Overview

Financing for social protection often comes from government funds. Any way of expanding fiscal space could therefore be useful with the political will for prioritisation (UNESCP, 2016). Egypt created an Economic Justice Unit in the Ministry of Finance to review expenditure priorities, and Costa Rica and Thailand shifted military spending to finance universal health services (Ortiz et al., 2015b).

Ortiz et al. (2015) offer options for government to increase social investment: reallocating public expenditures, increasing tax revenues, expanding social security coverage and contributory revenues, lobbying for aid and transfers, eliminating illicit financial flows, using fiscal and foreign exchange reserves, borrowing or restructuring existing debt and, adopting a more accommodative macroeconomic framework. The authors advise against VAT or consumption tax increases as they have a negative social impact unless targeted to luxury goods.

Taxes on items that create negative externalities such as beer, cigarettes or petroleum may be more politically acceptable if proceeds are spent improving social issues (Ortiz et al., 2015).

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There are benefits for public and personal health as consumption is discouraged. In the Philippines a tax on gaming corporations supports National Child Development Centers which provide integrated services for children from birth to 4 years old (Putcha et al., 2016).

Ortiz et al. (2015) recommend taxing financial sector transactions as it is highly progressive. Other advantages are that it is relatively easy to monitor as institutions already keep records and it allows cross-checks for fiscal control (ibid). Asher and Bali (2014) suggest looking at remittances as a source for social investment.

In Bolivia, oil and gas revenues received from the government were changed from 18 per cent to 50 per cent in 2006 (Ortiz et al., 2015). The revenue increase allowed expansion of social policies such as non-contributory pensions (UNDP, 2011) and cash transfers for school children. Civil society organisations carry out monitoring of company payments to the State and the management of related revenue at the national and subnational levels (Urban, 2016a). In Mongolia, excess revenues from the mining sector are used to fund pensions (UNESCAP, 2016). Governments using taxes from extractive industries must plan for price instability. UNRISD (2012) highlights the importance of building state capacity and fostering positive institutional change to harness mineral wealth for social policy.

Social contributions require formalisation of the labour market, particularly challenging for low-income countries (LICs) (Barrientos, 2011). For this to function countries will need to invest in collection mechanisms (Ortiz et al., 2015).

A civil society-led initiative in Pakistan, run by an organisation called the Citizen Foundation, builds and operates schools (UNESCAP, 2016). Parents contribute to the school fees based on household income.

Improving systems so that efficiency gains can be used to improve social spending should be considered. One example is better management of pension funds (Asher and Bali, 2014). Financial education and literacy is required to maximise the potential of pensions (Asher, 2015). Asher (2011) describes micropensions in India. These are long-term saving schemes for relatively low income, informal sector workers.

Social impact bonds (SIBs) are becoming popular in high-income countries (Beesabathuni, 2016). A private investor pays funds which the government repay if agreed outcomes are reached (The Rockefeller Foundation, 2017). There is one example of this in India to improve enrolment and learning outcomes for girls (Beesabathuni, 2016). An early example of this type of financing was in Peterborough, UK, where repeat criminal offending was reduced (Social Finance Limited, 2014). SIBs have been criticised for being complex (Dear et al., 2016).

Investment for companies with both a financial and social aim has been successful in Haiti where a production facility for nutrient supplements was set up (Beesabathuni, 2016). The Power of Nutrition sources funds from private and non-traditional sources which are then matched by donor funds (Beesabathuni, 2016). Funds are being used for primary healthcare and for nutrition in Sub-Saharan Africa and Asia.

Section 3 identified documents looking at the concept of innovative financing for development. Guarnaschelli et al. (2014) describe innovative financing instruments as reallocating risks from investors to institutions better positioned to bear the risk and, in the process, enable participation from mainstream investors. Liquidity is enhanced and volatility reduced. They propose three drivers of innovative financing: 1) increased use of established financial instruments, 2)

expansion into new markets through growth of replicable products, and 3) creation of new innovative financing products.

## 2. Taxation and financing for social protection

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

Ortiz, I., Cummins, M., and Karunanethy, K. (2015a). ILO.

<http://www.social-protection.org/gimi/gess/RessourcePDF.action?ressource.ressourceId=51537>

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. This working paper 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.

Examples in this paper:

- Costa Rica and Thailand reallocated military expenditures for universal health.
- Egypt created an Economic Justice Unit in the Ministry of Finance to review expenditure priorities.
- A large number of countries are increasing taxes for social investments – not only on consumption (generally regressive) but also on income, corporate profit, property and natural resource extraction.
- Brazil used a financial transaction tax to expand social protection coverage.
- Bolivia, Mongolia and Zambia are financing universal pensions, child benefits and other schemes from taxes on mining and gas.
- Ghana, Liberia and Maldives have introduced taxes on tourism.
- 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 re-negotiated debts, and more than 20 defaulted/repudiated debt, 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 socioeconomic recovery.

The paper does not recommend raising VAT or consumption taxes as this leads to a negative social impact unless a product that the wealthier population consume more of is targeted.

Another type of consumption tax that can be used to increase fiscal space is excise tax, which is collected on goods such as beer, cigarettes and petroleum whose consumption creates negative externalities (e.g. the cost of the good does not factor in the negative side effects to third parties or society that result from its consumption). The advantage of increasing so-called “sin” taxes is that they may be more politically acceptable, especially if the revenue is directed toward social expenditure, although their disadvantage is that by their nature they aim at reducing the underlying consumption. Based on current tax proceeds, the WHO<sup>1</sup> estimates that a 5-10 per cent increase in the tobacco tax rate could net up to US\$1.4 billion per annum in additional revenue in low-income countries and US\$5.0 billion in middle-income countries; raising tobacco taxes by 50 per cent could cover nearly half of public health expenditures in a number of developing countries. Given the public health spillovers and revenue potential associated with new or higher “sin” taxes, many governments appear to be considering this option in the current policy environment. According to IMF country reports this includes Antigua and Barbuda, Jamaica, Kyrgyz Republic, Liberia, Republic of Congo and Turkey, covering around 1.3 per cent of the world population.

Corporate taxes have largely been reduced to encourage entrepreneurial risk taking and generate new economic activity. However, the potential trade-off needs to be carefully balanced, to ensure that the short-term gains from increased business activity do not come at the expense of foregone essential investments for human and economic development.

Taxing financial sector transactions is a feasible option to fund social protection and a viable option to increase social spending.

Advantages:

- It is relatively easy to implement and monitor because it works within supervised banking institutions that use electronic transactions/records.
- It covers everyone, even those who evade payroll contributions.
- It is a fiscal control instrument that allows cross-checks to be made with information on financial transactions throughout the economy.
- It is highly progressive and allows resources to be channelled directly from the formal economy to those who need social protection.

The Contribuição “Provisória” por Movimentação Financeira (CPMF) tax was levied in Brazil from 1997 to 2007. The contribution took the form of deductions from accounts held by financial institutions. The maximum value of the CPMF quota reached 0.38 per cent of the value of financial transactions. For accounting purposes and because the CPMF was designed mainly to finance social protection expenditure, the mechanism was classified as a “social contribution.” During the period in which the tax was applied, 42 per cent of the revenue collected was used for the public unified health system, 21 per cent for social insurance, 21 per cent for Bolsa Família and 16 per cent for other social purposes. By 2007, total revenue from CPMF amounted to 1.4 per cent of GDP, enough to cover the total cost of Bolsa Família and other non-contributory social protection programs. Although pressures from the financial sector led to its rescinding in 2007, a financial transaction tax was re-instated in 2009 at much higher levels (6 per cent) in

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[https://www.internationalhealthpartnership.net/fileadmin/uploads/ihp/Documents/Results\\_\\_Evidence/HAE\\_\\_results\\_\\_lessons/WORKING%20GROUP%20%20REPORT%20-%20Raising%20and%20Channeling%20Funds.pdf](https://www.internationalhealthpartnership.net/fileadmin/uploads/ihp/Documents/Results__Evidence/HAE__results__lessons/WORKING%20GROUP%20%20REPORT%20-%20Raising%20and%20Channeling%20Funds.pdf)

order to help curb liquidity in international markets and fast capital inflows/outflows that disrupted Brazil's development. It was repealed once again in 2013, after leaving significant resources to the Brazilian government to implement social policies, a reason driving the ongoing calls from civil society to adopt financial transaction taxes as part of social justice.

In addition to altering corporate tax rates, governments can also increase fiscal space by taking concerted actions to minimize tax evasion and/or aggressive avoidance of taxes on the part of large companies.

Developing countries that rely on non-renewable natural resources as a main source of wealth should consider ways of distributing effectively and equitably the mineral rent to society to support social and economic development initiatives. There are also significant environmental and social externalities associated with natural resources, such as the impacts on local communities, which, if not adequately addressed, serve as a subsidy to extracting companies and further distort the true cost of development.

A government may raise revenues either by directly extracting the natural resources through a state-owned enterprise, joint-ventures or other forms of co-extraction, or by selling off the exploitation rights and taxing the profits, both of which can provide transitory revenues for social investments. Regarding the former, a number of countries have effectively managed their natural resources through public companies, including Botswana (diamonds), Brazil (oil), Indonesia (oil and gas) and Malaysia (forestry, tin, oil and gas).

Natural resources, including gold, tin, petroleum and gas, are the main pillar of Bolivia's wealth and key to the country's national development. As a result of orthodox neoliberal policies in the 1980s, the majority of production was privatized, often through foreign companies. In the process, royalty taxes were cut down to 18 per cent, which led to extremely high profits for producers (82 per cent) and very low returns to the Bolivian population. The widespread dissatisfaction with this situation led to an activist campaign named "Hydrocarbons are No Longer Ours." After violent repression of this movement during the so-called "Gas Wars," President Sánchez de Lozada resigned and a national referendum led to a new regulation on the distribution of hydrocarbon wealth. The previous share of 82 per cent of oil revenues for the producers and 18 per cent for the state was equalized at a 50-50 split (and a reversed 82-18 split for the largest gas field). Renegotiation of former contracts led to an increase in oil and gas income for the state from US\$558 million in 2004 to US\$1.53 billion in 2006. Such significant revenue increases allowed the government to expand/sustain social policies such as Renta Dignidad (Dignity Rent), a non-contributory pension to all Bolivians over 60 years old, or the Bono Juancito Pinto, a cash transfer for all children in public elementary schools (from first through eighth grade), which offsets the costs of transportation, books and uniforms to increase school attendance.

The government in Peru expanded taxes on the mining sector to invest in health and education. Mongolia is financing a universal rights-based child benefit from taxation on copper exports; when copper prices dropped with falling demand in 2009, Mongolia was advised by the international financial institutions to target its universal child benefit. Given the volatile nature of primary commodity prices, some governments have created "stabilization funds" based on windfall taxes. Instead of spending the revenue on social and other development programs, governments have accumulated such funds because they allow for smoothing income and expenditure. In many countries, however, the private sector takes the lead in exploiting natural resources. In these situations, the state is indirectly included in the rents since it receives a

portion via taxes. This can include: (i) production-based taxation (per unit or ad valorem royalties, sales taxes, export and import duties, VAT, payroll tax, stamp duty, etc.); (ii) profit-based taxation (corporate income tax, resource rent taxes, taxes on windfalls, profit tax on dividends, royalty based on profit, etc.); and (iii) environmental taxes to compensate for negative environmental externalities caused by the activities of mining companies.

Other taxes considered in this document are: property and inheritance tax; airline and hotel taxes, taxes on tourism; international transportation taxes; linking taxes to social programs; remittance taxes; carbon taxes; arms trade taxes; and a national lottery.

Generating funding through expanding coverage social contributions is by its nature associated with the extension of contributory social protection. Much of the scope for increasing social security contributions depend on the efforts of social security administrations and labour inspectorates to enforce the legal provisions and ensure compliance of employers and workers to register, on the one hand, and to pay fully their contribution dues, on the other hand. Investments into social security collection mechanisms are important. In countries like Brazil, Costa Rica and Uruguay, social contributions are closely associated with the introduction of innovations to encourage the formalisation of the labour market. The formalisation of employment and enterprises goes hand in hand with the extension of social security. This creates a virtuous cycle, as more companies go within formality, the collection of taxes and social contributions simultaneously are increased as well.

Monotax is a simplified tax collection/payment scheme for small contributors in Uruguay. The micro-entrepreneurs who join the scheme are automatically entitled to the benefits of the contributory social security system (except for unemployment protection). Monotax contributions are collected by the Uruguayan Social Security Institute (BPS), and the share corresponding to tax payments is transferred by the BPS to the fiscal authority. The remaining share is then used by the BPS to finance social security benefits for social insurance members affiliated through the scheme and their families. Monotax has proven to be an effective tool to formalise micro- and small enterprises, as well as to extend social security coverage to independent workers, especially women. Argentina, Brazil and Ecuador are developing schemes similar to Monotax.

### **Financing Social Protection**

UNESCAP. (2016).

<http://www.unescap.org/sites/default/files/Financing%20Social%20Protection.pdf>

Key points:

- The issue of finding fiscal space and prioritising is one of political will, rather than lack of resources.
- Contributory schemes: employers and employees contribute – challenge for LIC's is that only a small fraction work in the formal sector so coverage limited – this is for Asia-Pacific. Non-contributory social assistance schemes for those in the involuntary sector are rare. One option here therefore is to increase/promote formal sector work.
- The main source for social protection is tax, and of these income tax. Examples of countries which have developed tax-financed social protection programmes for children with specific nutritional, health and education objectives include Kyrgyzstan, the Philippines, and Sri Lanka. Examples of countries providing tax-financed non-contributory pensions are Nepal, Maldives, Samoa, and Vietnam.

- Earmarking tobacco taxes to correct negative externality of second-hand smoke and reduce consumption whilst also raising revenue for health and health promotion is another option. For example, in 1982 Korea introduced tax on alcohol, tobacco, interest and dividend income, as well as banking and insurance industry which was earmarked for education purposes. 5 years later the tax accounted for 15% of the education budget.
- However, weak tax admin and collection constrain the ability of countries in the region to finance social protection.
- In the absence of new fiscal space for expanding social protection, policy makers can consider reprioritising public spending in favour of social protection eg. removing fuel subsidies.

Innovative ways of funding:

- Dedicated funds from extractive industries. Mongolia supports pensions through the Human Development Fund by collecting excess revenues from mining sector. Also healthcare housing and educational benefits.
- Private or civil society-led initiatives. For example, in Pakistan the Citizens Foundation builds and operates schools. Parents contribute to the school fees based on household income whilst corporate and philanthropic donations cover the rest. In India, the All India Disaster Mitigation Institute of Development Studies developed the micro-insurance mechanism Afat Vimo which is a collaboration between poor entrepreneurs, commercial and public insurance companies.
- Cross-subsidisation. Uruguay combined contributory social insurance and tax-based programme into a “monotax” which bridges the gap between those employed in the formal and informal sectors.

### **Financing Social Protection in Developing Asia: Issues and Options**

Asher, M. G., & Bali, A. S. (2014). *Journal of Southeast Asian Economies*. 31(1), 68–86.

<https://muse.jhu.edu/article/545553>

The paper offers 3 options generating fiscal space:

1) Realising Efficiency Gains in Managing Provident and Pension Fund Organisations. The operating expenditure as share of assets is relatively high in Thailand and in the Philippines. This may reflect the extent to which the pension system design permits the accumulation of member balances and the time since the scheme has been in operation. Thus, a possible reason for a higher ratio in the Philippines is the partial funding nature of its social security scheme, which is a defined benefit (DB) type. Under such schemes, benefits are defined but the contributions required to pay for them are not. Member contributions and investment income during the year are used to pay for the benefits of the current retirees. Only the current demographic structure of the Philippines, i.e. the smaller number of retirees in relation to contributing members, has led to the accumulation of funds. Thus, as the population of the Philippines ages, and the proportion of retirees relative to the working population increases, its total assets will decline or at least exhibit less rapid growth.

In contrast, the schemes of Malaysia and India are of a defined contribution (DC) nature, in which members are required to contribute in a defined manner but benefits are left undefined. As a result, contributions of members plus investment returns (sans pre-retirement withdrawals) accumulate with the provident fund organization, and are returned to members only at the point

of retirement. Thus, DC funds can potentially be higher than those under a DB scheme, which utilizes current contributions of workers plus investment incomes to pay for pensions.

Efforts to bring down the high ratio in the Philippines are currently underway, for example, through the greater use of technology to improve coverage and reduce processing time. The SSSNet by the Social Security System (SSS) is an example of how IT systems can be used for better coverage of workers, including overseas workers. Eight hundred employers with over 420,000 employees are registered with SSSNet. Payments remitted through SSSNet make up 11 per cent of the SSS's monthly bank collections. Prior to this, it would on average take between three and six months to post monthly contributions to the individual accounts of members. This process now takes less than three days. This, in turn, has resulted in shorter processing times for benefits and loan applications.

2) Innovations in Design, and Enhanced Policy Coordination and Coherence. Social protection the two main components are healthcare and pensions, both of which can also be viewed as a bundle of goods and services that the elderly will need to consume. Better coordination between the two programmes could facilitate social security for migrant workers, strengthen social safety nets and positively impact economic growth.

3) Generating Budgetary Resources from Conventional and Unconventional Sources. Enhancing competence to generate resources from unconventional sources such as utilizing state assets (land, property rights such as air-space, oil and mining resources and carbon trading, among others) efficiently could provide avenues for generating additional resources. It has been estimated that the OECD governments have saleable land and buildings worth up to US\$9 trillion, equivalent to nearly a fifth of their combined gross debt. A similar situation exists in most Asian countries. The Indian Railways, for example, have been attempting to utilize their land assets to generate funds for railway modernization. To the extent such efforts are successful they could release resources for other government programmes, including financing the social sector. However, generating such revenue also requires enhancing capacity to undertake public-private partnerships successfully.

Conventional tax reforms, and improving compliance levels and efficiency, could generate significant additional resources. In Europe and the United States, as well as in Asia, corporate tax reforms, particularly those provisions designed to protect the tax base, have become a priority. In 2012, the OECD created a forum on Value Added Tax (VAT) to help counter aggressive tax planning of VAT by businesses. This suggests a need to invest in modernizing tax administration and tax laws. While such modernization cannot be undertaken quickly, in the medium-term it represents a more efficient and equitable way of generating additional revenue instead of merely increasing tax rates.

Five types of fiscal resources have been proposed to finance growth. These resources are classified as debt, other capital receipts, foreign aid and other unilateral grants, non-tax revenue including resource rents, seigniorage, and taxes. There are three broad findings that are relevant to the discussion in the paper. First, DA economies need to pay greater attention to non-tax revenue and "other taxes", including property taxes and corrective taxes, in order to expand their relatively low fiscal resource bases. Second, there is considerable diversity in the fiscal systems amongst DA economies. This diversity is represented in the number of taxes, the size of sub-national government, relative contributions of various taxes as well as sub-national governments' shares in the total revenue and spending, tax compliance and leakages from tax system. Third,

there is volatility in various sources of revenue available to the government, with taxes being the least volatile, and non-tax revenue being twice as volatile.

As indicated in section II, remittances play a significant role in generating household incomes in many countries in DA. In 2013, these flows are projected to be three times the Official Development Assistance (ODA). More productive use of remittances could help improve local economies, provide savings for productive investments and contribute to productive consumption. These, in turn, could potentially increase the core rate of economic growth and thereby provide funding for social protection programmes.

Sovereign Wealth Funds (SWFs) and foreign exchange reserves could also play financing roles. Higher return SWFs have been set up to manage the excess of current receipts over expenditure arising from energy resources, trade surpluses, and other sources, and between generations. These represent another avenue for funding old age needs. For example in Asia China, Malaysia, South Korea and Singapore have been adept at using SWFs to fund future expenditure needs, including those of the aged.

It has been estimated that even if a conservative definition of excess reserves (defined as the difference between the reserves and the 12.5 per cent of M2 or broad money supply) is used, select Asian countries could generate additional investment income equivalent to: 1.48 per cent (China); 1.19 per cent (Malaysia); 0.7 per cent (Korea); and 0.6 per cent (India) of GDP (Park 2008).

Financial product and service delivery innovations each reduce transaction costs of pension schemes and could contribute to better retirement income security. Thus encouraging phased or programme withdrawal of payouts in defined contribution schemes, instead of lump sum or mandatory annuities, may better align individual risk preferences and retirement needs. Specific initiatives to transform real estate assets and precious commodities such as gold into an income stream also merit consideration.

**Fiscal Space for Social Protection: Options Exist even in the Poorest Countries** Ortiz, I., Cummins, M., & Karunanethy, K. (2015b). ILO.

Brief:

<http://www.socialprotection.org/gimi/gess/RessourcePDF.action?ressource.ressourceId=53244>

Eight financing options described in this brief are supported by policy statements of the United Nations and international financial institutions.

1) Re-allocating public expenditures. For example, Egypt created an Economic Justice Unit in the Ministry of Finance to review expenditure priorities, and Costa Rica and Thailand shifted military spending to finance universal health services.

2) Increasing tax revenues. For example, Bolivia, Mongolia and Zambia are financing universal pensions, child benefits and other schemes from mining and gas taxes; Ghana, Liberia and the Maldives have introduced taxes on tourism to support social programs; and Brazil introduced a tax on financial transactions to expand social protection coverage.

3) Expanding social security coverage and contributory revenues. For example, Uruguay's Monotax and Argentina, Brazil, Tunisia and many others have demonstrated the possibility of broadening both coverage and contributions.

4) Lobbying for aid and transfers.

5) Eliminating illicit financial flows.

6) 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. Chile, Norway and Venezuela, among others, are tapping into fiscal reserves for social investments.

7) Borrowing or restructuring existing debt.

8) Adopting a more accommodating macroeconomic framework.

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, lack of public ownership, adverse socio-economic impacts and, frequently, civil unrest.

Full Paper: <http://www.social-protection.org/gimi/gess/RessourcePDF.action?ressource.ressourceId=51537>

### **Social protection and poverty**

Barrientos, A. (2011). International Journal of Social Welfare, 20(3), pp.240-249.  
<http://onlinelibrary.wiley.com/doi/10.1111/j.1468-2397.2011.00783.x/full>

The route to the expansion of social protection followed by today's developed countries was through payroll taxes to finance social insurance, but this is an unlikely route for countries in which the majority of the labour force works informally. The constraints to financing social protection and assistance in poorer countries are significant. In low-income countries in sub-Saharan Africa, poor revenue mobilisation is an important barrier to the extension of social assistance.

### **Financing Social Protection through contributions and the removal of fuel subsidy – Indonesia**

Chowdhury, A. (2016). ILO.

<http://www.social-protection.org/gimi/gess/RessourcePDF.action?ressource.ressourceId=53849>

Indonesia reprioritised its spending by cutting expensive fuel subsidies and successfully managed the political resistance by putting in place a compensatory scheme supporting low income families. It simultaneously worked on the extension of social protection by supporting the creation of a universal healthcare system and extending pension coverage.

### 3. Innovative finance

#### **Innovative Financing for Development: A New Model for Development Finance?**

Hurley, G. (2012). UNDP.

[http://www.undp.org/content/dam/undp/library/Poverty%20Reduction/Development%20Cooperation%20and%20Finance/InnovativeFinancing\\_Web%20over.pdf](http://www.undp.org/content/dam/undp/library/Poverty%20Reduction/Development%20Cooperation%20and%20Finance/InnovativeFinancing_Web%20over.pdf)

There is no internationally agreed definition of ‘innovative financing for development’. In reality, the term encompasses a heterogeneous mix of innovations in fundraising and innovations in spending, i.e. innovative financing for development comprises both innovations in the way funds are raised as well as innovations in the ways funds are spent on international development. Several international bodies have offered various interpretations of the term ‘innovative financing for development’:

- The Leading Group on Innovative Financing for Development suggests that innovative financing for development is “complementary to official development assistance. Innovative mechanisms are also predictable and stable. They are closely linked to the idea of global public goods and are aimed at correcting the negative effects of globalisation”. The Leading Group also recommends that innovative financing initiatives comply with the principles of the 2005 Paris Declaration on Aid Effectiveness and the 2008 Accra Agenda for Action.
- The World Bank defines innovative financing for development as “those that depart from traditional approaches to mobilizing development finance —that is, through budget outlays from established sovereign donors or bonds issued by multilateral and national development banks exclusively to achieve funding objectives. Innovative development finance therefore involves non-traditional applications of solidarity, PPP, and catalytic mechanisms that (i) support fundraising by tapping new sources and engaging investors beyond the financial dimension of transactions, as partners and stakeholders in development; or (ii) deliver financial solutions to development problems on the ground”.
- The OECD considers innovative financing “to comprise mechanisms of raising funds or stimulating actions in support of international development that go beyond traditional spending approaches by either the official or private sectors, such as: i) new approaches for pooling private and public revenue streams to scale up or develop activities for the benefit of partner countries; ii) new revenue streams (e.g. a new tax, charge, fee, bond raising, sale proceed or voluntary contribution scheme) earmarked to developmental activities on a multi-year basis; and iii) new incentives (financial guarantees, corporate social responsibility or other rewards or recognition) to address market failures or scale up ongoing developmental activities”.

Four broad categories or ‘typologies’ of innovative finance mechanisms can be identified:

1. Taxes, dues or other obligatory charges on globalised activities;
2. Voluntary solidarity contributions;
3. Frontloading and debt-based instruments; and
4. State guarantees, public-private incentives, insurance and other market-based mechanisms.

Most of the resources raised through the airline ticket tax are channelled into UNITAID. The agency was founded specifically to channel resources raised through this initiative into treatment

and care for those affected by HIV/AIDS, tuberculosis and malaria, i.e. MDG 6. UNITAID derives around 70 percent of its income from the international solidarity levy on air tickets. The remainder comes from more traditional multi-year budgetary contributions from bilateral partners and other donors. Since inception, UNITAID reports that it has raised close to US\$2 billion in resources to help provide treatment for approximately 47 million people worldwide. The prospects for broadening the implementation of the airline ticket tax are high.

Voluntary contributions most closely resemble more traditional forms of fundraising and charitable giving; the innovation lies in the method of collection which is often technology driven. Several initiatives have recently emerged which collect 'solidarity' contributions from consumers, businesses or diaspora communities for international development on a strictly voluntary basis. These differ from initiatives such as the international solidarity levy on air travel which is a government imposed (i.e. mandatory) tax on all consumers of a specified product. Sometimes referred to as 'micro-philanthropy', examples of recent initiatives include the '1% digital solidarity' initiative and MASSIVEGOOD.

Under the former, public institutions and private companies are urged to donate one percent of the value of an information and communications technology (ICT)-related contract to the Global Digital Solidarity Fund, which works to reduce the digital divide between developed and developing nations. The latter encourages travellers to make a micro-donation towards major global health causes such as malaria when they make a travel reservation on-line. Both initiatives are currently extremely small in size.

'Product (RED)' is a variation on this theme. When consumers purchase items branded Product (RED), producers donate 50 percent of profits on that item to the Global Fund to fight AIDS, TB and malaria. According to (RED), "since its launch in 2006, (RED) has generated over US\$170 million for the Global Fund and over 7.5 million people have been impacted by HIV and AIDS programs supported by (...) (RED) purchases" ((RED) 2011).

International solidarity efforts have also been furthered by tapping national lotteries. To date, Belgium and the United Kingdom have financed international aid programmes through their national lotteries. Since 1987, Belgium has mobilized nearly €330 million from its national lottery for food security projects in sub-Saharan Africa carried out by the national development agency, Belgian Technical Cooperation (BTC), non-governmental organizations (NGOs) and international organizations. In the United Kingdom, since 1995, approximately US\$310 million of national lottery resources has funded projects in developing countries. Clearly much more potential exists in this area. Proposals for a 'global lottery' have also been tabled to fund international development and climate change.

An emerging class of innovative finance initiatives involves the use of donor funds and/or private flows to catalyse market creation and development. The Advance Market Commitment (AMC) for pneumococcal vaccines is one example.

In December 2010, the Leading Group created a task force on health which, among other issues, would explore options to increase taxation on tobacco and pool additional revenues received. While many countries already tax tobacco heavily, proposals have recently emerged for some form of 'Solidarity Tobacco Contribution'. At the discretion of the taxing governments, small increases in tobacco excise in both developed and developing countries could be pooled and allocated to a menu of internationally agreed global health objectives. In 2011, the World Health Organization (WHO) released a discussion paper entitled: "The (Global) Solidarity Tobacco

Contribution—A new international health-financing concept prepared by the World Health Organization.” The WHO estimates that a tax increase of US\$0.05 per pack sold in G20+ countries would raise US\$4.3 billion for international health (WHO 2010). Bill Gates estimates that a Solidarity Tobacco Contribution may raise US\$9 billion per year for health. Moreover it could combine substantial revenue mobilization with positive health outcomes. The WHO also reports that there is substantial room for many developing country governments to act at national level to increase tobacco taxes to raise more funds for health and development. In 2010, the WHO showed that a 50 percent increase in cigarette excise taxes in 22 low-income countries could generate US\$1.42 billion to strengthen national health systems. As with carbon taxes, governments typically face significant pressure to use the majority of revenues collected nationally on tobacco consumption to fund national health priorities. As such, it is likely that only a small proportion of revenues collected via tobacco taxes will ever be allocated to international development objectives such as health.

In the health sector, the reach and development impact of initiatives such as the airline ticket tax, IFFIm and the AMC is well publicised on each mechanism’s respective website(s) and in annual reports. UNITAID, which is funded primarily through the international solidarity levy on airline travel, reports that it provides HIV/AIDS, TB and malaria treatment to approximately 47 million people in 94 countries worldwide. It has also reduced the cost of quality second-line anti-retroviral treatments by more than 50 percent. The 2011 Evaluation of the IFFIm estimates that between 1.3 million and 2.08 million deaths will have been averted by the end of 2011 due to the IFFIm. The WHO reports that 8,000 future deaths will be averted with GAVI pneumococcal vaccine support from 2000-2010. However, it should also be noted that take-up of the pneumococcal vaccine in the developing world has been slow to-date (MSF and Oxfam 2010). Other development outcomes are also attributed to these initiatives, some of which are summarised in the annex. Various factors are cited to explain these positive health outcomes. These are connected, in large part, to the delivery modalities selected for innovative finance streams. To date, most innovative finance initiatives have channelled resources through so-called ‘vertical funds’ (also known as ‘vertical programmes’ and ‘global programmes’). These programmes focus on specific themes (such as a communicable disease) and target resources exclusively at interventions to tackle that problem. Vertical programmes typically involve partnerships between multiple actors in both the public and private sectors.

### **Innovative Financing for Development: Scalable Business Models that Produce Economic, Social and Environmental Outcomes**

Guarnaschelli, D.S., Lampert, S., Marsh, E., Johnson, L. and Wallace, S. (2014). Global Development Incubator, New York, Washington, DC, and Hong Kong.

<http://2uqnr73tzny3sl15p2nqglls.wpengine.netdna-cdn.com/wp-content/uploads/2016/02/Innovative-Financing-for-Development.pdf>

Innovative finance (IF) is defined here as including broad range of financial instruments and assets including securities and derivatives, results-based financing, and voluntary or compulsory contributions.

Often, innovative financing instruments reallocate risks from investors to institutions better positioned to bear the risk and, in the process, enable participation from mainstream investors.

Three primary drivers of growth of innovative financing are noted:

- Increased use of established financial instruments. Established instruments that investors can evaluate through existing risk frameworks, such as green bonds, will attract new

participants, including pension funds and institutional investors. Channelling the proceeds of these instruments to productive development goals will require new standards that specify how funds can be used most effectively.

- Expansion into new markets through growth of replicable products. Over the past ten years, the international development community has experimented with new instruments such as performance-based contracts. These instruments do not yet have the track record to attract institutional investors, but offer promising opportunities to improve development outcomes in new sectors.
- Creation of new innovative financing products. New products have emerged that are theoretically promising, but have not yet demonstrated results. While these products will remain a small portion of the market in the short-term, the authors encourage donor governments and other funders to continue experimenting with these products so they can mature into the next important asset class.

Innovative financing can transform financial assets through financial structuring and intermediation to meet the needs of development programs by distributing risk, enhancing liquidity, reducing volatility, and avoiding timing mismatches. For example, green bonds and other thematic bonds provide capital to support investments in low-carbon infrastructure such as wind farms, sustainable forestry management, and urban infrastructure. In addition, innovative financing mechanisms such as the Pledge Guarantee for Health provide bridge financing for projects and institutions during the gap period between when resources are committed and resources are disbursed.

Access to essential health commodities through Advance Market Commitments accelerates the flow of capital to public goods that are not economically viable without public support. How it works: in an advance market commitment (AMC), a buyer—typically a government or international organization—agrees to a predetermined purchase price for a good or service with a provider—typically a private company. Originally, AMCs were conceived as a means to encourage companies to invest in research and development for new products, but it has also been used to increase production for an existing product. Under the Pneumococcal AMC, for example, donors pledged \$1.5 billion to fund the subsidized purchase of 2 billion doses of pneumococcal conjugate vaccine (PCV) beginning in 2009. In exchange for this subsidy, manufacturers agreed to sell PCVs to low-income countries at a price no greater than \$3.50 for the next ten years. As a point of comparison, the Pneumococcal AMC's prices for PCV are over 90% lower than those in high income markets.

### **A call for public financing: innovative finance is welcome, but not enough**

Putcha, V., Upadhyay, A. and Burnett, N. (2016). Early Childhood Matters.

[https://bernardvanleer.org/app/uploads/2016/07/Early-Childhood-Matters-2016\\_9.pdf](https://bernardvanleer.org/app/uploads/2016/07/Early-Childhood-Matters-2016_9.pdf)

Innovative finance can increase total volume through innovative sources, but can also improve the efficacy of those investments through the use of innovative delivery mechanisms. Innovative sources of finance can come in the form of new taxes with proceeds earmarked for early childhood programmes, corporate social responsibility, consumer donations, and impact investors. For example, in Colombia, a national payroll tax supports services run by the Colombian Family Welfare Institute (ICBF), which include health services, childcare, preschool education, and parent education. In the Philippines, a tax on gaming corporations supports National Child Development Centers (NCDCs) which provide integrated services for children from birth to 4 years old.

Innovative delivery mechanisms – which include results-based aid, results-based financing, conditional cash transfers, and impact investing – can incentivise innovative thinking about how to increase the efficiency and effectiveness of early childhood services. For example, in South Africa, social impact bonds are being used to fund the testing of various models in the Western Cape Province; the provincial Departments of Social Development and Health have committed to paying for outcomes. Linking financing to outcomes can be especially appropriate for mixed public– private systems, as are typical in early childhood development. Another example comes from Peru, where a results-based financing approach has been used to support ‘Cuna Más,’ which provides childcare and home visiting services across the country.

However, these innovations have their limitations. In this paper Emily Gustafsson-Wright and Sophie Gardiner discuss the current state of knowledge on impact bonds: while still at a nascent stage of development, they may ultimately not prove suitable for financing nationwide programming, especially where they require low- and middle-income countries to implement new and often complex legal frameworks. Likewise, the use of payroll tax revenue in Colombia has been challenged by weaknesses in the country’s overall tax collection system, while macroeconomic fluctuations have reduced the predictability of revenue. The more fundamental drawback of focusing too strongly on innovative financing is that it relegates ECD to a ‘special category’, and detracts attention from securing long-term, sustainable investments from governments. Ultimately, ECD should not solely be associated with innovative financing but should be able to benefit from those traditional sources of finance that support investments in older children and adults.

Innovative finance alone will not solve the problem of underinvestment. However, it may allow countries to jump-start investments and interest in early childhood services, which can help secure long-term support from traditional sources of finance. For example, in the Philippines, there are hopes that the Early Childhood Care and Development Council – responsible for the NDCCs funded by the tax on gaming corporations – will secure financing from the central government once the current legislation on the gaming tax expires in 2018.

### **Innovative financing for nutrition**

Beesabathuni, K. (2016). *Sight and Life*, 30 (1), pp53-61.

[http://www.sightandlife.org/fileadmin/data/Magazine/2016/Mag1/Innovative\\_Financing\\_for\\_Nutrition.pdf](http://www.sightandlife.org/fileadmin/data/Magazine/2016/Mag1/Innovative_Financing_for_Nutrition.pdf)

Joe Dougherty from Dalberg Global Development Advisors explains that: “Innovative financing is simply anything other than a traditional grant. It is of two types. One type seeks no financial returns such as performance-based contracts and the other type seeks financial returns such as debt, equity or a hybrid of the two.”

A particular class of impact investing, social impact bonds (SIB) – also called “pay for success” – has become popular in high-income countries. Private investors provide capital to fund a social intervention, and governments repay the investor only if an agreed outcome is achieved. Development Impact Bond (DIB) is similar to a SIB but implemented in low- and middle-income countries: a donor, as opposed to the government, funds the outcome.

The first and most notable DIB was started in 2014 in Rajasthan, India, and is called Educate Girls DIB. It aims to increase enrolment and improve learning outcomes for girls and funding is fully tied to outcomes. This DIB is a proof of concept to demonstrate both social and financial returns. In practice, it works as follows: Educate Girls (service provider) received working capital

from UBS Optimus Foundation (investor) to carry out a three-year intervention. ID Insight (outcome evaluator) will assess progress made in improving enrolment and learning outcomes and provide an evaluation report to the Children's Investment Fund Foundation (CIFF), UBS Optimus Foundation and Educate Girls after the program ends in 2018. CIFF (outcome payer) will disburse payments to UBS Optimus Foundation according to the indicators measured for the program.

Bridge funds are designed to increase the speed and efficiency of funding from international donors. Two notable examples are UNICEF's Pledge Guarantee for Health (PGH) and the US Fund for UNICEF Bridge Fund. PGH6 is a financial tool that enables governments and NGOs to obtain short-term, low-cost financing based on pending aid commitments. PGH transactions average six months in duration, allowing the \$100 million in credit from commercial banking partners to be turned over twice annually, thus reducing the time between a donor pledge and "money in the bank." Recipients are thus empowered to use committed donor funding in advance of disbursement, resulting in higher buying power, accelerated procurement and delivery, and optimization of the supply chain. This means that costs associated with uncertain payment timings, additional premiums, expedited production and shipment, stock-outs, wastage, and expired commodities are lowered.

The Power of Nutrition is an independent charitable foundation that has committed to unlock \$1 billion by 2020 in new private- and public-sector financing for child nutrition that would not have been generated in its absence. Every dollar from private and other non-traditional sources of financing (such as non-OECD donors) is first matched by the UK's Department for International Development (DfID). A second match is guaranteed by the implementing partners. This financing is expected to drive a measurable reduction in child undernutrition by scaling up a package of evidence-based nutrition interventions in hotspot geographies in sub-Saharan Africa and Asia. Incubated by CIFF and the UBS Optimus Foundation, the Power of Nutrition was launched in April 2015 with \$200 million in signed commitments. It identified Tanzania as the first nutrition hotspot and made a first investment to the country in partnership with the World Bank. This investment unlocks up to \$44 million to provide incentives to primary health care facilities for successful performance against nutrition indicators.

A new investment that unlocks \$10 million to tackle child undernutrition in post-Ebola Liberia has just been announced in partnership with UNICEF. UNITLIFE is a model built on the solidarity levy in extractive industries started in 2014. Replicating the very successful UNITAID model, UNITLIFE brings together political leader commitments from seven countries in Africa to eliminate chronic malnutrition. It is estimated that \$100–\$200 million in annual revenues can be generated from a micro levy of \$0.10 on each barrel of oil sold by the state. Benefits include substantial source of funding, low maintenance to collect once installed, ability to expand to gas and minerals, independence from annual public budgeting and discussion process in parliament, which makes the solidarity levy mechanism less volatile. The structure of the model is currently being designed, and may look similar to UNITAID. UNITLIFE will be governed by a steering committee whose members will include contributing countries and UNICEF (as the host organization), whilst the committee will be supported by a small technical secretariat located in Geneva. A technical advisory committee, whose members are independent, will evaluate proposals to support the implementation of nutrition-specific interventions as mentioned in The Lancet and to advise the steering committee.

Impact Investment provides growth capital to companies with both a financial and a social mission. Investments typically run for at least five years and provide a return of principal, with

returns ranging from zero to market rate. A good example in nutrition is the loan made by LGT Venture Philanthropy, through a partnership with GAIN, to Meds & Food for Kids, a Haitian-based producer of lipid-based nutrient supplements. A loan of \$732,000 helped to set up a new production facility that now has the capacity to produce 10 times more than it did at its previous facility. Over a period of five years, more than 100,000 children received these supplements. Such examples are few, and funds have yet to be effectively targeted towards nutrition. This is partly due to the lack of investable companies, which are either too small or not sufficiently profitable. However, if partnerships with the public sector are catalysed, one can expect to see scale through impact investment, as in the case of Africa Improved Foods in Rwanda, which has a total project size of \$59 million through a mix of debt and equity from investors, private sector and the government of Rwanda. Africa Improved Foods in Rwanda aims to reach more than a million people with adequate nutrition in two years.

### **Innovative financing for development**

Douste-Blazy, P. (Coordinator). (2009). UN.

<http://www.un.org/esa/ffd/documents/InnovativeFinForDev.pdf>

Cases studies:

- UNITAID – taxation of airline tickets.
- The International Finance Facility for Immunization [IFFIm] created to support the Global Alliance for Vaccines and Immunizations [GAVI].
- Advanced market commitments. Donors commit upfront to buy vaccines at a set price if and when they are available, meet minimum pre-specified criteria and are demanded by developing countries.
- Voluntary Solidarity Contribution' project – micro-donations for those buying air tickets.
- (RED) - a brand created to engage business and consumer power in the fight against AIDS in Africa.
- Debt2Health - initiative of the Global Fund. Converts portions of old debt claims into new domestic resources for health.
- Revenues from the carbon market – selling emissions allowance and using the funds for development.
- Socially responsible investments example – a mutual investment fund in partnership with a French bank.

### **Innovative financing for health: what is truly innovative?**

Rifat Atun, F. M. (2012). London: Lancet

<https://www.ncbi.nlm.nih.gov/pubmed/23102585>

Abstract: Development assistance for health has increased every year between 2000 and 2010, particularly for HIV/AIDS, tuberculosis, and malaria, to reach US\$26.66 billion in 2010. The continued global economic crisis means that increased external financing from traditional donors is unlikely in the near term. Hence, new funding has to be sought from innovative financing sources to sustain the gains made in global health, to achieve the health Millennium Development Goals, and to address the emerging burden from non-communicable diseases. We use the value chain approach to conceptualise innovative financing. With this framework, we identify three integrated innovative financing mechanisms-GAVI, Global Fund, and UNITAID-that have reached a global scale. These three financing mechanisms have innovated along each step of the innovative finance value chain-namely resource mobilisation, pooling, channelling,

resource allocation, and implementation-and integrated these steps to channel large amounts of funding rapidly to low-income and middle-income countries to address HIV/AIDS, malaria, tuberculosis, and vaccine-preventable diseases. However, resources mobilised from international innovative financing sources are relatively modest compared with donor assistance from traditional sources. Instead, the real innovation has been establishment of new organisational forms as integrated financing mechanisms that link elements of the financing value chain to more effectively and efficiently mobilise, pool, allocate, and channel financial resources to low-income and middle-income countries and to create incentives to improve implementation and performance of national programmes. These mechanisms provide platforms for health funding in the future, especially as efforts to grow innovative financing have faltered. The lessons learnt from these mechanisms can be used to develop and expand innovative financing from international sources to address health needs in low-income and middle-income countries.

### **Sharing innovative experiences. Successful Social Protection Floor Experiences**

UNDP. (2011).

[http://www.ilo.org/wcmsp5/groups/public/---ed\\_protect/---soc\\_sec/documents/publication/wcms\\_secsoc\\_20840.pdf](http://www.ilo.org/wcmsp5/groups/public/---ed_protect/---soc_sec/documents/publication/wcms_secsoc_20840.pdf)

Social protection floors are nationally defined sets of basic social security guarantees that should ensure that, as a minimum, over the life-cycle all in need have access to essential health care and to basic income security, which together secure effective access to goods and services defined as necessary at the national level.

- In 2008 Bolivia created a universal non-contributory pension for all people 60 years of age and over, financed by a share of the special hydrocarbon tax and dividends from capitalised public enterprises. Called Renta Dignidad (the Dignity Pension), key points include the following: Launched in 2008 as a universal benefit for all people 60 years of age and older.
- Universal non-contributory pension.
- Identification documents are needed to register for the scheme; biometric registry is being developed.
- Benefit can be paid monthly or accumulated over up to 12 months. The amount is equivalent to about \$340 per year.
- By 2010 there had been 800,000 beneficiaries and \$500 million paid.
- Financed by a fixed share of the special direct tax on hydrocarbons (impuesto directo a los hidrocarburos— oil and gas revenue), with contributions from all levels of government, and dividends from capitalized public enterprises (association with the multinational enterprises, which are now undergoing nationalisation).
- Impact: a 5.8 per cent reduction in extreme poverty between 2007 and 2009 (especially in rural areas).

China's Rural New Cooperative Medical Scheme is a multi-channel financing mechanism. Both central and local governments subsidize the enrollees, and the households of the enrolled farmers should also contribute. In addition, social-sector donations are a funding source. Subsidies from the central government have increased from 10 yuan (US\$1.477, or US\$2.632 PPP) per capita in 2003 to 60 yuan (US\$8.863, or US\$15.789 PPP) per capita in the central and western regions in 2010. The average per capita contribution collected from all channels has increased from 30 yuan (US\$4.431, or US\$7.895 PPP) in 2003 to 150 yuan (US\$22.156, or US\$49.474 PPP) currently.

The Medical Assistance Scheme (MAS) in China is funded by the Government and voluntary donations from social sectors. It offers special financial assistance to the poor and other households that suffer or cannot afford large medical expenses.

## 4. Natural resources

### **Financing social protection through taxation of natural resources - Bolivia**

Urban, S. (2016a). ILO.

<http://www.social-protection.org/gimi/gess/RessourcePDF.action?ressource.ressourceId=53854>

Lessons learned:

- Natural resource-rich countries can boost their social protection system through the taxation of natural resources, increasing government revenues and supporting the expansion of social protection expenditures.
- Earmarking government income generated from natural resources can directly link the allocation of funds to social protection programmes.
- The process of increasing social expenditures was accompanied by a transparency initiative that requires local and national governments to disclose their revenues and transfers. Civil society organizations in parallel carry out the monitoring of company payments to the State and the management of related revenue at the national and sub-national levels.
- Through the taxation of natural resources and the expansion of social protection spending, the government managed to reduce poverty rates and inequality, while also supporting economic growth.

### **Financing social protection through taxation of natural resources - Zambia**

Urban, S. (2016b). ILO.

<http://www.social-protection.org/gimi/gess/RessourcePDF.action?ressource.ressourceId=53857>

In 2013, Zambia's extractive revenue was US\$ 1.5bn annually and represented 30 per cent of total government revenue. With the help of the extractive industry revenues, the government increased the budget for the social cash transfer schemes substantially, from KR 55 million in 2012 to KR 199.2 million in 2014.

The case of Zambia exemplifies that resource rich developing countries can substantially expand fiscal space for social protection and other socio-economic expenditures. Taxing natural resource extracting industries allowed the Zambian government to improve their fiscal position and created the basis for the expansion of their social protection system.

### **Financing social protection through taxation of natural resources - Zambia**

Urban, S. (2016c). ILO.

<http://www.social-protection.org/gimi/gess/RessourcePDF.action?ressource.ressourceId=53856>

Mongolia is an example of a country that has recently started to take more advantage of its vast natural resources. Mongolia's development has been spurred by revenues from extractive industries. The Government has made significant efforts to ensure that the wealth created from its natural resources is shared among the wider population and that resources are directed to social protection programmes, such as the Universal Child Money programme.

## **Mineral Rents and the Financing of Social Policy: Options and Constraints**

Hujo, K. (2012). UNRISD.

[http://www.unrisd.org/80256B3C005BCCF9/\(httpAuxPages\)/C3C55CD888A5AECC1257ACA004C8FA9/\\$file/RPB16e.pdf](http://www.unrisd.org/80256B3C005BCCF9/(httpAuxPages)/C3C55CD888A5AECC1257ACA004C8FA9/$file/RPB16e.pdf)

Mineral wealth is not a curse but an economic opportunity. UNRISD research suggests that when countries carefully balance productive and redistributive goals, mineral wealth can be harnessed for equitable and sustainable development. To manage the challenges of a mineral-led growth path successfully, countries need to design and implement comprehensive, inclusive and rights-based social policies; build strong democratic institutions; and be given the policy space to foster productive diversification while safeguarding macroeconomic stability.

Policy implications identified:

- Build state capacity and foster positive institutional change.
- Design policies that foster stability, diversification and equality.
- Channel mineral rents into comprehensive social policies.
- Make foreign investors commit to national development strategies and create fair rules on global commodity markets.
- Do not neglect mobilization of other domestic revenues.

## **Innovative financing mechanisms to improve fiscal space for social spending**

Annycke, P. (2009). Summary of the presentation at the GTZ Conference in Bishkek, Kyrgyzstan- 30 Nov.-1 Dec 2009.

<http://www.social-protection.org/gimi/gess/RessourceDownload.action;jsessionid=11KfYLzWkVznpQBthmDQP2GmkpsCkTJQ5XT1pj5Wnn84vbGyBjty!79209976?ressource.ressourceId=15007>

Key examples:

- Petrol for Basic income in Alaska - Alaska Permanent Fund (1976):Funded by a share of oil revenues to benefit to present and future generations of Alaskans. Each year, the residents of Alaska receive a cash transfer: in 2009 this flat rate was \$1,305, although it is revised annually. Norwegian Government Petroleum Fund (1990), revenues from oil and gas. This was transformed in the Government Pension Fund (2006) to support the pension system.
- Financial income tax to support pension schemes eg. In France, the tax on estate and financial incomes to support the national pension schemes. This involved Generalised Social Contributions' (CSG), that is tax on all incomes (from labour and capital), to finance a minimum non-contributory pension.
- VAT to support social security:
  - Ghana has increased VAT by 2% on some products to finance health care.
  - Belgium and other European countries have increased taxes on alcohol and tobacco products to finance social security (social cost of alcohol and tobacco abuse).
  - Brazil created a special fund to finance pension for farmers (FUNRURAL), financed by a tax (2.2%) on the first purchaser of rural goods
- The combination of sources to extend health care. For example, in Colombia non contributory health care is financed through a health lottery + games of chance, tax on alcohol and

tobacco, coffee corporation, health contributory schemes (1.5% of due contribution) and general government tax.

## 5. Social impact bonds

### Social Impact Bonds

The Rockefeller Foundation. (2017). Webpage accessed 20.3.17

<https://www.rockefellerfoundation.org/our-work/initiatives/social-impact-bonds/>

Federal, state, and local governments are facing a financial crunch, and social services—especially prevention-oriented services—often face cutbacks or elimination, impacting vital areas including healthcare, education, poverty, and the criminal justice system.

Sitting at the nexus of the Foundation's work in scaling innovation and impact investing, social impact bonds (SIBs), like 'pay-for-success' projects, represent one component of the rapidly growing field of innovative finance, aimed at helping state and local governments fund critical social programs through a combination of government initiation, private investment, and non-profit implementation. In the social impact bond model, the private sector works with governments and philanthropies to fund critical prevention focused social programs that help address the world's most pressing problems. In this public-private partnership, investors are only repaid if and when improved social outcomes are achieved. Social impact bonds have the potential to open new funding sources for prevention-oriented programs that deliver measurable social benefits, saving taxpayer dollars in the process.

### **Peterborough social impact bond reduces reoffending by 8.4%; investors on course for payment in 2016**

Social Finance Limited. (2014). Social Finance Limited press release.

<https://assets.rockefellerfoundation.org/app/uploads/20150316202925/Peterborough-Social-Impact-Bond-Reduces-Reoffending-by-8.4-percent.pdf>

Social Finance launched the Peterborough Social Impact Bond in 2010, supported by 17 foundations who committed to invest £5million. It was designed as a seven year pilot to test the premise that offering comprehensive and individual support to prisoners would help them stay out of prison and build a new life for themselves on the outside. The first cohort of prisoners was released from September 2010 – May 2012. During this period, Social Finance set up a new service, known as the One Service, which included delivery organisations St Giles Trust, Sova, Ormiston Families, YMCA and, MIND to provide housing, family, health, employment and training support. The One Service also works with local drug and alcohol services. John Laing Training joined the project in the second cohort.

As the programme progressed, it was clear that there were three gaps which impacted the lives of prison leavers most profoundly: the provision of accommodation, support for low-level mental health needs and the lack of training and employment opportunities. Flexible funding from investors allowed the One Service partners to create a multi-agency offering to respond to these needs of the offenders.

Repeat offending by short sentenced prisoners has challenged the UK for many years but no statutory support has been on offer for this group of prisoners. As offenders recognised that the Peterborough project was stable and long-term, and would continue to support them even if they ended up back in prison, engagement levels rose from 74% in Cohort 1 to 86% in Cohort 2 while in prison, and from 37% (Cohort 1) to 71% (Cohort 2) after release. Not only did engagement

levels rise over the course of the first four years, but the team's understanding and ability to meet the needs of offenders improved. This is reflected, for example, in the reoffending rates for the first six months of the Cohort 2 which lie 8% below those for the first six months of Cohort 1.

### **Social impact bonds. The early years.**

Dear, A., Helbitz, A., Khare, R., Lotan, R., Newman, J., Crosby Sims, G., and Zaroulis, A. (2016). Social Finance.

[http://www.socialfinance.org.uk/wp-content/uploads/2016/07/SIBs-Early-Years\\_Social-Finance\\_2016\\_Final-003.pdf](http://www.socialfinance.org.uk/wp-content/uploads/2016/07/SIBs-Early-Years_Social-Finance_2016_Final-003.pdf)

A Social Impact Bond is a public-private partnership which funds effective social services through a performance-based contract. Social Impact Bonds enable federal, state, and local governments to partner with high-performing service providers by using private investment to develop, coordinate, or expand effective programs. If, following measurement and evaluation, the program achieves predetermined outcomes and performance metrics, then the outcomes payer repays the original investment. However, if the program does not achieve its expected results, the payer does not pay for unmet metrics and outcomes.

The core utility of Social Impact Bonds is to fund intensive services tailored to complex and individual needs. They are typically worth considering when:

- Identifiable populations with complex, cross-agency needs, who require tailored interventions, are not being served.
- Current spending has poor or undetermined outcomes.
- There are high financial and political costs to society and government in not addressing the social issues.
- There is a benefit to using external investment to provide risk capital and assume innovation and implementation risk for new or evidenced-based programs.
- There are social sector partners who can deliver effective services, but there is an element of uncertainty about what outcomes can actually be achieved.

Social Impact Bonds might not be a proven model, but they are no longer untested. In the six years since the launch of the Peterborough Social Impact Bond, 60 projects have launched and 22 projects have reported performance data. 21 projects indicate positive social outcomes and 12 projects have made outcome payments, either to investors or to be recycled into service delivery. 4 projects have fully repaid investor capital.

While 21 projects report positive performance, not every project has delivered positive impact or will in the future. In one instance—the first US Social Impact Bond at Rikers Island in New York City—the project was discontinued early due to unsuccessful results. However, even in this example, the mechanism worked as intended: when the project evaluation revealed the services were not leading to a reduction in recidivism, investors took a loss and the government did not pay for unsuccessful services.

The most common complaint of Social Impact Bonds is that they are complex. By virtue of the social issues they address, it is hard to imagine they will ever be completely simple. But there is recognition that the complexity of the development process will inhibit the growth of the market and it is known that the model needs to simplify so it can reach the impact and scale being looked for.

Signs of standardization are already being seen in the field, with programs being replicated and adapted to multiple geographies. This is important: it will accelerate the development of existing Social Impact Bond models, reduce the costs for government and allow for new social issues to come to the fore. Funders will gather data and be able to value specific outcomes with more confidence and new, non-governmental outcome payers will emerge.

## 6. Pensions

### **Social Protection in ASEAN: Challenges and initiatives for Post 2015 Vision Asher, M.G. (2015). Forthcoming.**

The goal of any pension system should be to enable people in old age to obtain a bundle of services in a manner which is adequate, affordable by the society, and accessible. Countries use different financing-mixes and differing methods of social and household risk pooling arrangements to enable the elderly to obtain retirement income for financing the bundle of services needed. This has been the case in ASEAN countries, where Singapore, Malaysia, and Thailand mostly rely on compulsory savings whilst Indonesia, Philippines, and Vietnam have employed social insurance principles to organise their pension system.

These programme-mixes or instrument-mixes reflect historical legacies, institutional choices, and country-specific administrative and fiscal capacities. Given the heterogeneity in a relatively small area such as ASEAN, there is no blueprint that can be provided to organise a pension system. Member countries will have to design their own instrument-mix based on country-specific circumstances such as formality of labour markets, fiscal space to finance public pensions, professionalism of social protection organisations, and regulatory capacity to supervise social protection organisations.

Avenues to generate resource savings and fiscal space, and finance for funding expenditure on the aged are briefly noted below:

- There is considerable scope for economic resource savings, which can be obtained through increased professionalism in the design, administration and structure of provident and pension funds and health care systems, among others. The Philippines SSS (Social security system), for example, exhibits administrative costs of around 7 per cent of contributions, while the estimate for Malaysia's EPF (Employee Provident Fund) is around 3 per cent. A reduction in costs of the SSS through process and system reforms could thus improve benefits. The SJSN Law of Indonesia (2004) has insufficient clarity on financing, benefits etc., and does not adequately address the need for appropriate organisational incentive structures. This neglect may generate contingent fiscal liabilities. Separating charges for fund investments and for administration by pension fund managers could reduce pension management costs in the UK, thus improving benefits. There is a strong case for exploring various avenues for reducing administration and compliance costs of pension and health care programs.
- Enhancing competence to generate resources from unconventional sources, such as utilising state assets (land, property rights such as air-space, oil and mining resources, and carbon trading, among others) efficiently. This is likely to involve better coordination among and between pension and healthcare sectors for increased resource savings and greater policy coherence.
- Conventional tax reforms, and improving compliance levels and efficiency.

- Sovereign Wealth Funds (SWFs), set up to smoothen excess of current receipts over expenditure arising from energy resources, trade surpluses, and other sources, and between generations, represent another avenue for funding old age needs. In Asia, South Korea, China and Singapore have been adept at using the SWFs to fund future expenditure needs, including those of the aged.
- Financial innovations, particularly at the pay-out phase, are accumulation schemes. The conventional practice of relying on annuities will be inadequate given limited financial instruments to mitigate longevity risk, and due to uncertainties in longevity trends as a consequence of uncertainties in medical technology breakthroughs. Such innovations, which reduce transaction costs of service delivery and provide better risk sharing between the insurance company, the individual, and the government, will be needed.

As pre-funding arrangements, through retirement savings or accumulation of reserves, become increasingly common (pension assets are expected to grow significantly in ASEAN countries), the development of domestic financial and capital markets has become essential. Provident and pension funds will need to increasingly acquire competencies to deal with sophisticated investment strategies using diverse asset classes (e.g. debt, equity, real estate and currencies) and diverse players (such as hedge funds, private equity investors and sovereign wealth funds).

Such sophisticated strategies however should not be attempted without adequate preparation; and without understanding downside risks. In many low and middle income countries, it may be prudent to not fully attempt to obtain upside potential from investments or from financial innovations such as credit-default risks, in order to minimize downside risks. Fiscal policy and financial and capital markets are essential for effective for social security reform.

Provident and pension schemes require greater degree of financial education and literacy on the part of all the stakeholders, particularly individual members. The growing complexity of financial products and multiplicity of new financial players underscore the importance of financial education and literacy. Financial education and literacy should not be interpreted narrowly as only provident and pension funds in providing leadership and finances in designing and delivering these services to members. The lessons of financial education and literacy should be incorporated in the design and governance structures of the provident funds. This unfortunately is not the case with many provident funds in ASEAN.

### **Micropensions in India: Issues and Challenges**

Asher, M.G. (2011). International Social Security Review, 64, no. 2: 1 – 21.

[http://www.umdcipe.org/conferences/policy\\_exchanges/conf\\_papers/Papers/shankar-asher.pdf](http://www.umdcipe.org/conferences/policy_exchanges/conf_papers/Papers/shankar-asher.pdf)

Micropensions refer to long term savings, by relatively low income, informal sector workers, with the objective of obtaining income security during old age. While the microfinance industry has shown rapid growth, micropensions are still in the early stages of development. A micropension plan is typically designed as a defined contribution plan providing for small value, frequent contributions which are collected at a place convenient to the member. The plan needs to address longevity, investment and inflation risks specifically in the context of low income members. Demographic trends underline the need for micropensions in India. The possibility of using microfinance institutions (MFIs) as a channel for organizing micropensions is analysed. Case studies of two micropension plans launched recently in India are discussed. The paper concludes that with appropriate regulation and more robust risk sharing arrangements, there is potential for micropensions to play a useful role as an integral component of India's social security system.

The UTI micropension is based on small value of deposits (ranging from Rs. 50 to Rs. 200 per month); flexibility in payments (monthly or yearly contributions are not mandatory), and presence of a third party, such as a cooperative, SHG, MFI or an NGO. The non-mandatory nature of the contributions is an important departure from the traditional pension plans. The contributions must typically be made until age 55 and the pension payments begin after age 58, with nomination facility being available on death of the person. The role of the third party is to be a locus for generating a large number of members with common characteristics; to undertake certain administrative functions; and act as a channel of communication. The third party assists in reducing transactions costs. The savings from members are pooled and transferred to UTI for funds management. Records are maintained on an individual basis and each member receives a unique account number. The third party must therefore command trust and confidence of the members as well as be competent in administration and financial matters. Moreover both the trust and the competence must be sustained over a long period. Increasing supply of such third parties is therefore critical to expanding the reach of micropensions.

The first micropension scheme with UTI asset management company (AMC) as the fund manager was launched in partnership with an urban cooperative bank run by SEWA (Self Employed Women's Association) an MFI. Thereafter schemes have been launched with COMPFED, a federation formed by milk producers in Bihar; Paradip Port and Dock Mazdoor Union (a labour union), self help groups of REPCO Bank, Union Bank of India and Bank of India and an MFI, SHEPHERD (Self Help Promotion for Health and Rural Development) and Mann Deshi, a cooperative bank. The fund management is done by UTI. A maximum of 40% of the corpus is invested in equity and the balance is invested in debt. Actual investment in equity is however around 20%. The target appears to be an annual return of 10 to 12 % after all expenses. It is too early to evaluate the extent to which the target is likely to be achieved. UTI AMC has made only minor adjustments in their usual charges levied for managing regular pension funds. The management fees range from 1.75% to 2.5% of assets depending on the assets under management. There are however, no empirical studies available as yet to estimate such costs as a percentage of contributions and of assets and their behaviour over time.

In savings-based micropension schemes, investment, macroeconomic and other risks are borne by the individual. Risk-sharing arrangements have therefore been often advocated. Some have argued for co-contributions by the government at the accumulation stage for participants in micropensions. Other options include risk sharing by the society (through government) at the pay-out phase. These could be in the form of special bonds or bank deposits with higher interest rates for senior citizens (with a cap on total investment) which vary according to market interest rates on long-term government bonds. This can be combined with well-targeted and reasonably funded old age assistance schemes financed from general budgetary revenue. More research is needed in the Indian context before designing risk-sharing options. In particular, political economy considerations, where populist policies often trump financial and economic sustainability, should play an important role in design of such options. It would appear that co-contributions by the government at the accumulation stage may be particularly vulnerable to dysfunctional populist policies. The issue of who should bear the costs of the services of the third parties needs to be considered.

For the back end operations and the MIS required for the scheme, SEWA has entered into a collaboration with Invest India Micropension Services Limited (IIMPSL), a company set up by a group of leading NGOs (including SEWA) and activists for the purpose of providing services for

design and implementation of sustainable and scalable micropension and microinsurance schemes for low income groups. IIMPSL effectively results in sharing of overheads by organizations seeking to implement pension schemes. This will enable MFIs to access better technologies due to economies of scale and scope than they would have individually been able to afford. IIMPSL primarily envisages working with MFIs, cooperatives, associations and public service networks. IIMPSL's services include individual partner level process design, information technology capacity building, training and certification. It is also in the process of developing and piloting web based social security application (sCube). The UTI AMC is an example of provision of micropension through collaboration of MFIs with professional fund managers. The use of shared overhead costs by partnership with IIMPSL improves the viability of the scheme. In the first one year, the UTI SEWA initiative had 40,000 enrolled members out of the target of 100,000 members. The other collaborations of UTI have been announced in the last one year and are still in the early stages.

Rajasthan Vishwakarma Unorganized Sector Workers (Motivational) Contributory Pension Scheme 2007: the scheme was launched in August 2008 and is being jointly implemented by the Rajasthan state government and IIMPSL, as the consultant and turnkey implementation agency. As mentioned earlier, IIMPSL was set up by a group of leading NGOs and activists for the purpose of providing services for design and implementation of sustainable and scalable micropension and microinsurance schemes for low income groups. The minimum contribution for the scheme is Rs. 100 at one time. The scheme is a co-contributory one with the Rajasthan State Government having committed to add a matching contribution to the members' savings subject to a maximum of Rs. 1000 per annum per worker.

The government is paying an interest of 8% p.a. on the total contributions in the retirement account. It is examining the possibility of investing the funds of the scheme with a regulated fund manager which is itself regulated by the PFRDA. Upon reaching the age of 60 years, the member will receive a pension based on the sum total of member contributions, government contributions and interest generated.

As of September 2008, an estimated 20,000 workers from six districts of Rajasthan had enrolled for it. The state is aiming for at least half a million workers to be covered by 2010. IIMPSL estimates that out of the 80 million workers capable of saving for retirement, at present only 5% are doing. They also estimate the size of untapped savings to be as high as Rs.110 billion. The Rajasthan micropension scheme is an interesting experiment though the contribution by the government will impose a fiscal cost on the state. Moreover the funds need to be professionally managed. Considering the long time horizon, maintenance of returns at the fixed interest rate being offered may need considerable financial expertise.

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