

TOOL FOR FISCAL SPACE ANALYSIS WHEN FINANCING SOCIAL PROTECTION

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Global Coalition for
SOCIAL PROTECTION FLOORS

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Introduction

What is an Interagency Social Protection Assessment tool?

In 2012, the Social Protection Interagency Cooperation Board (SPIAC-B) decided to develop tools that would facilitate interagency work on social protection. They first pulled together a framework for analysis for various aspects of the performance of social protection systems at the system, programme and delivery levels. The resulting Interagency Social Protection Assessment (ISPA) tools thus have a standardized structure and process for their components and for their implementation, including piloting and interagency approval.

The development of ISPA tools is done through working groups. A working group for the fiscal space tool was constituted in February 2019 under the leadership of the International Labour Organization (ILO). As the lead agency, the ILO is now tasked with elaborating the zero version of the fiscal space tool.¹

ISPA tools are diagnostic tools. They are not prescriptive and do not provide a specific implementation plan for reforms or interventions. However, they can be used to assess strengths and weaknesses that serve as inputs when developing policy options and recommendations. The ISPA tools are expected to produce an evidence base for country dialogues on strengthening social protection systems, programmes and delivery aspects and also function as a mechanism to promote exchange and coordination between national and international partners.

The ISPA tools follow a similar structure and logic: (a) taking stock of a situation in a given country, including the legal and policy frameworks and existing structures and practices; (b) analysing performance against national objectives and standardized performance criteria; (c) providing an evidence base for country dialogue on how to strengthen performance, taking into account local conditions; and (d) promoting exchange and coordination between national and international partners.

The government in any given country should lead the use of the ISPA tools, and the process should involve relevant government ministries and agencies, social partners, civil society organizations, national social protection practitioners and experts, the private sector as well as international development partners. Countries can also request technical assistance from international development partners when implementing the ISPA tools.

This report presents implementation guidelines that reflect the type of activities that should be undertaken to use the fiscal space tool in the field. They are not intended to be prescriptive nor restrictive. Each ISPA tool application will require an adaptation of these guidelines to fit local circumstances, depending on the needs and availability of data and resources.

Over the years, the development partners have developed methods and procedures to support national dialogue in analysing fiscal space and assessing financing options for social protection. This know-how can be useful for national policymakers because it can guide national estimates and models and support their assessment of their country's capacity for social protection costing and financing. A write-up of these methods and procedures is the starting point for a fiscal space tool. In view of significant financing gaps that hinder the achievement of universal and adequate social protection,² countries can request technical assistance in their assessment, costing and financing of social protection. Regularly, development partners and governments have prepared individual approaches to the assessment of fiscal space. Given this, the fiscal space tool is a good idea to integrate multiple perspectives into one method when it gives policymakers a methodology to analyse their country-specific situations.

1 A new tool developed by a working group can only receive the ISPA denomination after it has been piloted in at least two countries. For this reason, this paper refers to the tool for fiscal space analysis when financing social protection as the "fiscal space tool".

2 See for example, ILO, [Social Protection Financing Gaps](#), 2020.

Fiscal space tool for financing social protection

There are institutional differences in the definition of fiscal space. The fiscal space tool is based on a broad definition instead of a narrow view of public debt assessment. It also emphasizes that fiscal space is dynamic in the sense of not having limited potential but instead is a variety of sources that can be considered when searching for options to mobilize resources to finance and invest better in social protection. The tool's definitions are thus consistent with the ILO Convention on Social Security (Minimum Standards), 1952 (No. 102), the ILO Social Protection Floors Recommendation, 2012 (No. 202) and Sustainable Development Goal target 1.3, among others.

Social protection is a fundamental human right, as declared in the United Nations High Commissioner for Human Rights' 2021 report on economic, social and cultural rights to the Economic and Social Council.³ The provision of social protection should align with the principles of service availability, benefit adequacy, accessibility, universal coverage, equality and non-discrimination, among others.

For the tool to be fully usable and pertinent to different national contexts, it offers widely applicable methodologies and a scope of assumptions to simplify the estimation of revenues generated by different financing options. It primarily targets national policymakers who want to develop or strengthen their country's national capacity to model and estimate the fiscal space for social protection and consider new financing options that are consistent with international standards and good practices on social protection.

3 See www.ohchr.org/en/statements/2022/07/introduction-report-economic-social-and-cultural-rights.

1. Conceptual considerations

This chapter discusses the conceptual foundations around fiscal space for social protection considerations.

General motivation

Over the past few years there has been international recognition that social protection has a critical role in the achievement of the goals of the 2030 Agenda for Sustainable Development (SDGs) and myriad other positive effects. There are several channels through which social protection exerts influence on different sectors within a country. For instance, cash transfers and other monetary benefits may reduce poverty or may reduce the severity of poverty that the most vulnerable households and individuals experience. Social benefits may influence, directly or indirectly, the improvement of social conditions through enhanced levels of savings, increased physical and human capital accumulation as well as enabling innovation and entrepreneurship.

Pecuniary benefits may stimulate demand and consumption, thus contributing to economic growth and employment (OECD 2019; UNDESA 2018). HelpAge International (2021) found that social protection investments are good for social cohesion because they promote transparency in the allocation of resources; expand the levels of social trust, participation in community activities and satisfaction with living standards; reduce economic inequality; and improve social mobilization. In short, social protection is a tool that strengthens the social contract and social cohesion.

In addition to theoretical developments, diverse studies over the past decade have aimed at empirically estimating the effects or impact of social protection on social and macroeconomic variables. The Organisation for Economic Co-operation and Development (OECD) (2019), for instance, explored the micro-effects of social assistance programmes in Brazil, Germany, Ghana and Indonesia. Their empirical results showed that conditional cash transfers for children associated with higher levels of investment in education (including enrolment and attainments), especially among poorer students. Conditional cash transfers also associated with less child labour but they had no effect on early pregnancy. As part of the Multipliers of Social Protection Project, Tadeu Lima et al. (2021) conducted statistical and econometric estimates for Cape Verde, Ecuador, Mexico, Pakistan, Paraguay and Viet Nam. They concluded that social benefits had a positive impact on the level of economic activity.

Due to the expected positive social and economic outcomes from increased social protection investments, multiple voices have clamoured for universal coverage as the ultimate goal in this field. The ILO and World Bank Group's Concept Note to its Shared Mission for Universal Social Protection states that "universal coverage and access to social protection are central to ending poverty and boosting shared prosperity",⁴ while the United Nations Human Rights Office (2022) takes the position that social protection coverage implies that "all persons should be covered by the social security system, especially the most disadvantaged and marginalized groups, without discrimination". The achievement of these goals requires, as expected, new funding to expand programmes over time.

According to Durán-Valverde et al. (2019) and the World Social Protection Report 2020–22 (ILO 2021), only around 45 per cent of the world's population is covered by at least one social protection benefit. In other words, more than half of the global population (about 4 billion persons) is fully unprotected. To close or reduce this proportion, all countries should allocate incremental investments in social protection on a regular basis.

As of 2019, the estimated gap to fully cover the global population with monetary social protection floor benefits for children, maternity, disability and old age⁵ was estimated at US\$527.1 billion, or 1.6 per cent of the global gross domestic product (GDP). Deplorably, the financing gaps to achieve a basic level of social protection for everyone increased by approximately 30 per cent after onset of the COVID-19 crisis. In 2020 alone, all low- and middle-income countries would have needed to invest US\$1.2 trillion, or 3.8 per cent of

4 See www.ilo.org/wcmsp5/groups/public/---dgreports/---dcomm/documents/genericdocument/wcms_378996.pdf.

5 These benefits exclude essential health services.

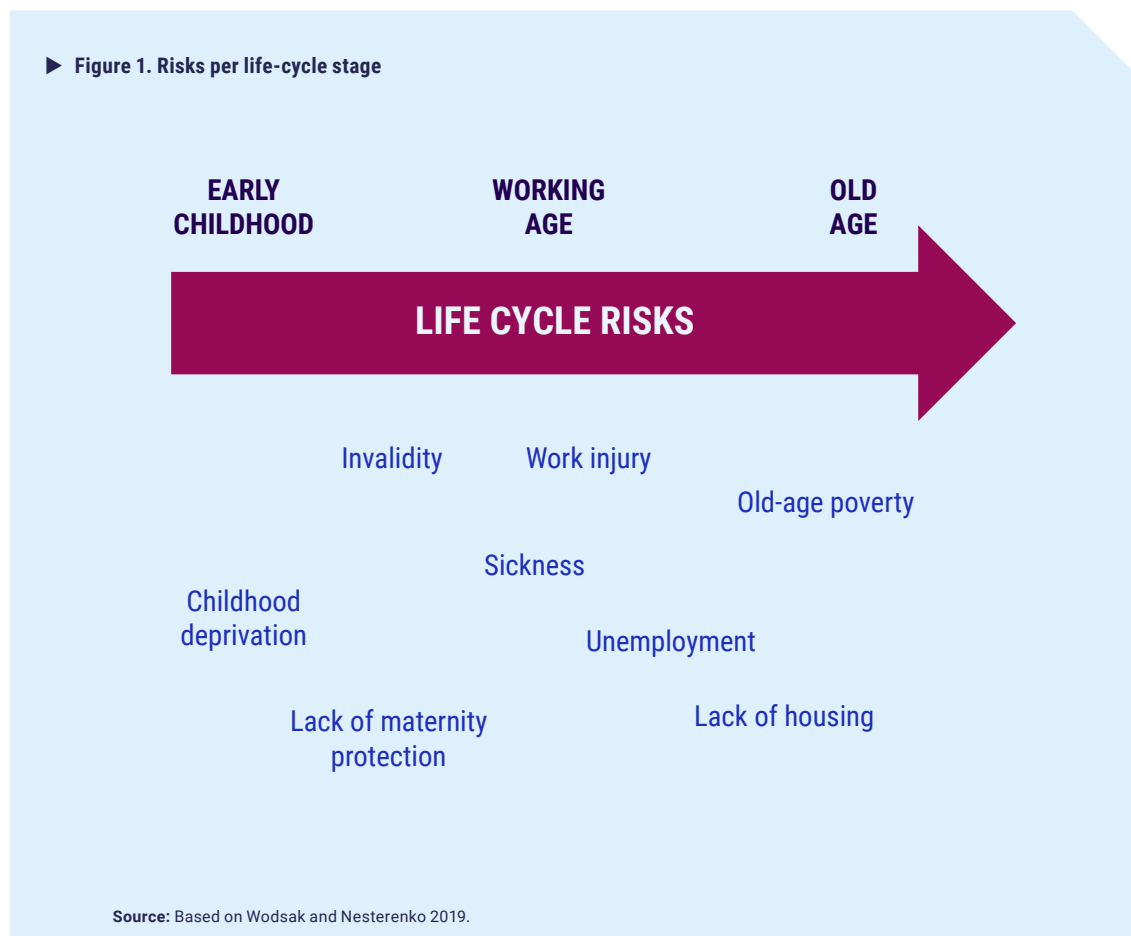
their GDP, to achieve the SDG targets in social protection and health (Durán-Valverde et al. 2020).⁶ These figures summarize the required fiscal space creation that is needed to achieve universal coverage.

The potential options, the methodological possibilities to estimate the required revenues and the factors influencing the feasibility of each alternative represent the spirit of the fiscal space tool.

Life contingencies and the life-cycle approach

All men and women in the world are exposed to a range of contingencies that may affect their well-being throughout their life. This is true regardless of the individual characteristics or socio-economic conditions of each person. Risk exposure is a permanent condition (Bonilla and Gruat 2003) and is known as the life-cycle approach. According to the OECD (2019), the life-cycle approach to social protection focuses on the idea that individuals face different types of risks and vulnerabilities at different moments of their lives, and thus there is need to tailor specific social protection interventions to minimize the effects of such risks in case they materialize.

Risks over the life cycle are numerous and of the most diverse nature. These manifestations may take the form of sickness, unemployment, work injury, maternity, invalidity (disability), death of the breadwinner, poverty due to family changes and old age-related conditions. Although some of these risks are specific to age and gender, there is another aspect that cannot be neglected: some subgroups may be more exposed than others (more vulnerable). Thus, the incidence and effects of life contingencies are not equally distributed across and within population segments. Figure 1 accents some of the risks identified as part of the life-cycle approach. The fiscal space tool intends to help countries find alternatives for financing their social protection programmes and avoid the risk that these contingencies remain uncovered.



⁶ Note that these estimates include health services.

Concept of social protection

The existence of permanent risks over the life cycle as well as the existence of multiple sources of risk (economic and financial crises and climate-related risks)⁷ make the case for social protection initiatives that reduce or eliminate the negative consequences of the materialization of those risks. Although a large share of these conditions has an individual nature, there are also covariate risks that take the character of collective risks, as is the case with disasters or climate change or conflict-induced social risks. Such concepts like adaptive social protection (Davies et al. 2008) and climate-responsive social protection (Kuriakose et al. 2013) now integrate climate change, disaster risk reduction and poverty reduction into single frameworks aimed at facilitating adaptation, mitigation and climate resilience (Costella et al. 2023).

According to the Universal Social Protection 2030 call to action, social protection is “a nationally defined system of policies and programmes that provide equitable access to all people and protect them throughout their lives against poverty and risks to their livelihoods and well-being”.⁸ The Core Diagnostic Instrument (CODI) tool (ISPA 2014: 7) defines social protection as:



...the set of policies and programs aimed at preventing or protecting all people against poverty, vulnerability and social exclusion throughout their life cycles, with a particular emphasis towards vulnerable groups.”

From an integrated perspective, social protection pursues several objectives: (a) compensate for loss of income; (b) facilitate access to social services and fulfil basic needs; (c) cover healthcare expenditures to avoid catastrophic effects due to sickness; (d) help build up the resilience of poor and vulnerable households by investing in their capacity to prepare for, cope with and adapt to shocks to ensure that they do not fall (deeper) into poverty (Bowen et al. 2020: vii); and (e) facilitate livelihood transformations; compensate for negative impacts of climate change responses; contribute to human development and productive outcomes; and increase equity, inclusion and social justice (Costella et al. 2023)

In a similar perspective, the World Bank describes the mission of social protection in terms of helping “the poor and vulnerable [households] cope with crises and shocks, find jobs, invest in the health and education of their children and protect the aging population”.⁹ The World Bank expanded this approach by considering the importance that social protection schemes may have on the improvement of people’s resilience and by promoting opportunity because it supports the construction of human capital and access to jobs and assets.

7 According to Holzmann (2001), “The capacity of individuals, households and communities to handle risk and the appropriate risk management instrument to be applied depend on the characteristics of risks: their sources, correlation, frequency and intensity. The sources of risk may be natural (for example, floods) or the result of human activity (for example, inflation resulting from economic policy); risks can be uncorrelated (idiosyncratic) or correlated among individuals (covariant), over time (repeated) or with other risks (bunched); and they can have low frequency but severe welfare effects (catastrophic) or high frequency but low welfare effects (non-catastrophic). The main sources of risk and the degree of covariance can range from purely idiosyncratic (micro or individually specific), to regionally covariant (meso), to nationwide covariant (macro) events.”

8 See <https://usp2030.org/#why>.

9 See www.worldbank.org/en/topic/socialprotection/overview#1.

Principles of social protection financing

To fulfil the objectives, the financing of social protection should be guided by the following Universal Social Protection 2030 principles.

- ▶ It should take a rights-based approach and be guided by international social security standards.
- ▶ The State is the primary actor for social protection financing and implementation. It should follow six priorities:
 - assign greater priority to social spending within government budgets;
 - enhance the progressiveness and effectiveness of the tax system to increase tax revenue and ensure equity in financing efforts;
 - increase revenue from social insurance contributions by expanding coverage of uncovered workers;
 - improve efficiency and transparency of public financing across all relevant levels and agencies of the government and partners;
 - ensure adequate provision of shock-responsive financing; and
 - engage in inclusive social dialogue to determine the reforms and financing of social protection.
- ▶ International resources should support the expansion of social protection systems in countries with limited fiscal space. This can be done through:
 - increased and better coordinated international financial support for social protection;
 - debt relief and restructuring;
 - international tax reform to increase revenues; or
 - coordinated international policy advice.

In addition to these principles, it is necessary to add the importance of seeking comprehensive approaches to the creation of fiscal space. This means supporting countries in the processes for institutional redesign, strengthening their human resources and improving their governance models to progressively raise domestic resources, which is the most sustainable form of financing the long-term operation of a social protection system.

Risks and social protection functions

Table 1 shows the responses of social protection programmes to different risks over the life cycle. During the early stages of life, risks mostly associate with poverty, access to education, health care, nutrition and costs related to child-raising (food, medical care, etc. even before schooling begins) and because time spent by working-age adults, especially mothers, caring for children takes time away from earning an income. Then, at working age, the relevant risks are mainly linked to unemployment, invalidity (disability), employment injury and occupational diseases, maternity protection and sickness. Finally, at old age, the government responses should protect the population from inadequate material conditions (poverty) through pension schemes, healthcare services and long-term care. In addition to individual-based risks, social protection should also pay attention to collective risks (natural disasters, conflicts, etc.) to support the adaptation of individuals and families to shocks so as to avoid falling into poverty.

Following Hagemejer (2003), table 1 defines the link between life-cycle risks and the expected social protection policy responses. There are 12 critical risks, each of them associated with a list of possible interventions, including cash benefits, healthcare services, special grants and in-kind benefits.

Table 1. Social protection functions and potential policy responses

Main functions	Possible policy responses
Sickness	Prevention and health promotion Primary healthcare Other healthcare
Disability	Disability pensions and cash benefits Disability benefits in-kind Caregiver benefit or credit Other cash benefits (including tax benefits), residential care, day care and rehabilitation, home help services and other)
Death of the breadwinner	Survivors' pension (widows, widowers, orphans) Survivors' cash benefits Survivors' benefits in-kind Other cash benefits (death grant, other), funeral expenses, etc.
Employment injury	Temporary cash benefits to the insured Disability pensions to the insured Other cash benefits to the insured Survivors' pensions Other cash benefits to survivors Employment injury benefits in-kind Healthcare and physiotherapy Rehabilitation (professional) and support for labour market re-entry Other benefits in-kind (prosthesis, etc.)
Poverty during old age	Old-age pensions and cash benefits Old-age benefits in-kind Other cash benefits Accommodation, care, transportation and mobility, etc.
Risk of poverty of families with children	Birth grant Family or child allowance cash benefits Family benefits in-kind Other cash benefits (including tax benefits) Day care, accommodation, home help, other
Unemployment	Unemployment cash benefits (unemployment insurance, unemployment assistance) Early retirement for labour market reasons Labour market training Placement services and job-search assistance Job rotation and job sharing Sheltered work (rehabilitation schemes) Job creation in the public or non-profit sector Start-up incentives
Maternity protection	Maternity and paternity leave benefits Maternity healthcare Parental leave benefit Caregiver benefit or credit
Poverty	Low-income benefits (cash, services) Indigenous persons' benefits (cash, services) Immigrants and refugees' benefits (cash, services) Miscellaneous benefits (cash, services)
Non-standard worker categories	Group-adapted social security schemes, including healthcare, old-age and retirement benefits
Informal economy workers	Maternity benefits Old-age pensions Non-contributory pensions Childcare and allowances Death cover
Persons exposed to and/or affected by climate change, conflict or disasters	Long-term cash transfers Food or food vouchers or stamps Health services

Source: Adapted from Hagemeyer 2003.

There is no single, unified classification for social protection programmes. Cichon et al. (2004) structured the social protection sector around the following groups:

- ▶ **Social insurance schemes and employment-related benefit schemes.** Pensions, short-term cash benefits, employment injury and unemployment benefits are some of the benefits included in this category.
- ▶ **Universal social benefit schemes.** These schemes typically consist of tax-financed programmes for the entire population, including healthcare benefits.
- ▶ **Social assistance schemes.** These initiatives mostly refer to poverty-alleviation schemes.
- ▶ **Supplementary benefit schemes.** These are initiatives sustained by community-based agreements or individual contracts mandated by law.

In short, social protection systems typically address all these policy areas by a mix of public social insurance (paid from employers' and workers' contributions), universal benefit schemes (financed from the government budget) and social assistance (paid from the government budget). However, there is a need to develop and rely on an integrated response framework that entails carefully calibrated and balanced contributory and non-contributory contexts of social protection provisioning.

Social protection and the SDGs

The significant influence that social protection has in the promotion of human development, political stability and inclusive growth makes it a fundamental component in the efforts to achieve the 2030 Agenda, both directly and indirectly.

Direct links are found in five of the SDG targets: target 1.3, target 3.8, target 5.4, target 8.5 and target 10.4 (figure 2). Target 1.3 provides the most straightforward link with the SDG Agenda because it measures the implementation of social protection systems (including social protection floors) and the corresponding population coverage that would benefit from them. The other targets are related to the expansion of health care, decent work (a concept that contains a pillar on social protection) and employment services.

In addition to the direct influence of social protection systems in the 2030 Agenda, there are also indirect links with many other objectives. The OECD (2019b) pointed out that social protection can influence more than 14 of the 17 SDGs, including Goals 2, 4, 6, 12, 13 and 17.

▶ Figure 2. Social protection links with the 2030 Agenda objectives



Source: OECD 2019b.

The fiscal space tool will help countries contribute to the achievement of the SDGs because closing the existing financing gaps in social protection is an enabler to materialize the respective policy approaches.

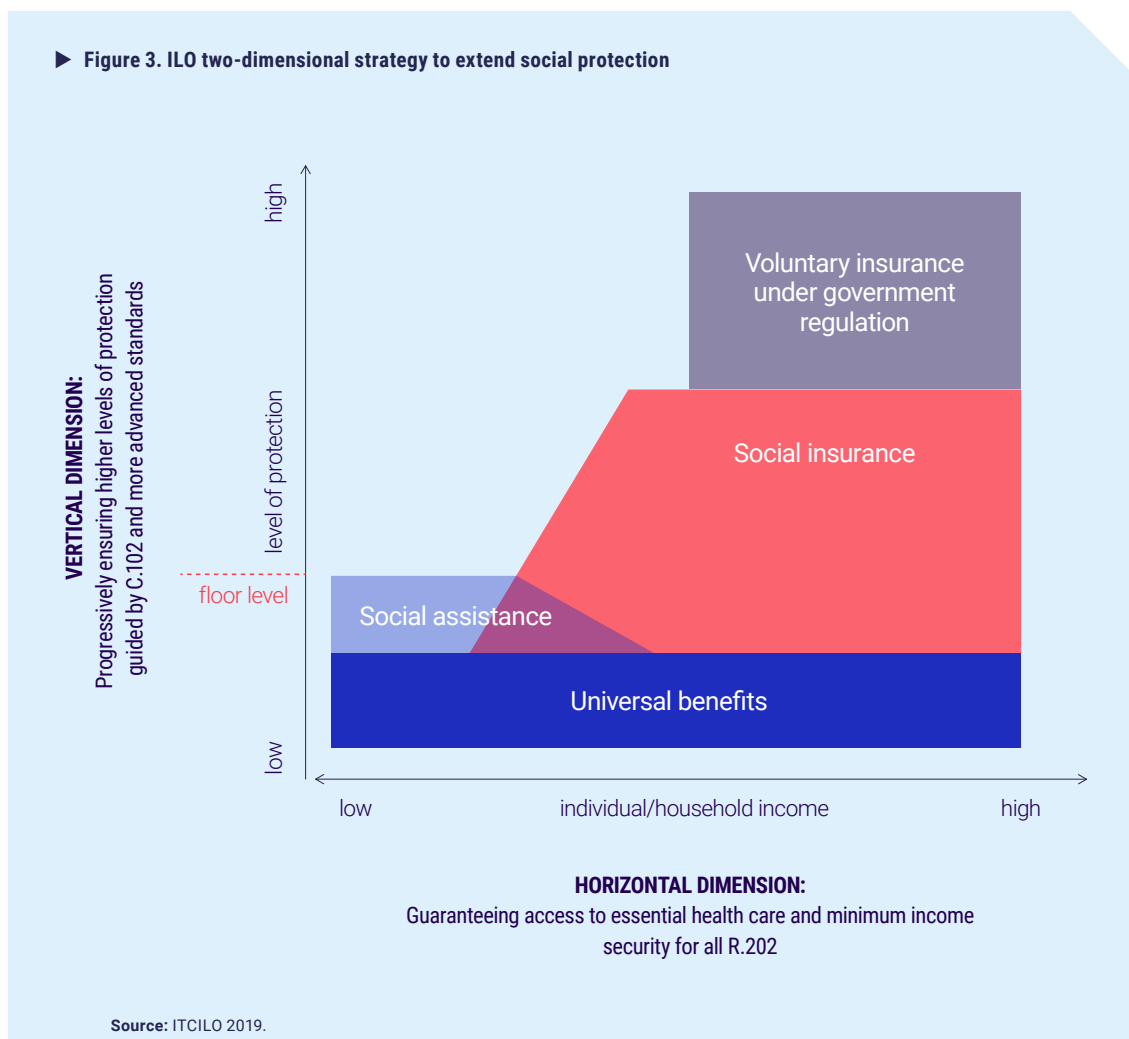
Social protection floors

The ILO strategy on the extension of social security across countries follows a two-dimensional approach as per the considerations that emerged from the 100th Session of the International Labour Conference in 2011, the Resolution concerning the second recurrent discussion on social protection (social security) as well as the ILO Centenary Declaration for the Future of Work (2019) that confirmed the mandate and deepened the vision of universal social protection.

The first realm, the **horizontal dimension**, aims at the rapid implementation of social protection floors with basic social security guarantees that allow the population to access healthcare services and a minimum income level. This dimension is anchored in the Social Protection Floors Recommendation, 2012 (No. 202).

The **vertical dimension** (second component of the strategy) deals with higher levels of protection within a comprehensive social security system according to Convention No. 102 on social security and reinforced by Recommendation No. 202. Figure 3 summarizes the described approach.

The fiscal space tool has the advantage that it contributes to both the horizontal and vertical dimensions. Although this approach is useful for the purposes of this tool, more complex approaches may be required now that additional factors like climate change are added to the discussion on the role and operation of social protection. The need for a carefully balanced, integrated and calibrated social protection response framework to inform social protection provisioning is still imperative.



The core of the strategy is the concept of a social protection floor. According to paragraph 2 of ILO Recommendation No. 202, social protection floors are “nationally defined sets of basic social security guarantees which secure protection aimed at preventing or alleviating poverty, vulnerability and social exclusion”. At the least, any social protection floor should include the following guarantees:

- ▶ access to essential healthcare, including maternity care;
- ▶ basic income security for children, providing access to nutrition, education, care and any other necessary goods and services;
- ▶ basic income security for persons in active age who are unable to earn sufficient income in cases of sickness, unemployment, maternity and disability; and
- ▶ basic income security for older persons.

There are three aspects that must guide the design and definition of a social protection floor: First, a social protection floor eschews a one-size-fits-all recipe, meaning that the design and implementation strategy is context-specific and the result of decisions reached through social dialogue. The second consideration, in line with the previous, is that a floor is nationally defined, depending on countries’ social and economic circumstances and the current state of the social protection system, among other aspects. Third, each country decides on the best combination of social protection options to cover its population.

These alternatives may take the form of targeted or universal schemes, contributory or non-contributory schemes, cash or in-kind instruments or any combination of them. In summary, a social protection floor should be envisioned as a nationally defined minimum level that should be extended to all persons. From the vertical dimension perspective, the social protection floor is the first step in the process. It is then followed by higher levels of benefits and enhanced coverage of more branches. The horizontal and vertical extensions may be implemented simultaneously, depending on the political and fiscal conditions of the country, although as new elements are included in the discussion about social protection (social risks, life-cycle risks, income-related risks, livelihood risks), the need for a new framework increases.

2. Methodological approach to assess the public finance situation

This chapter explains the different components of fiscal space analysis for social protection financing. Two issues are important to clarify at this point: first, the basic concept of fiscal space applies to any type of public expenditure. No matter if the analysis focuses on education, environment, housing or culture, all these sectors can be subject to fiscal space considerations. Although the chapter largely focuses on fiscal space for social protection, the root of the concept and process is practically the same for all sectors.

Second, there is a clear division between fiscal space for contributory and non-contributory programmes. Typically, social contributions are fully earmarked to social insurance schemes that include healthcare, pensions and employment injury. Non-contributory programmes are mostly financed with taxes, either general or specific ones.

On the concept of fiscal space

Heller (2005: 3) provided one of the most well-known concepts of fiscal space, defining it in terms of “the availability of budgetary room that allows a government to provide resources for a desired purpose without any prejudice to the sustainability of a government’s financial position”.

Since then, a range of similar definitions have appeared with more or less the same orientation. For instance, in its 2006 *Interim Report on Fiscal Policy for Growth and Development*, the Development Committee (2006: 14) defined fiscal space as “the gap between the current level of expenditure and the maximum level of expenditures a government can undertake without impairing its solvency”. Ostry et al. (2010: 6) uses a similar approach when stating that fiscal space is “the difference between the current level of public debt and the debt limit implied by the country’s historical record of fiscal adjustment”. Within this vision, the creation of fiscal space is constrained to a limited number of measures, including enhanced efficiency policies, budget reallocation in favour of certain sectors (social protection, for instance) and increased indebtedness, until some point that does not jeopardize the macro balance.

As the discussion of this concept progressed, an extended group of definitions emerged with a focus on the **multidimensional conditions** of the term. Roy and Heuty (2009: 33), for instance, proposed a new concept:



Fiscal space is the financing that is available to [the] government as a result of concrete policy actions for enhancing resource mobilization, and the reforms necessary to secure the enabling governance [and the] institutional and economic environment for these policy actions to be effective for a specified set of development objectives.”

As it is referred to in Ortiz et al. (2019: 9), fiscal space should be seen as an “active exploration and utilization of all possible revenue sources” as well as the measures at the legal and institutional realms to make those options effective.

This new conception introduces at least three changes to the traditional view: First, the creation of fiscal space should have an attached label. In this case, it must be fiscal space for social protection. Second, the creation of fiscal space is a dynamic process in which governments can actively search for additional resources from other channels, going beyond budget redistribution or debt. Taxation, for instance, is considered a critical alternative. Third, fiscal space creation implies both new funding and institutional transformations. In particular, expenditure management arrangements are critical to maximize the eventual impact of the new resources on the population.

Roy and Heuty (2009: 7, 33) emphasized the following issues in relation to fiscal space creation:

1. Domestic resources should be at the centre of any fiscal space strategy.
2. Official development assistance can only be effective if it contributes to an increase in domestic resource mobilization.
3. The context in which reforms are implemented has a major role, given that the sustainability and effectiveness of policy actions depend on the political economy in a country.

Any fiscal space assessment should also consider the broader developmental outcomes. Specifically, it should ensure that the results associated with increasing public spending on social protection may yield positive effects on economic growth, population welfare, environmental sustainability and other related outcomes in line with the 2030 Agenda. In addition, there may be multiplier effects of this spending on public revenues as a result of enhanced long-run growth.

Methodological considerations

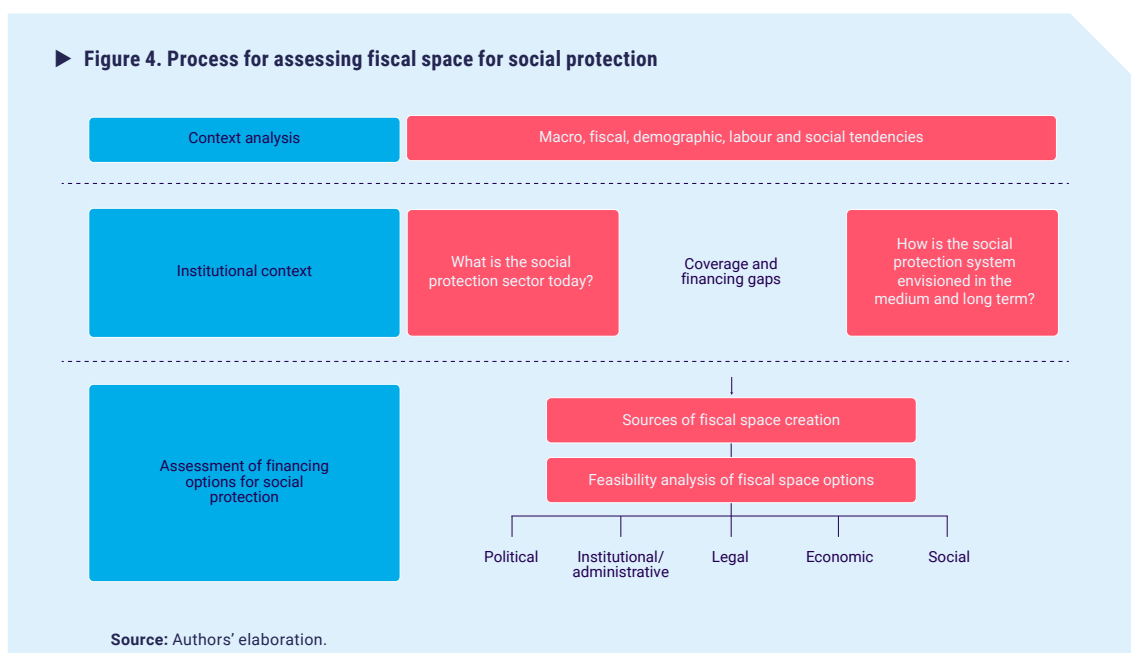
Figure 4 summarizes the overall process to prepare a fiscal space analysis when using this fiscal space tool. The corresponding document should follow the outline and contents specified in Chapter 5 of this tool.

In short, the full process consists of three steps.

Step 1: Context analysis. This stage prepares a detail assessment of the performance of macro, fiscal, labour, social and demographic variables and the way they can influence a country's social protection sector.

Step 2: Institutional context. The analysis here focuses on understanding the main features of a country's social protection sector, including institutional organization, programmes and the performance of such schemes in terms of coverage and financial allocations. The primary outcome of this step is the estimation of the coverage and financing gaps. To construct these gaps, the analysis requires two inputs: (a) an estimation of current coverage rates (per scheme, population group, etc.) and the corresponding levels of investments and (b) the expected situation of the social protection sector at a determined point in the future.

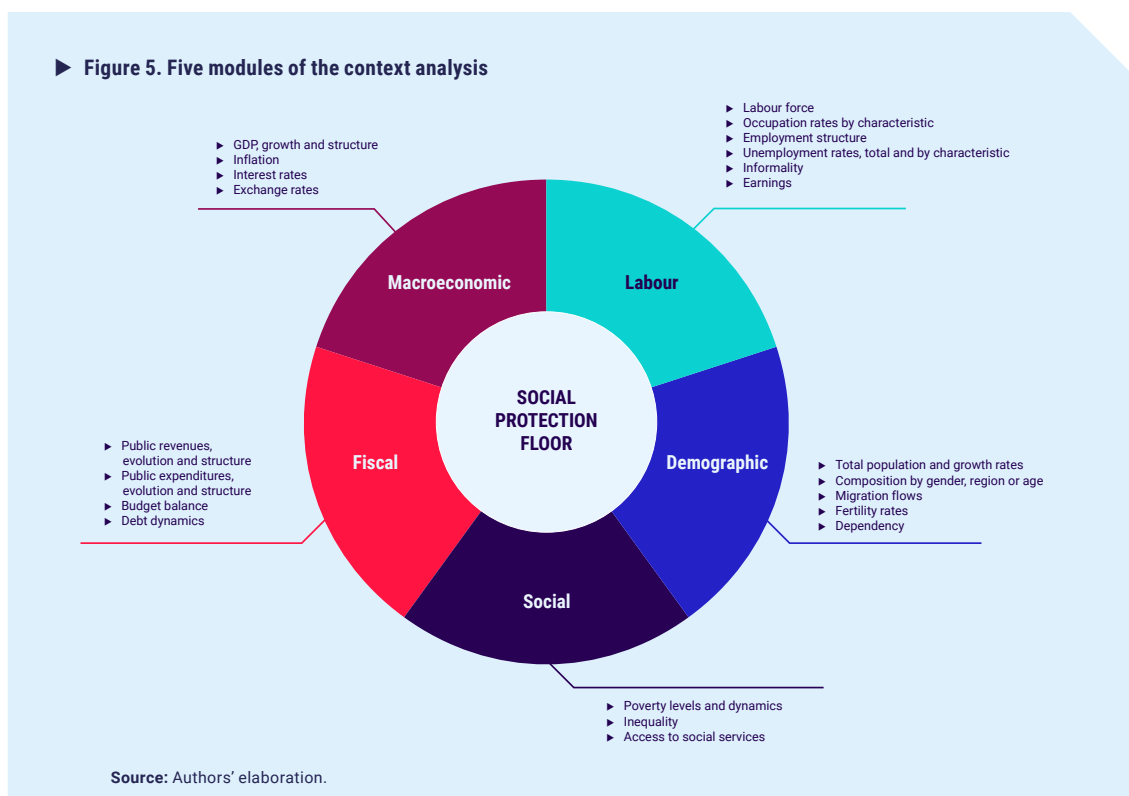
Step 3: Assessment of financing options for social protection. Guided by the results of the previous step, this stage assesses the different fiscal space options from quantitative and qualitative perspectives. The quantitative perspective estimates the potential level of funding that each one of the eight fiscal space options may generate (see Chapter 3). These results are then compared with the financing gap. The qualitative perspective prepares a feasibility assessment whereby each fiscal space alternative is analysed in five dimensions: political, institutional, legal, economic and social. Each step has its own particularities that are explained further on.



Step 1: Context analysis

The first part of the methodology analyses the context, which is an essential input for the overall understanding and feasibility assessment of the fiscal space options. The context analysis involves a deep characterization of the environment in which the domestic social protection sector operates as well as the conditions in which fiscal space can be created.

Figure 5 presents the sections and possible content of each module of the context analysis. In total, at least five modules should be considered: macroeconomic (production and macro prices), labour market, demographic, social conditions and fiscal balance. Some cross-cutting topics, such as gender and climate change, should be considered in each case, although dependent upon data availability.



The first module concentrates on assessing the **macroeconomic conditions** and their connection with the social protection sector. Macro variables to consider in this segment include the size, dynamics and structure of GDP, inflation rates, real interest rates and exchange rates. This module is relevant because the overall performance of the economy may have direct implications for the social protection sector through employment generation, tax revenue collection and poverty reduction.

An important source of information for the budgetary and macroeconomic context will be public expenditure and financial accountability. It provides a framework for assessing and reporting on the strengths and weaknesses of public financial management using quantitative indicators to measure performance. Available national and subnational reports can provide data on the performance of the following areas:

- aggregate fiscal discipline, which requires effective control of the total budget and management of fiscal risks;
- strategic allocation of resources, which involves planning and executing the budget, in line with government priorities aimed at achieving policy objectives; and
- efficient service delivery, which requires using budgeted revenues to achieve the best levels of public services with available resources.

Labour market conditions are relevant to understand the evolution of such critical variables as employment, unemployment and earnings. There are multiple connections between the labour market and social protection that should be considered in this module: First, salaried persons may constitute the main source of social insurance financing. Thus, the number of salaried workers and associated earnings provide information for social protection funding.

Second, self-employed persons are usually associated with informality, which is an important topic for social protection policies and programmes. Indeed, in a long list of countries, informality accounts for the majority of employed persons.¹⁰ According to the latest ILOSTAT data, self-employed persons represented, for example, 77 per cent of total employment in sub-Saharan Africa in 2021.

Third, topics around the participation or exclusion of women in the labour market are highly pertinent. Participation rates, wage differentials by gender, unemployment rate and rate of economic inactivity are some of the issues that should be assessed in this second module.

Fourth, unemployment presents serious challenges for social protection because it is a life-cycle risk.

Fifth, although not always considered in social protection analysis, persons outside the labour force (people not occupied or unemployed) can provide relevant information on possible barriers that women face in entering the labour market. As a result, care services may become relevant in the discussion of the portfolio of benefits.

Information for preparing this module includes the following:

- ▶ labour force and participation rates, total and by group (gender, zone, age, poverty status or wealth assets);
- ▶ occupation rates, total and by group (gender, zone, age, poverty status or wealth assets);
- ▶ employment disaggregated by status (employees, self-employed, salaried);
- ▶ occupation by branch;
- ▶ occupation by job classification;
- ▶ unemployment, total and by group (gender, zone, age, poverty status or wealth assets);
- ▶ out of the labour market, total and by group (gender, zone, age, poverty status or wealth assets); and
- ▶ evolution of earnings, especially work-based ones.

The third module analyses the **demographic structure**. As in the previous module, there are several ways to approach the connection with social protection. For example, changes in the population pyramid may provide evidence of ageing processes observed in the country and the pressures this may be exerting on certain programmes, such as old-age pensions. Population distribution by age, gender and place of residence (urban or rural) also become relevant for programme design and financing. For instance, childbearing women tend to use health services in a more intensive way. Children, especially those in their early years, also demand health services more than other population groups. Finally, migration has a critical role in social protection because migrants may become both contributors to the system and a source of benefit and service demand. The module may require the following data for its preparation:

- ▶ total population and corresponding growth rates;
- ▶ population distribution by gender and type of place of residence;
- ▶ population pyramid and dependency ratios;
- ▶ fertility rates;
- ▶ migration flows; and
- ▶ disability rates.

¹⁰ According to ILO calculations, informality is above 85 per cent of the total employment in Afghanistan, Angola, Bangladesh, Benin, Burkina Faso, Burundi, Cambodia, Cameroon, Chad, Comoros, Democratic Republic of the Congo, Ethiopia, Guinea-Bissau, Haiti, India, Côte d'Ivoire, Kenya, Lao Peoples Democratic Republic, Liberia, Madagascar, Malawi, Mali, Mauritania, Mozambique, Nigeria, Republic of the Congo, Rwanda, Senegal, Sierra Leone, Sudan, Togo, Uganda, United Republic of Tanzania and Zimbabwe.

Social characteristics and trends are the fourth block. **Poverty and vulnerability** assessments are two of the core topics included in this module because a large share of social assistance interventions are implemented to reduce poverty conditions. Also, the poverty line is a possible criterion of reference established by Recommendation No. 202 for the social protection floor benefits.

The characteristics, extension and volume of required services for social assistance programmes depend on how poverty historically has performed and what are the main characteristics of poor households in terms of average size, composition, sources of income, labour market conditions and other related variables. In addition to poverty assessments, the module may also incorporate other elements, such as analysis of vulnerability conditions.

The following indicators should be collected:

- ▶ poverty incidence and poverty gap rates;
- ▶ poverty incidence by characteristic (age, gender, zone, etc.);
- ▶ multidimensional poverty;
- ▶ life expectancy;
- ▶ mortality rates (general, maternal, child, infant);
- ▶ access to safe water;
- ▶ access to sanitation;
- ▶ education enrolment rates; and
- ▶ other education indicators.

The last module evaluates fiscal performance. This is a critical component for the overall fiscal space analysis because the evolution of public finances may impose restrictions for the expansion of social protection financing. Taxation, public budget distribution and debt dynamics are factors that influence the possible availability of funding through multiple channels, including political economy reasons.

The analysis of domestic fiscal conditions may require the following pieces of information:

- ▶ public revenues, total and by source;
- ▶ public expenditures, total, by sector (social protection, environment, security, etc.) and by accounting category (salaries, transfers, etc.);
- ▶ net fiscal balance, primary and financial; and
- ▶ stock of debt and related repayment conditions.

Step 2: Institutional context

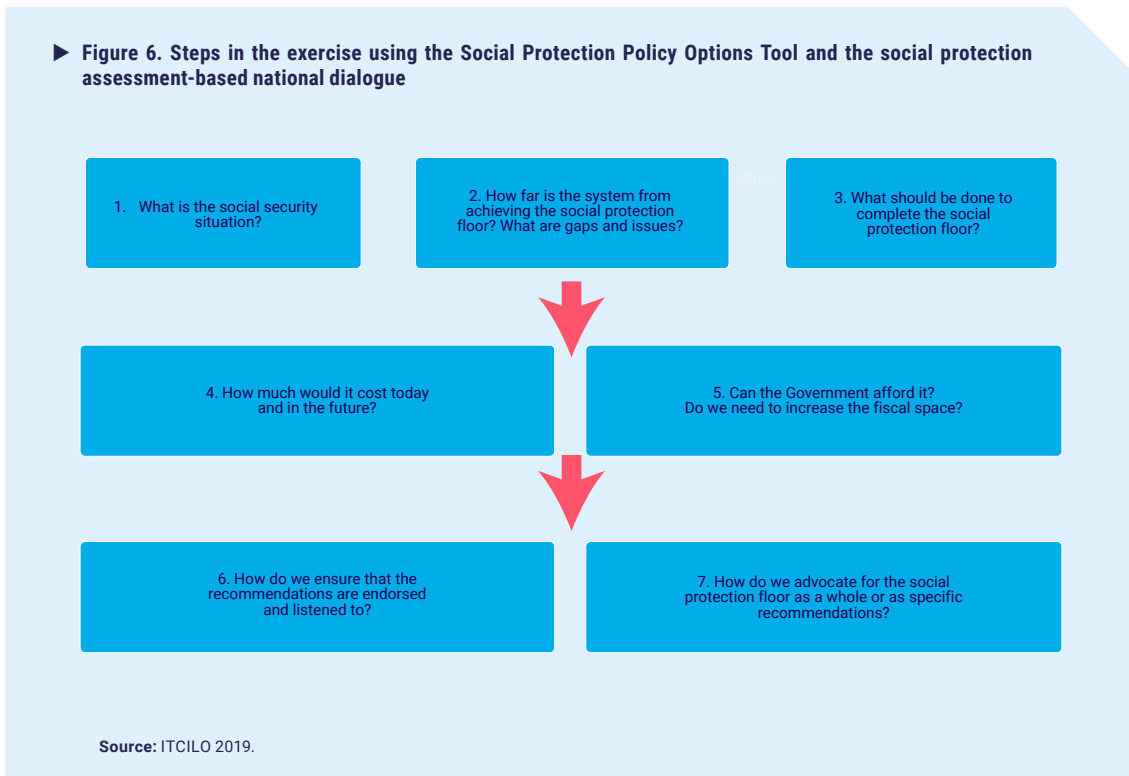
Step 2 aims at collecting information on the level of social protection in the sector and its performance in the recent past. Data about the general organization of the social protection sector, existing programmes, legislation and other normative rules about the institutions and departments that manage the different schemes and quantitative information on coverage and budgets are essential. All this compilation will provide the required inputs to answer the questions of this step:

- ▶ What does the legislation say about social protection in Country X in relation to financing, institutions in charge of administering the schemes, requirements to access the benefits, beneficiary groups, delivery of services and other management practices (accountability, transparency, evaluations)?
- ▶ What are the main characteristics of the institutions that manage the different social protection schemes?
- ▶ What is the number of beneficiaries and how did this figure evolve in recent years?
- ▶ What is the level of spending per programme and how did this figure evolve in recent years?

Step 2 provides the information to construct the baseline with the following issues: (a) coverage rates per population group and/or scheme; (b) total and disaggregated budgetary allocations; (c) average benefit per beneficiary person; and (d) population and financing gaps.

To prepare the outcomes for step 2, the analyst or consultant can rely on the information provided by such tools as the Core Diagnostic Instrument (CODI), the Social Protection Policy Options Tool (SPPOT) and the Social Protection Assessment-based National Dialogue (ABND). The latter two are used together.¹¹

The CODI tool, the SPPOT and the ABND complement each other and provide information on the existing social protection programmes in a country while also identifying alternatives to social protection floors that may be politically attractive and financially feasible. Figure 6 summarizes the steps and activities that this process involves.



Analysis of information using the CODI assessment

According to ISPA (2014: 8):



Countries can use CODI to systematically take stock of their social protection provisions, assess their social protection systems, and identify ways to improve system performance. In addition, CODI should also strengthen country capacities for system analysis, as well as facilitate coordination among international development partners.”

The CODI is mainly interested in (a) mapping in detail all existing social protection schemes, including objectives, policies, strategies, coverage, budgetary allocations and other management practices; (b) evaluating performance per initiative and according to pre-established objectives; (c) being an instrument for social dialogue activities; and (d) providing inputs for the SPPOT and ABND approach in the discussion of social protection floor content and financial implications.

For the fiscal space assessment, the analysis should take a sample of the information generated by the CODI, in line with the programme inventory highlighted in table 2. The fiscal space analysis requires information on actual coverage, total expenditures, risks covered and programme category, as per the CODI definitions.

¹¹ For more details of each exercise, please visit <https://ispatools.org/core-diagnostic-instrument/> for CODI and www.social-protection.org/gimi/ABND.action for SPPOT and ABND.

Table 2. CODI's programme inventory table (sample of variables)

	Programme/ benefit category	Risk covered/ function	Target population	Benefit level and indexation method	Objective	Geographical areas covered	Number of beneficiaries		Total expenditure in local currency	
							Value	Most recent year	Value	Most recent year
Non-contributory social assistance programmes										
	Programme A									
	Benefit 1									
	Benefit 2									
	Benefit 3									
	Programme B									
	Benefit 1									
	Benefit 2									
	Benefit 3									
Contributory social insurance programmes/ schemes										
	Programme A									
	Benefit 1									
	Benefit 2									
	Benefit 3									
	Programme B									
	Benefit 1									
	Benefit 2									
	Benefit 3									
Labour market measures and services										
	Programme A									
	Programme B									
	Programme C									

Source: CODI data collection framework.

Even if a country does not conduct a CODI assessment, the analyst or consultant should access the corresponding online ISPA Tool¹² as a guide on the main elements included in the instrument so they can prepare a similar chapter with the information that the CODI provides. This may imply, however, an important extension in the project schedule that should be considered in an appropriate way.

Social protection floor assessment using the SPPOT and ABND approach

The SPPOT and ABND analysis is the second part of step 2 and takes the information from the CODI assessment, identifies critical gaps in the system and prepares recommendations for achieving a social protection floor. This analysis thus provides the following inputs.

12 See <https://socialprotection.org/discover/publications/core-diagnostic-instrument-codi>.

1. Legal and effective coverage levels, per branch (maternity protection, sickness, old age, invalidity, etc.).
2. Level of effective coverage per population group. Effective coverage gap refers to the difference between the total size of the population and the actual number of beneficiaries.
3. Level of relative coverage per population group. Relative coverage is the percentage of the target population that currently receives the benefit, or the division between beneficiaries and total size of group.

The analyst or consultant at this point should be able to identify potential social protection floor options with different compositions and coverage targets. The regular practice is to first define universal coverage (100 per cent) as the ultimate coverage goal (benchmark) and then to identify intermediate scenarios that may reflect the progressivity needed to reach universalization. These intermediate scenarios are more realistic for policy analysis.

The characteristics of each guarantee are summarized in the assessment matrix outlined in table 3. Two types of recommendations may emerge:

- ▶ recommendations to introduce non-contributory benefits, increase non-contributory benefit amounts and extend coverage; and
- ▶ recommendations to introduce social insurance, work on the coordination between schemes and operations and qualitative recommendations to improve quality of services or delivery.

Table 3. SPOT and ABND assessment matrix

	Social protection floor objectives	Government strategy	Existing provisions	Policy gaps	Implementation issues	Recommendations
Health	Four social protection floor guarantees	Identifying existing situation in the country		Identifying policy gaps and implementation issues, addressing which would complete the social protection floor		Priority policy options, decided through national dialogue
Children						
Working age						
Older persons						

Source: ITCILO 2019

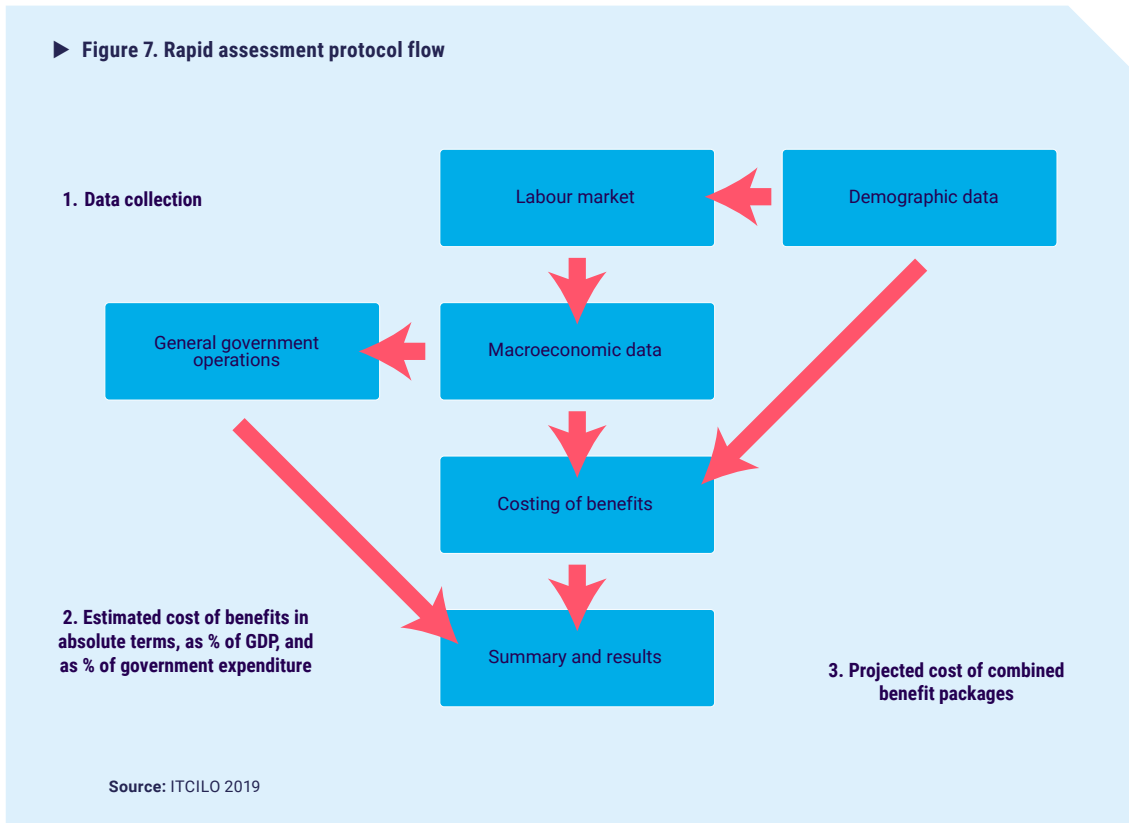
After completing the description of the baseline situation, the next step entails estimating the **coverage and financing gaps**. The financing gap refers to the difference between the level of spending under universal coverage (the social protection floor covers all of the population) or any other scenario and the current level of spending in the components of that floor in time. It is expected that any identified scenario proposes coverage rates above the existing situation.

To estimate this gap, the analysis follows the approach of the ILO Rapid Assessment Protocol Social Protection Costing Tool. This is an Excel-based tool that the ILO developed to estimate the cost of providing social protection floor benefits (for healthcare, children, working-age adults and older persons) over a five- to ten-year period.¹³ Conceptually, the model follows the flow indicated in figure 7. Using the information collected for the context (demographic, labour, macroeconomic and fiscal), the rapid assessment produces cost estimates of the actual and the proposed benefits for each social protection floor scenario. The analysis defines scenarios of expanded coverage above the baseline situation. This

13 The rapid assessment protocol can be found online at the Quantitative Platform on Social Security platform: qps.ilo.org.

can be a short-, medium- or long-term exercise, although the general practice suggests periods of four to seven years because expanding coverage may need some initial conditions to increase in a sustained way.

The costing of the social protection floor also can be prepared using reform scenarios of actuarial projections that include the extension of benefits financed in part or totally with taxes. The ILO Pensions and the ILO Health actuarial models contain tools for such scenarios.



Mathematically, the financing gap is equivalent to:

$$FG_j = SPFC_j^U - SPFC_j^t \quad (1)$$

where FG_j refers to the financing gap in Country j , $SPFC_j^U$ is the cost of the social protection floor of Country j in the context of universal coverage¹⁴ (target scenario), while $SPFC_j^t$ is the cost in moment $t=1$ of the components that integrate the selected social protection floor (baseline scenario). Given that social protection floors represent a set of guarantees, then the equation can be formulated in the following terms:

$$FG_j = \sum_{i=1}^n TC_{ij}^U - TC_{ij}^t \quad (2)$$

where TC is the total cost of guarantee of i in Country j under universal coverage (U) or in the baseline year (t). The FG depends, therefore, on the existing effective coverage rate for each guarantee, irrespectively if this coverage is ensured through contributory or non-contributory sources of finance.

As an example, assume a total number of 125,000 children in Country X . The existing conditional cash transfer currently covers 25,000 children, or 20 per cent of the group. At US\$75 annual benefit per beneficiary, the total cost of this guarantee under the baseline (current) scenario is US\$1,875,000 (25,000*75). If the proposed situation is to achieve universal coverage, then the cost of the programme in

14 Alternatively, the "universal coverage scenario" can be substituted by a "partial coverage scenario" in the understanding that this partial situation moves the country to a higher level of protection than it is now. The decision of opting for universal or partial scenarios depends on the baseline situation and the time span of the policy that would be implemented (short, medium or long term). In practice, it is usual to first calculate a universal coverage gap and then alternative scenarios of partial coverage.

that condition would be US\$9,375,000 (125,000*75). The corresponding gap to reach universalization is US\$7,500,000.

Although the gap is initially assumed to be the difference between current and universal coverage, it is for each country to decide whether universal coverage is the targeted scenario in, say, five to seven years, with intermediary coverage rates of, say, 30 per cent in two years. The proposed equation can be generalized such that the first component (now with an *) refers to any scenario in which coverage is higher than the current situation of the country, with the decision limited by the starting point (current coverage), main context limitations and fiscal performance:

$$FG_j = \sum_{i=1}^n TC_{i,j}^* - TC_{i,j}^t$$

In short, to estimate each gap, the analyst or consultant should proceed in the following way.

1. To calculate the base scenario, it is necessary to have the total size of the group (projected for the next N years), the existing coverage rate (which will remain the same during the period of analysis), the expected number of covered persons under constant conditions, the benefit per year, the administrative costs, projected GDP and government expenditures. This component aims at responding to the question of where the social protection system is in terms of coverage and spending using data from the CODI assessment, the **ILO Social Security Inquiry**, **UNICEF's social protection reports and social protection expenditure reviews** and other similar exercises.
2. To calculate the target scenario, the analysis requires the same information used in the SPPOT and ABND stage. The first is the definition of the target rate and an assumption of how this rate will move from today to the target value. Second, the analysis should incorporate a price adjustment – it should define whether the benefit will change or not according to inflation. Finally, it is important to set an administrative cost rate. According to Convention No. 102, benefits should be protected against the loss of purchasing power and adjusted on a regular basis by inflation, real wages or a mix of both.

It is important to emphasize here that the share of administrative costs is usually the subject of important discussions, with no single consensus on their optimal value. For instance, for the ILO (2007), administrative costs may be 15 per cent of the total costs of universal programmes and 33 per cent of targeted cash benefits aimed at reaching poor households. However, the United Nations Economic and Social Commission for Asia and the Pacific estimates administrative costs in the range of 5–15 per cent, depending on the complexity of the programme.¹⁵ Regardless of these considerations, it is clear that universal schemes usually experience lower administrative costs than targeted ones. The gap is the difference between the results in the previous point 2 (target scenario) minus the results in 1 (base scenario).

Table 4 illustrates how the template looks for either the baseline or target cases.

¹⁵ See <https://spot.unescap.org/glossary#:~:text=Administrative%20costs%20usually%20range%20between.value%2C%20depending%20on%20its%20complexity>.

Table 4. Gap estimation matrix

	Guarantee Group 1: Children	Formula	Year t-3	Year t-2	Year t-1	Year t	Year t+1	Year t+2	Year t+3	Year t+4	Year t+5
1	Total size of the group	Size of group according to statistical institute estimates									
2	Existing coverage	Size of beneficiaries according to institution who administers program									
3	Existing coverage rate	. = Coverage/total size of group									
4	Target rate	% (decided by consultant)									
5	Total beneficiaries under target rate	. = total size * target rate									
6	Average benefit per person per year in local currency	Number in local currency									
7	Total expenditure, current	. = Existing coverage * average benefit									
8	Total expenditure, target scenario	. = Beneficiaries under target * average benefit									
9	Coverage gap	. = line 5 - line 2									
10	Financing gap	. = line 8 - line 7									
11	Administrative costs	7% to 10% of line 10									
12	Total additional costs/financing gap	. + line 10 + line 11									
11	Gap costs as % of GDP	. = line 12/nominal GDP									
12	Gap costs as % of government expenditures	. = line 12/government expenditures									
13	Gap costs as % of government revenues	. = line 12/government revenues or taxes									

Following the example from the previous page, the total size of the group in the gap matrix illustrations (table 4) refers to the number of children in the country. The target group is, thus, a subsegment of the total number of children, defined in line with what the social dialogue identified for each scenario. Children who live in poor households, for instance, is an example of this subgroup. Actual coverage refers to the number of existing beneficiaries divided by the estimated size of the population. The target coverage refers to the total population size (per group) times the coverage rate that the strategy would like to achieve during the next years.

In terms of cost estimation, the benefits per year refers to the total amount of funds that each beneficiary child receives in a year multiplied by the total number of expected beneficiaries (in thousands or millions). In addition, the administrative costs multiply the financing gap times a factor that usually ranges between 7 per cent and 10 per cent, depending on the characteristics of the country. The exercise usually assumes a constant rate, although these outlays are not linear at different coverage rates due to economies of scale and other determinants. The coverage and financing gaps refer to the difference between target beneficiaries versus actual beneficiaries and target costs versus actual costs, respectively. Total additional costs are the sum of the financing gap plus administrative costs.

For analytical purposes, the exercise may estimate three additional indicators: (a) total additional costs as a share of GDP; (b) total additional costs as a share of government spending; and (c) total additional costs as a share of government revenues or taxes (or both).

Step 3: Assessment of financing options for social protection

This stage encompasses the fiscal space analysis, which is the assessment of potential sources of funding for social protection purposes. This segment includes the estimation of additional resources per alternative option (given some parameters), the contribution of each alternative to closing the financing gap and a feasibility evaluation in economic, legal, political and institutional terms. Because this is the core subject of the IPSA Fiscal Space Tool, the following chapter is dedicated to this analysis.

3. Estimating fiscal space: Conceptual, methodological and analytical factors

This chapter elaborates on how to analyse the alternative options for the creation of fiscal space for social protection. For each alternative option, the fiscal space tool covers four aspects:

- ▶ rationale of the intervention (concept);
- ▶ method of estimation;
- ▶ sources of data; and
- ▶ special issues to consider.

Fiscal space for social protection: Options

Ortiz et al. (2019) identified eight potential sources of fiscal space for social protection. These eight sources represent a mix of alternatives that combine domestic and external sources, traditional and non-traditional and revenue-based and expenditure-based options:

1. **Expanding social security coverage and contributory revenues.** This option may take the form of expanding coverage (among salaried and independent workers), increasing contributory rates or a mix of both.
2. **Increasing tax revenue.** As in the previous case, fiscal space can be created by expanding the base, increasing existing rates, approving new taxes, reducing tax expenditures (exemptions) and reducing evasion.
3. **Eliminating illicit financial flows.** This alternative includes estimating the flows going out of the country in terms of money laundering, bribery, tax evasion, trade mis-invoicing and other financial crimes.
4. **Reallocating public expenditures.** This alternative does not create new funding, but it basically promotes the movement of resources from one sector to another or improvement in the internal level of efficiency of the social sector. This may include replacing high-cost, low-impact investments with those that have larger socio-economic impacts, eliminating spending inefficiencies and/or tackling corruption.
5. **Using fiscal and central bank foreign exchange reserves.** This includes meeting temporary additional needs using 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.
6. **Managing debt – borrowing or restructuring sovereign debt.** This involves an active exploration of domestic and foreign borrowing options at low cost, including concessional loans, following a careful assessment of debt sustainability. Other options include restructuring existing debt.
7. **Increasing aid and transfers.** These transfers refer to the flow of funds coming from international agencies, governments and other entities for developmental purposes.
8. **Adopting a more growth-oriented macroeconomic framework.** This option aims at promoting a macroeconomic approach to promoting growth and decent jobs without the inflationary spirals that can jeopardize the overall macroeconomic sustainability.

Expanding social security coverage and contributory revenues

a) Concept

According to Ortiz et al. (2019: 55) social contributions are “a prior payment that is directly linked to protection guarantees (acquired rights and entitlements) through insurance mechanisms”. In a similar way, the OECD¹⁶

¹⁶ See [https://data.oecd.org/tax/social-security-contributions.htm#:~:text=Social%20security%20contributions%20are%20compulsory,\(contingent\)%20future%20social%20benefit.](https://data.oecd.org/tax/social-security-contributions.htm#:~:text=Social%20security%20contributions%20are%20compulsory,(contingent)%20future%20social%20benefit.)

defines social contributions as “compulsory payments paid to general government that confer entitlement to receive a (contingent) future social benefit”.

Based on the considerations defined in ILO Convention No. 102 on social security, social contributions should be aimed at covering guarantees for maternity protection, unemployment support, employment injury benefits, sickness benefits, health protection (medical care), old-age benefits, invalidity (disability) benefits and survivors’ benefits. The OECD includes a larger list of benefits, such as unemployment insurance benefits and supplements; accident, injury and sickness benefits; old-age, disability and survivors’ pensions; family allowances; and reimbursements for medical and hospital expenses or provision of hospital or medical services.

In addition to the positive effects on population protection, social security contributions are also favoured on the grounds of their redistributive effects. A first redistributive effect comes from employers to workers because contributions represent a transfer of funds for covering employees, usually financed by both employers and workers. Second, social security contributions often entail a subsidy that goes from healthy to sick persons, from young to old persons, from rich to poor households and from families without children to families with children.

b) Method of estimation

Increased contributions from social insurance may be the result of the following three possible policies (either individually or simultaneously): The first one considers increments in the contribution rates (Policy 1). Setting the contribution rates should be done at a level that allows for expanding coverage. Convention No. 102 requests that an actuarial study be produced when a reform modifies the rates of contribution of a social insurance system. Therefore, this is not an arbitrary option to increase funds to subsidize informal workers but needs to be part of an approach that combines a formalization policy and/or the extension of legal coverage. The actuarial study needs to set the contribution rates at a level that allows for the incorporation of the new persons and for the scheme to continue or become sustainable.

The second policy refers to extended coverage of informal dependent workers in formal firms (Policy 2). In Latin America, for instance, about 30 per cent of the workers in formal companies can be considered informal; that is, they work on a regular basis with the firm, but they are not reported as such to the social security entity. From a fiscal space perspective, this situation may take the form of new contributors because firms are declaring them for the first time or they are newly hired employees. This type of initiatives may expand fiscal space, although the collected funds may be used only to finance social security benefits and not other types of schemes, like social assistance.

The third alternative points to increasing coverage of informal workers (Policy 3). It is important to underline here that the fiscal space effects of coverage extension differ depending on the labour group considered. There are several points to consider in relation to these policies: First, increased coverage policies may refer to groups that legislation already includes but with coverage well below universalization. Second, the policy may opt to expand legal coverage of those groups not formally included in the existing laws. This decision may have, from a fiscal space perspective, different effects. If the focus is on workers with a significant level of income (managers, professionals, military, etc.), this will probably increase revenues. However, if potential beneficiary groups are the more vulnerable ones (domestic workers, agricultural workers, workers in small and medium-sized enterprises, etc.), then additional net revenues may not increase substantially, at least not in the short run, for different reasons: (a) affiliation of these categories usually increases at a slow pace; (b) their contributions are low and frequently require cross-subsidization; (c) they need adaptations of the administrative mechanisms, which increases the administrative costs; and (d) they will possibly present a historically not-served need of social protection benefits and services, hence they probably will present a higher-than-average take-up rate and constant fluctuations, at least at the beginning.

Therefore, the extension to low-income segments will not bring a high level of revenue, and it should not be seen as a major source of finance. Rather, the formalization of average and higher-than-average wage earners as well as the correct setting of contribution rates may offer better alternatives for these purposes.

Finally, regarding efforts to increase the level of social contributions, it is important to incorporate at least two additional topics: The first is the potential fund recovery coming from such practices as wage

under-declaration. The second one explores the possible existence of debt between the central government and the social security institute, a situation that is frequently observed in assessed countries.

The following mathematical expression can be considered as the base equation for estimating the previously referred situations. In short, the four components of the base equation involve:

$$SC_t = \sum_{i=1}^N TG_{i,t} * ALE_{i,t} * CovR_{i,t} * ContrR_{i,t}$$

where for the N contributory groups (wage and salaried workers and self-employed persons) in a social regime, the expected revenue collection from social contributions is the result of multiplying the size of the specific group (TG) times the average labour income (annual basis, or ALE) times the contributory rate (ContrR), times the coverage rate (CovR).

The same equation applies whether the objective is to estimate contributions for healthcare, pensions or any other guarantee.

Each one of the previous situations may have its own adjusted equation. For instance, in the case of Policy 1, there is a risk of declining or decelerating contributions due to increments in the contributory rate. This may be the result of an adverse reaction in the number of enrolled persons (declining coverage rate) or in the reported earnings.

It is important to emphasize that these changes may or may not materialize. Thus, it is up to the analyst or consultant to decide how to incorporate them into the final computation. The final possible effects depend on the strength of the enforcement mechanisms available to the social insurance administration. The risk of declining contributions is also likely to depend to some extent on structural factors, such as the contributory capacity of new groups who are being covered. For some groups with low and irregular incomes who do not have a clear employer and face a double contributory challenge (some self-employed workers), state subsidies are critical to sustain their contributions.¹⁷

The modified equation in this case may take the form of:

$$SC_t = \sum_{i=1}^N TG_{i,t} * ALE_{i,t}^{Adj} * CovR_{i,t}^{Adj} * New ContrR_{i,t}$$

where New ContrR reflects the new contributory rate while ALE and CovR are adjusted according to the expected response to the increasing rate.

The second policy assumes increasing coverage of salaried workers. In this case, the base equation only observes a change in one parameter – the coverage rate of dependent workers – so it now reads as:

$$SC_t = TG_t^{Salaried} * ALE_t * CovR_t^{Adj} * ContrR_t + TG_t^{self} * ALE_t * CovR_t * ContrR_t$$

Only one parameter (coverage rates of salaried workers) changes while all the components on the side of the independent workers remain unaltered.

Policy 3 assumes increasing coverage of independent workers. Given that the international experience shows that these types of policies usually require government subsidies for an effective implementation, this alternative yields a new base equation:

$$SC_t = [(TG_t^{Self} * ALE_t * CovR_t^{Adj} * ContrR_t) + PublicSub_t] + TG_t^{Salar} * ALE_t * CovR_t * ContrR_t$$

¹⁷ There is no strong evidence that supports the idea that social insurance revenues fall with growing rates or that increasing rates are the main explanation for informality and job creation.

This mathematical formula now includes a new coverage rate for independent workers and one additional item for public subsidies to support self-employed affiliates.

In some other instances, two topics may be of interest when talking about social security and financing: The first is contribution gaps. The second refers to existing public and private debts with the social security institutes.

Contribution gaps aim at measuring the difference between actual total contributions and the potential level of contributions if all employed persons in the economy were affiliated. Under-contributing may come from either a reduced number of affiliated workers or from underreported salaries and earnings. The corresponding equation may take the following form:

$$CG_t = (TSW_t - TSAW_t) * (AW_t) + (TIW_t - TAIW_t) * (AIRE_t)$$

where TSW and TSAW refer to total salaried workers in the economy and total salaried affiliated workers, while AW defines the average salary. Similar considerations emerge in the second part of the equation where TIW and TAIW are, respectively, total independent workers and total affiliated independent workers. AIRE refers to average independent reported earnings. Some parameters, such as the total number of salaried and independent workers and the average wages and independent earnings, may come from such sources as household surveys or labour market surveys.

At this point, in specific contexts, a reduced contribution rate may apply for some sectors as an incentive to promote certain activities. Reduced rates act here as “tax expenditures” and may be used as part of broader industrial policies. In general, however, it is not a good idea to use this type of measure to incentivize determined activities.

In the case of the debt with the social security, the figure is usually calculated by the institution. A review of mechanisms to effectively claim it and a comparison with how debt recovery may improve the performance of the social security system can be a good complement to the analysis. In several situations, the amount calculated is not realistic for many reasons. Sometimes, the debt-filled companies do not exist anymore, their goods and funds have disappeared or their payment schedules need to foresee a long period of instalments to allow them to recover from a crisis. A separate analysis should be done if the debt has a public nature. In those circumstances, in addition to a deep revision of legislation and the characteristics of the debt (due to unpaid contributions by the government as an employer or because the norm created specific responsibilities not fulfilled by the finance ministry), it would be important to discuss the potential mechanisms to recover it.

c) Sources of data

Statistics coming from the social insurance institutions and the national statistics office are usually the most important sources of data. Social insurance organizations may provide information on contributory rates per scheme, current affiliation, affiliation by group, affiliation by gender, coverage rates and reported earnings per group.

The statistics office, on the other hand, may provide information on the size and composition of the labour force and other groups of interest, informal employment, self-employment and earnings among the key variables.

Other sources of information on a specific country's social security features are:

- ▶ [Social security programmes throughout the world](#)
- ▶ [International Social Security Association](#)
- ▶ [ILO social protection reports](#)
- ▶ [World Bank, World Development Indicators](#)
- ▶ [IMF, Government Finance Statistics](#)
- ▶ [IMF, World Revenue Longitudinal Data](#)
- ▶ [Eurostat social protection statistics](#)
- ▶ [OECD social security contributions](#)

Some surveys may also provide information on wages, self-employed earnings and the size of the different labour categories that may be useful to calculate the salary mass by a specific group. Labour Force Surveys, Household Surveys and the Global Wage Report may be good references.

d) Special issues to consider

The following highlights some critical topics that could be part of the discussion around social contributions as a fiscal space creator.

- ▶ Social security contributions are less flexible than taxation in their use across the different social protection interventions. As an earmarked revenue, funding is utilized to cover the financial needs of the specific guarantee for which they were collected. So, if there are financing gaps in other areas (social assistance, for example), they should not be filled with revenue coming from social contributions.
- ▶ Although increasing the contributory rate is usually the first option to consider when assessing new fiscal space, there are many other areas that should be assessed. For instance, extending both the legal and effective coverage may be a good alternative with less political reactions and better social outcomes.
- ▶ In most countries with established social security systems, there is an intensive debate on whether social contributions affect competitiveness, employment and growth. This is not a minor issue, and depending on the actual labour cost that the social contributions represent, the feasibility of creating fiscal space through this channel can be eroded. Social dialogue becomes a critical tool in the search for consensus and joint decisions, facilitating the achievement of national agreements. Also, there is a need to strengthen the capacity of enforcement of the contributions, which depends on labour market inspection institutions.
- ▶ Along similar lines, efficiency in revenue collection and compliance may pose a barrier to other reforms. If the social security institution has weak mechanisms to recover debt or to control evasion, then the possibility of increasing contributory rates may be weakened.
- ▶ Focusing on informal employment and the policies needed for formalizing informal workers is perhaps one of the most hotly debated topics today. Emerging research in the field shows no link between increased contribution rates and informality rates.
- ▶ From a financing perspective, coverage of informal workers yields at least two critical issues: The first is the need to consider public subsidies as a tool to support affiliation of this particular group, something that exerts pressure on government expenditures. However, as self-employed affiliation increases, the tax base expands, creating in this way a virtuous cycle due to increased government revenues.

Increasing tax revenue

a) Concept

Taxation is one of the two largest sources of social protection financing, along with social contributions. Multiple conditions characterize this option: First, it is a very good source of massive funding; as such, taxes usually contribute a significant portion of the overall sectoral needs. Second, taxes tend to be stable, helping in the long-term establishment of social protection schemes that require sustained sources of funding to preserve them over time. Third, if well designed, taxes can improve the progressivity of the economic system. Fourth, taxation (except earmarked one, where they exist) is more flexible than social contributions; so, taxes can be more easily assigned to different interventions. Fifth, when social contributions are earmarked to finance social security schemes, taxation usually has a broader scope and may cover all types of social protection programmes.

The analysis of tax-based fiscal space creation may take into consideration at least four broad categories: The first is general taxation, in particular, the potential new resources that may come from value-added tax, the income tax, the corporate tax and some custom taxes or similar levies. Second, specific taxes applied to certain goods and services with a predetermined destination. The list of this option is long but country-specific, so a preliminary brief feasibility assessment should be conducted with relevant stakeholders to discharge those with little chance to be implemented. Third, tax evasion emerges as a critical component because it represents existing resources that legally belong to the public sector but were retained by private agents in an illegal form. Fourth, tax expenditures, meaning “the revenue that is foregone by the

application of benefits or special tax regimes” (Villela, Lemgruber and Jorratt 2010: 2), should also be carefully analysed. Some of these exemptions may not be fair or they may not be cost-effective or cost-beneficial for the society. Hence, their elimination may generate funding for social protection programmes.

b) Method of estimation

This section explores fiscal policy recommendations (especially in terms of revenue) tending to strengthen institutional capacities for the adequate collection of the previously discussed tax revenues. Due to the COVID-19 response impacts on the economy and the fiscal dimension, governments face a challenge to improve revenue collection through a strengthening of their normative and organizational structures, particularly their tax authorities and customs departments.

One way to guide the development of this section is through the so-called **Medium-Term Revenue Strategy**. It is a methodological approach promoted by the Platform for Collaboration on Tax.¹⁸ The Medium-Term Revenue Strategy is “a comprehensive approach for undertaking effective tax systems reform for boosting tax revenues and improving the tax system over the medium term through a country-led and whole-of-government approach”.¹⁹ The strategy has four components:

- ▶ **Revenue and other goals.** In this component, the analysis focuses on estimating the financing needs (required spending) that the government may need in the next few years. In terms of this tool, the estimation of the financing gap fulfils this condition and provides an idea of the required level of resources to finance social protection programmes.
- ▶ **Tax system reform to meet goals.** This component prepares ideas for a road map to transform the system. The analyst or consultant should review and assess the main components of the system, including tax policy, revenue administration and the legal framework to identify specific measures in each component.
- ▶ **Sustained political commitment to fully develop and implement tax system reform.** This section outlines concrete and visible political-based measures to support implementation of the corresponding reforms.
- ▶ **Coordinated capacity-building to support tax system reform implementation.** The fourth component aims at identifying the resources needed for the process of reform itself, including external and public ones.

In line with the Medium-Term Revenue Strategy framework, the analyst or consultant should pay special attention to the following:

- ▶ existing legislation and other normative regulations;
- ▶ tax policy design and components (including health, gender equality and environmental tax);
- ▶ organization of the tax administration system;
- ▶ tax governance;
- ▶ core procedures and functions (registration, filing, payment, taxpayer services, tax audit and dispute resolution processes); and
- ▶ IT systems and human resources.²⁰

Examples of how to integrate elements into the analysis can be reviewed in the web page of Platform for Collaboration on Tax.²¹

¹⁸ See www.tax-platform.org.

¹⁹ See www.tax-platform.org/medium-term-revenue-strategy.

²⁰ For specific details, see www.worldbank.org/en/programs/the-global-tax-program and www.imf.org/external/np/ins/english/rmtf.htm#modularapproach.

²¹ See www.tax-platform.org/medium-term-revenue-strategy/countries.

In addition to the aspects featured here, the analyst or consultant should also prepare **quantitative estimates** for the different types of taxes included in this section.

General taxes

To estimate the incremental level of general taxes, the fiscal space tool uses a tax elasticity approach with the following equation:

$$\varepsilon_T^R = \frac{\frac{\Delta R_i}{R_i}}{\frac{\Delta TR_i}{TR}}$$

where the tax elasticity (ε) of revenues (R) to the tax rate (TR) is estimated as the percentage change of tax revenues after a 1 per cent increment in the TR.

$$\Delta R_i = \frac{\varepsilon \cdot (R_i \cdot \Delta TR_i)}{TR}$$

Multiple authors have measured tax elasticities for different countries and tax categories. Table 5 summarizes some of the empirical research conducted for those purposes. For a detail analysis of quantitative tax analysis, the analyst or consultant should refer to Jenkins, Kuo and Shukla (2000).

Table 5. Tax revenue elasticities to changes in tax rates, by selected cases

Tax category	Country	Estimated elasticity	Source
Corporate income	Switzerland	-0.43	Staubli 2018
Import duties		0.24	
Excise duties	Uganda	0.32	Ayoki, Obwona and Ogwapus 2008
VAT		1.45	
Capital gains	United States	-0.3 to -0.5	Agersnap and Zidar 2020
Corporate tax base	United States	-0.2	Gruber and Rauh 2005
Personal income tax	OECD	0.28 to 0.74	

Source: Authors' elaboration.

Earmarked taxes

Figure 8 presents a series of taxes that have been implemented in different countries to finance health or social protection programmes. This category includes taxes of the most diverse nature, including financial transaction levies, taxes on touristic activities, property taxes and duties on imported alcohol and tobacco.

► Figure 8. Examples of specific taxes used to finance social protection



Source: Ortiz et al. 2019.

Table 6 covers five of those taxes and the way their potential revenue-generation capacity can be calculated. The final form of each tax is subject to multiple assumptions and considerations. For instance, the financial transaction tax may include or exclude certain types of transactions (between banks, between accounts of the same persons, etc.) or may exclude transactions of less than a certain amount. A similar approach may appear when discussing telecommunications and touristic levies. In the former, the tax base may be mobile, digital or internet services (because in some countries the consumption of mobile minutes has been declining while internet communication has been expanding). A similar discussion may exist in the case of touristic services because the base may be the arrival of persons or the application of a special rate to every night of stay.

In general, it is important to take note of the trade-off that exists between taxes and GDP. It is likely that continuous or significant increments in tax rates may negatively affect total GDP. This relationship holds regardless of whether the analysis focuses on the macro or the micro level. For instance, large profit tax rates on firms may affect investment decisions while, equally, high levels of taxes on tourism may reduce the number of visitors or the level of spending of each tourist in the country. In short, when assessing individual general or earmarked taxes, the existing situation is important for evaluating the degree of freedom the country has to increase tax rates. This can be done by using benchmarks in relation to peer nations. Also, from a more qualitative perspective, it may be critical to analyse the way the new tax or existing rate increment is justified to the public (this tax would be used in poverty-reduction programmes, for instance).

Table 6. Formulas to estimate revenue collection from selected specific taxes

Name of the tax or levy	Tax base	Formula (% GDP)
Financial transaction	Bank transactions	$FTT = \frac{\text{No. transactions} * t}{\text{Nominal GDP}}$ where t = tax per transaction in local currency if it is a flat amount without distinguishment of the type of transaction. There may be different amounts depending on the size of the transaction. A second equation defines the expected revenue collection on the assumption that the tax is a percentage of the value of the transaction (%t)
	Local currency transactions	
	Foreign exchange transactions	
	Automatic payment	
	Securities transactions	
		$FTT = \frac{\text{Value of transactions} * \%t}{\text{Nominal GDP}}$
Tourism 1	Number of arrivals to the country	$TTA = \frac{\text{Arrival} * \text{tpt}}{\text{Nominal GDP}}$ where TTA is touristic tax on arrivals and tpt is the tax per tourist in local currency
Tourism 2	Number of nights spent in hotel	$TTN = \frac{\text{NHN} * \text{tpn}}{\text{Nominal GDP}}$ where TTN is the touristic tax per night, NHN is the number of hotel nights and tpn is the tax per night
Telecommunications	Minutes of mobile consumption	$TT = \frac{\text{MC} * \text{tpm}}{\text{Nominal GDP}}$ where TT is telecommunications tax, MC is the number of minutes consumed in mobile services and tpm is the tax per minute.
Digital tax services	Specific gross revenue streams of digital companies	$DT = \text{Revenues} * \text{Tax rate}$ where DT is the digital tax, revenues refer to the total revenues that are subject to taxation and tax rate is the share of those revenues that is collected in the form of digital tax.

Source: Authors' elaboration.

Tax evasion and tax expenditures

Tax evasion and tax expenditure analyses are the last two issues in this section. Tax evasion differs considerably across countries and across levy type, although in general terms it is widely accepted that evasion should be part of a social protection financing strategy either because it may yield a significant amount of resources or because it signals the political commitment of the government to improve revenue collection efficiency. The room for manoeuvring is wide because it is usually higher in value-added tax (VAT) than in income taxes. For instance, according to Vellutini et al. (2019), individual tax evasion in the European Union (comprising capital income tax, wealth and wealth-transfer taxes and personal income tax on the income originally transferred offshore²²) ranks between 0.03 per cent of GDP in Lithuania and 2.39 per cent of GDP in Malta. The United Nations Economic Commission for Latin America and the Caribbean estimated that the VAT evasion in Latin America averaged 2.4 per cent of GDP, ranging between 1.2 per cent in Uruguay and 3.4 per cent in El Salvador in 2015.²³

Tax evasion and tax expenditures deserve a different approach because their corresponding figures are usually prepared or estimated by official, academic or international agencies. The complexity of this type of

22 See www.taxobservatory.eu/repository/estimating-international-tax-evasion-by-individuals/.

23 See <https://dailybrief.oxan.com/Analysis/GA219892/Latin-America-tax-evasion-will-strain-state-funds>.

exercise makes it difficult to make a calculation during the preparation of the fiscal space report. The best strategy is to take the estimates already prepared by the IMF, the finance ministry or the Council on Economic Policies and the German Institute for Development and Sustainability (which together conduct the Global Tax Expenditures Database project) and analyse them, their components and potential contributions to gap closure. For example, it would be important to review the sources of tax exemptions and evaluate whether they should be maintained or if it is better to eliminate them or collect additional funds and allocate them for social protection.

c) Sources of data

The annual reports and the budget proposals of the finance ministry of the local country should be the first source of information. Alternatively, the IMF Government Finance Statistics database (<https://data.imf.org/gfs>) can provide useful data. Also, the Public Expenditure and Financial Accountability Programme “provides a framework for assessing and reporting on the strengths and weaknesses of public financial management using quantitative indicators to measure performance”²⁴ and thus contains plenty of information on the different components of public financial management systems.

A template like the one in table 7 should be filled with information in either local currency or in GDP terms for five years or so. In addition, information on nominal GDP may be required.

24 See www.pefa.org.

Table 7. Template to collect data on general taxes, by individual tax

Tax	Year 1	Year 2	Year 3	Year 4	Year 5
VAT					
Personal income					
Corporate					
Customs					
Other taxes					

Source: Authors’ elaboration.

For specific taxes, the sources of data are varied, so intensive searches should be conducted in multiple sites. Table 8 lists these alternatives.

Table 8. Methods to collect data on general taxes, by individual tax

Tax	Sources of information
Financial transactions	Central bank reports Bank regulators
Tourism	Ministry of tourism World Tourism Organization
Telecommunications	Reports from regulatory entities
Property taxes	Municipalities or local governments
Alcohol and tobacco	Customs authorities Tax authorities
Lotteries	National lottery organization
Gas, mining, etc.	Financial reports from formal companies in the field Information from tax authorities
Digital services	Report of multinational or local firms established in the country or that sell services in that particular country

Source: Authors’ elaboration.

d) Special issues to consider

The qualitative assessment of taxation as a potential source of fiscal space may require considering a series of topics, with the following among them.

- ▶ Time since the last tax reform. The feasibility of increasing general taxes depends heavily on the time span between the last reform and today's discussions. Political support may have eroded if proposals for new increments emerged after recent tax changes.
- ▶ In line with Stotsky (2022: 2), when deciding on tax reforms, it is important to consider that "taxes should minimize the degree to which the government distorts private economic decisions, including in consumption, savings investment and production". This may apply to a large share of situations, but in some particular cases, there may be an intention of the government to modify unfavourable behaviours, such as smoking, excessive carbon emissions, use of chemical products and cross-border speculative flows that may increase the risk of financial crises.
- ▶ None of the proposals of tax reform will succeed if there are no improvements in tax collection that aim at reducing tax evasion. Therefore, in parallel to any proposed increment, the government should announce changes in policies, organizational restructuring, human resources and IT allocations to demonstrate its intent to improve tax compliance.
- ▶ There is an ongoing and intense debate about whether taxes should be general or specific for social protection. While the finance ministry usually opts for the former, social protection organizations prefer the latter. Finance ministries prefer more budget flexibility so that resources can be allocated according to needs and political priorities, which are two variables that may change in the short term. On the contrary, social protection-related institutions favour earmarked taxes to assure present and future financing. This type of mechanism, however, may play against the sustainability of the programmes funded using this strategy. For instance, in Mongolia, rising copper prices created the conditions to increase revenues for the Human Development Fund, especially the Child Money Programme (ILO 2016). As long as high copper prices continue, the programme can operate without complications. However, downward fluctuations in the price would negatively affect the available resources and therefore the possibility of extending the coverage or, eventually, maintaining the current conditions.
- ▶ A general review of the legislation in terms of best practices and recommendations should be explored with a view to eliminating weak incentives, institutional limitations and other challenges to efficient tax collection.
- ▶ A detailed review of exemptions may also strengthen other tax proposals. Assessing their cost-benefit and cost-effectiveness is critical to sustain such measures.
- ▶ As Ortiz et al. noted (2019), there are some taxes with significant potential that have been poorly explored in developing countries, as in the case of real estate levies.
- ▶ All taxes have strengths and weaknesses. Hence, rejecting any specific proposal on the grounds of its limitations and side-effects may not be the best way to proceed. The possible limitations and side-effects need to be weighed against the potential benefits to be gained from additional resource mobilization (reducing poverty and inequality).

Eliminating illicit financial flows

a) Concept

According to the United Nations (2016: 1):



[Illicit financial flows] are defined broadly as all cross-border financial transfers, which contravene national or international laws. This wide category encompasses several different types of financial transfers, made for different reasons, including: funds with criminal origin, such as the proceeds of crime (for example, tax evasion, money laundering, fraud and corruption); funds with a criminal destination, such as bribery, terrorist financing or conflict financing; transfers to, by, or for, entities subject to financial sanctions under UN Security Council Resolutions such as Resolution 1267 (1999) and its successor resolutions (e.g. Al Qaida

and other terrorist organizations); and transfers that seek to evade anti-money laundering/ counter-terrorist financing measures or other legal requirements (such as transparency or capital controls)."

Illicit flows may have a financial or a trade nature and are usually conceived as wealth illegally earned through the implementation of such instruments as unreported cash movements, trade mis-invoicing (import under-invoicing to avoid higher tariffs and export over-invoicing to take advantage of export subsidies) and the mis-pricing of transactions (Ortiz et al. 2019).

Assessing illicit flows in the context of fiscal space analysis should have multiple objectives: First, it should provide an idea of the volume of flows in the economy. Second, based on that first calculation, it is equally important to have an idea of the share of flows that may be transformed into effective revenues for social protection considerations. Third, combating illicit flows may require a broad communications strategy to position the topic at the public level. Fourth, opening the discussion promotes a better understanding of the problem and the advent of policy measures for implementation. Finally, even if the funding coming from the illicit financial and trade flows is not substantial, the learning process for social security and fiscal institutions about the flows and the access to information and technology that allows the institutions to fight internal corruption and fraud may be relevant. And even if the recovery of illicit financial and trade flows in general for social protection is small, the strengthening of the institutional capabilities to prevent and recover values lost from fraud and corruption increases.

b) Method of estimation

The potential level of financing related to illicit flow recovery can be estimated using the formula:

$$IFPR_i = \frac{TVG_{i,j} * \alpha_{i,j} * \beta_{i,j}}{Nominal\ GDP_j}$$

where IFPR_i refers to illicit flows' potential revenues from source *i* (trade or financial) in Country *j*; TVG_i is the total value of the trade or financial gap in million or billion US dollars in Country *j*; α is the share of the TVG that can be effectively recovered, as per expert criteria; and β is the share of recovered TVG that can be collected in the form of taxes for social protection purposes.

c) Sources of data

The main source of information on illicit trade and financial flows is Global Financial Integrity (<https://gfintegrity.org>) and its series on illicit flows in developing countries. These are indirect and global estimates of the illicit flows' potential revenues, so they are mainly hypothetical figures. Table 9 lists several of those reports with their databases.

Table 9. Sources of illicit flows information

Name of the report	Year of publication	Link
Trade-Related Illicit Financial Flows in 134 Developing Countries 2009–2018	2021	https://gfintegrity.org/report/trade-related-illicit-financial-flows-in-134-developing-countries-2009-2018/
Trade-Related Illicit Financial Flows in 135 Developing Countries: 2008–2017	2020	https://gfintegrity.org/report/trade-related-illicit-financial-flows-in-135-developing-countries-2008-2017/
Illicit Financial Flows To and From 148 Developing Countries: 2006–2015	2019	https://gfintegrity.org/report/2019-iff-update/
Illicit Financial Flows To and From Developing Countries: 2005–2014	2017	https://gfintegrity.org/report/illicit-financial-flows-to-and-from-developing-countries-2005-2014/
Trade-Related Illicit Financial Flows: Data by Country	Several	https://gfintegrity.org/iif-data-by-country/

Source: [Global Financial Integrity](https://gfintegrity.org) webpage.

d) Special considerations

The following highlights some of the issues to consider when analysing illicit flows as a source of income for social protection purposes.

- ▶ What is exactly considered an illicit flow in the country of analysis?
- ▶ What would be the process to follow if an illicit flow is detected? The time elapsed between flow identification and effective recovery is critical for the opportunity of illicit financial and trade flows as a source of funding.
- ▶ What is the optimal levy that the country should apply to deal with the illicit financial and trade flows problem?
- ▶ What is the level of human and technological resources that the finance ministry, central bank or related organization must identify to recover these flows? Is the staffing of those organizations trained to detect and recover illicit financial and trade flows?
- ▶ How are domestic capital markets likely to be affected if inflows are big?
- ▶ How feasible is it to coordinate a programme with partner countries?

One major limitation with the available illicit flows' potential revenue estimations is that they are indirect estimates based on different methodologies that have been developed for those purposes (see, for instance, Methodological Guidelines to Measure Tax and Commercial Illicit Financial Flows²⁵). One criticism is that it still remains to be demonstrated that the recovery of flows is a feasible act and that there are institutional and legal ways to do so. Furthermore, the most effective recommendation seems to be the search for measures that prevent and/or stop illicit flows rather than the establishment of an institutional and legal apparatus for something that is complicated to put into practice. Discussion of possible preventative measures should be included as part of this section.

Other sources of information on prevention measures

- ▶ [Global Forum on Transparency and Exchange of Information for Tax Purposes](#)
- ▶ [U4 Anti-corruption Resource Centre](#)
- ▶ [Global Financial Integrity](#)
- ▶ [Stolen Asset Recovery Initiative](#)

As an example of recovering funds for social protection purposes, box 1 summarizes a situation in Uzbekistan and its efforts to recover money that had originated in bribery practices in the telecommunications sector.

²⁵ See <https://unctad.org/publication/methodological-guidelines-measure-tax-and-commercial-illicit-financial-flows-methods>.

▶ Box 1. Illicit asset recovery in Uzbekistan

The Government of Uzbekistan initiated a series of actions to recover funds in the hands of the Government of Switzerland due to bribes that the daughter of former Uzbek President Gulnara Karimova received from the telecommunications companies MTS, Telia and VimpleCom. Starting in 2015 and for about 18 months, Uzbekistan's International State Crime Initiative investigated Karimova as a result of an accusation filed by the United States Government stating that the daughter had received US\$850 million in the form of illicit flows. The investigation detected the existence of a corruption network in a structure that received both legal resources and illegal flows. Efforts thereafter were directed at recovering the funds on behalf of the State of Uzbekistan.

In the first round, the Government identified US\$131 million in 2019, which was returned by the Government of Switzerland in 2022, prior to the signing of an agreement between both parties. As part of this agreement, the Government of Uzbekistan committed to creating a fund that would be administered by the United Nations and

used to advance the implementation of projects to achieve the SDGs. Future resources from the same source, estimated at US\$719 million, would also be incorporated into the fund once they had been unfrozen. Of course, the recovery of assets occurred within a legal framework with principles that required (Lasslett 2017):

- ▶ transparency and accountability in the restitution process;
- ▶ use of the assets to improve the living conditions of the people of Uzbekistan;
- ▶ investment of the funds into projects that support sustainable development (in accordance with the 2030 Agenda and Uzbekistan's development strategy);
- ▶ establishment of a monitoring mechanism; and
- ▶ potential involvement of non-state actors.

Source: Federal Department of Foreign Affairs of Switzerland 2022.

Reallocating public expenditures

a) Concept

Budget reprioritization refers to the reallocation of resources from one sector to another or from one budget account to another. This can be done through multiple channels. In the short term, for instance, the budget can be nominally cut in one account and then reallocated into a different one. In the medium term, this can be achieved by freezing the budget of one institution so that, as a percentage of GDP, it starts falling, leaving some margin to expand the budget in other sectors (like social protection). Finally, long-term structural reforms may generate efficiency savings that can be reassigned to better cost-effectiveness interventions.

The analysis of budget reprioritization can be done using two approaches: The **economic approach** based on an accounting perspective – it assesses the structure of the budget according to remunerations, procurement of goods and services, transfers and capital spending. The **functional approach**, on the other hand, evaluates expenditure distribution according to the strategic function it performs (national security, environment, social protection, government, etc.).

b) Method of estimation

Two analytical strategies may be considered in this option: assessment of incremental budgets or sectors with high budgetary allocations and a review of spending efficiency and budgetary execution.

Assessment of historical evolution of the budget

For the first strategy, the analysis can be done following the equation:

$$\Delta \text{Budget}_i = \text{Budget}_{i,t} - \text{Budget}_{i,t-n}$$

where Δ is the difference in the budgetary allocation of institution or account i in the last n years (2022–15, for example). Figures in GDP terms may provide a better overview of the situation. The equation applies for either functional or economic approaches.

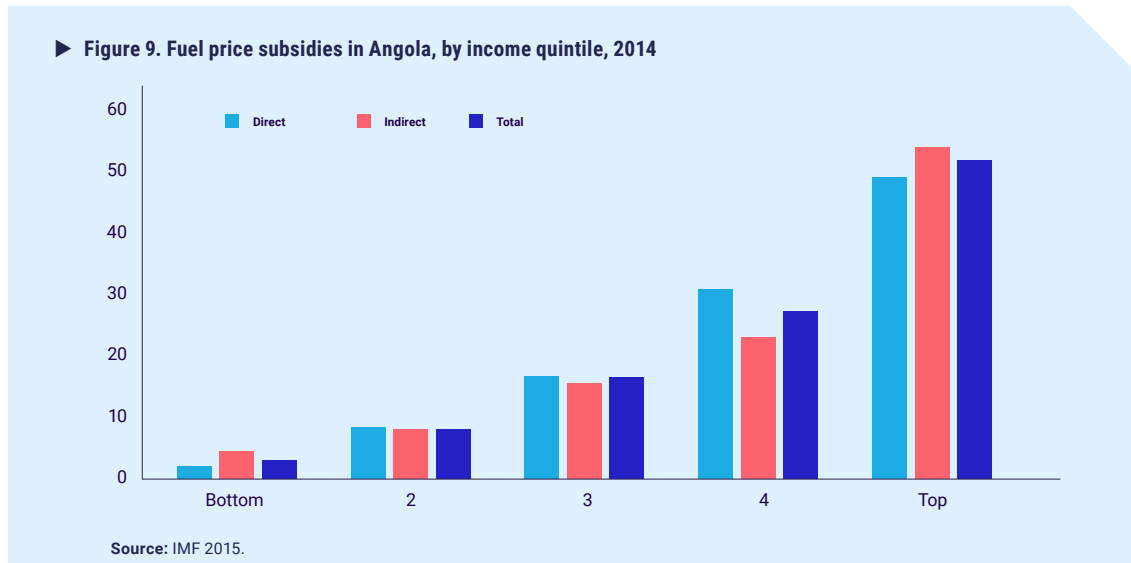
A detailed analysis of each case might be necessary. In principle, the assessment of the different sectors or budget items would focus on those that have obtained increases throughout the study period. However, the analysis cannot be limited to those categories with incremental budget. For example, it is possible that some sectors have not seen their budget increase because their initial level of spending was already high. Reviewing these cases could be equally important for the analysis of fiscal space.

Second, it may be much better to compare three-year averages than single-year figures. For instance, instead of comparing the situation in 2015 with 2021, it would be preferable to compare the average of 2014–16 with 2019–21 so that the effect of any extraordinary year is moderated. This may be the case of the social protection programmes in 2020, given the unusual growth due to the COVID-19 pandemic that may yield unrealistic conclusions about the historical trajectory of these budgets.

Efficiency assessment

The objective of this block of strategies is to identify areas of inefficiency or inequitable allocation of programmes that could free up resources for alternative use in social protection.

- **Benefit incidence analysis.** Cuenca (2008: 2) defined benefit incidence analysis as “a tool used to assess how tax policy or government subsidy affects the distribution of welfare in the population. In other words, it evaluates the distribution of government subsidies among different groups in the population, in particular, among different income groups”. Results of this type of analysis have been used, for instance, in the evaluation of how fuel price subsidies are distributed across income groups. Figure 9, for example, refers to the distributional characteristics of fuel subsidies in Angola (IMF 2015), where the top income group received about 50 per cent of the total fuel subventions.



- **Targeting assessment.** A targeting assessment is a close relative of the benefit-incidence analysis. It is intended to analyse if people who are poor are reached by social protection (World Bank 2019). The targeting analysis may provide information on the effective coverage of poor households or individuals and the level of inclusion and exclusion errors.²⁶ An example of this type of exercise is the Uzbekistan Social Assistance Targeting Assessment²⁷ (World Bank 2019).
- **Budgetary execution.** The analyst or consultant should also pay attention to budget execution because persistent under-execution rates may alert resource misallocation and may call for a different way to assign resources. An equation for assessing this would be:

$$ER_i = \frac{ES_i}{FB_i}$$

where ER refers to the execution rate of programme or category i ; ES is the executed or effective level of spending; and FB is the final budget, including amendments done to the initial budget. This exercise can be done by institution, programme or budget account (economic or functional).

Although the indicator may seem initially easy to estimate, some caveats should be made at the moment of interpreting the results. For instance, there is no single rule about what is good or poor execution. Execution rates above 5 per cent may refer to an excellent performance, rates in the range of 5 per cent to 15 per cent may be good, while an ER between 15 per cent and 25 per cent may be fair. Execution rates of 25 per cent or more may be labelled as poor.

Second, in line with the previous issue, it is important to stress that values are figurative because each budgetary account should be assessed according to the specific conditions of each case. For instance, the wage bill usually experiences high execution rates because the payroll is a stable account with high

²⁶ Inclusion errors refer to a situation in which a non-eligible person receives the benefit. On the other hand, an exclusion error refers to any situation in which a potential eligible person does not receive the benefit.

²⁷ See <https://openknowledge.worldbank.org/server/api/core/bitstreams/ec8f7605-ecbb-5046-8033-f54bd89b4136/content>.

predictability conditions. On the contrary, capital investments are more difficult to predict because they depend on the existing legislation, the stage of each project and the organization of the procurement processes.

Third, even if under-execution persists over time, it is not always possible to recommend a reallocation of the budget from account A to account B. Understanding the logic of public budgets is key in this regard. For example, budgets are usually prepared by assuming that all staff in institution X will be working 12 months. Vacancies are included in the budget formulation even when it is known in advance that the budget will not be executed until a new staff member enters.

- ▶ **Administrative costs.** Upon data availability, the analyst or consultant should check the size and composition of administrative costs associated with social protection programmes. There is no single parameter to assess administrative costs, but entities like the United Nations Economic and Social Commission for Asia and the Pacific indicate that administrative costs in social protection contexts may range between 5 per cent and 15 per cent, depending on current benefits volume.

c) Sources of data

The annual reports of the finance ministry are the most important source of data. Ideally, the information should be gathered for ten years or so, although five-year periods may also be valid. For the analysis of the functional approach, a template like the one in table 10 may be needed. Information should be assessed in GDP terms so that data to be collected will be in nominal terms (to be later converted into GDP terms) or directly in GDP terms, depending on the way it is reported.

Table 10. Template to collect information on functional distribution of the budget

Institution	Year 1	Year 2	Year 3	Year 4	Year 5	Year n...
Ministry of education						
Ministry of environment						
Ministry of defence						
...						

Similarly, the analysis of the economic approach may collect information similar to what is presented in table 11. As in the previous case, nominal or GDP-based data may be needed to proceed.

Table 11. Template to collect information on economic distribution of the budget

Institution	Year 1	Year 2	Year 3	Year 4	Year 5	Year n...
Remunerations						
Current transfers						
Capital expenditures						
...						

Other sources of information

- ▶ The IMF Government Finance Statistics may provide useful information, at <https://data.imf.org/?sk=a0867067-d23c-4ebc-ad23-d3b015045405>. The Detailed Expense Breakdown section contains information by country, year and budgetary account.
- ▶ Public Expenditure and Financial Accountability Programme reports can be accessed at www.pefa.org.

- ▶ Public expenditures reviews or social protection expenditure reviews may provide important insights on such topics as the historical evolution of spending categories and efficiency.
- ▶ Social assistance targeting assessments will be useful.
- ▶ Ministry of finance annual reports and memoranda also are necessary.

d) Special considerations

Proposed measures for budget reprioritization should be assessed with some of the following realities in mind.

- ▶ Strictly speaking, the budget reprioritization option does not create overall fiscal space but increases fiscal space for social protection while reducing the allocation to other sectors or accounts.
- ▶ Given the above, it is quite relevant to understand the political economy of the budgetary structure. This is true for both the economic and functional distributions. As mentioned, the budget reflects historical and current decisions on the use of public resources to favour certain sectors. The feasibility of any recommendation aimed at redefining this structure requires a deep understanding of the past policies that motivated the increase in allocations. In most cases, reviewing the legal frameworks (laws, decrees) behind the composition of the budget may provide inputs for assessing the feasibility of the different recommendations.
- ▶ Depending on the political and fiscal contexts, the public may have a different perspective regarding functional and economic approaches to the budget structures and their potential reforms. For example, cutting budget allocation to the environment sector will be viewed differently from controlling wages in the public sector. Whatever the focus of the reform, excessive austerity may affect the overall performance of the government and expected outcomes on human development. Wages are current expenditures in the standard accounting classification, and they are usually first in the line of expenditure control during budgetary cuts. Cutting salaries could affect the formation of human capital, not only because salaries in developing countries are already low but also because a larger cut could affect the quality of services in such areas as health and other social services.
- ▶ Measures should consider the level of “aggressivity of implementation” for creating fiscal space for social protection. It is thus important to analyse not only the size of the savings to be generated but also the speed of implementation of the corresponding measures. Shock-based measures usually have negative effects on the affected sector and poor feasibility prospects for their implementation. For this reason, one possibility is to either freeze the nominal value of the budget or to increase it at a rate below GDP growth.
- ▶ Some sectors that may be affected by budget reprioritization may demand similar reviews and measures aimed at improving allocation within the social protection sector. The sector, therefore, should also have a response to this type of consideration.

Using fiscal and central bank foreign exchange reserves

a) Concept

Countries may accumulate reserves in the form of fiscal or central bank foreign exchange reserves that may be utilized to finance social protection programmes, either through direct contribution of funds to cover operations or as collateral to back up loans. Fiscal reserves may come from public surpluses or profits from public companies while foreign exchange reserves are accumulated through foreign exchange market interventions by central banks in the context of balance of payments movements. The use of fiscal and foreign exchange reserves as potential financing sources for social protection, infrastructure and related fields has been explored by several authors, including Schmitt (2018) and Mbeng-Mezui and Duru (2013). Proponents of this alternative option have argued that there is a social cost to keeping reserves (see Rodrik 2006) and an opportunity cost to holding reserves (even if they generate positive returns) or of borrowing money for development projects. In general, if the country has reserves in excess, there is a case for considering them as a potential source of income. However, opponents to this idea consider that reserves should be used only as an insurance mechanism against sudden stops, economic crises or to cover unexpected movements in the balance of payments, among other arguments. The recent macroeconomic events in relation to increased debt and exchange rate pressures become relevant for this

discussion due to countries adopting a more cautious position and consequently defining optimal fiscal and exchange rate reserves at higher levels than historically, motivated by precautionary perspectives.

b) Method of estimation

Foreign exchange reserves

To estimate the possibility of using foreign exchange reserves as a real fiscal space alternative, two issues should be considered: First, it is important to define the term “reserves in excess” because not all of them can be used for financing purposes. Based on guidance from the European Central Bank (2012), Moghadam, Ostry and Sheehy (2011) and Greenspan (1999), the adequacy of reserves and their potential level in excess can be analysed using the following four indicators.

- ▶ **The total reserves in months of imports**, which considers that the optimal stock should represent at least a level covering the payment of three months of imports.
- ▶ **The Greenspan–Guidotti rule**, which establishes that the reserves should account for 100 per cent of the short-term foreign debt.
- ▶ **The ratio of foreign exchange reserves to the total foreign debt balance**. Mbeng-Mezui and Duru (2013: 5) indicated that this indicator “reflects a country’s ability to repay its total foreign debt balance with foreign exchange reserves”, with 40 per cent being the optimal value.
- ▶ **The ratio of foreign exchange reserves to money and quasi-money**, which represents a financial crisis precaution metric. The benchmark for this coefficient usually ranges between 10 per cent and 20 per cent of money and quasi-money if a country has a pegged or fixed exchange rate and 5–10 per cent for floating exchange rate regimes.

In addition to the selection of the adequate measure, the second issue consists of assessing the actual data from the four indicators above against the parameters recommended by the reviewed literature. The template in table 12 can be used to summarize the elements to estimate the level of excess foreign reserves. The benchmark is a fixed value, and this figure is contrasted against the value of the indicator in the last available year. One alternative is to estimate the average value of the past three or five years.²⁸ The difference between the latest available year and the benchmark is the level of excess. However, the key point is to transform this difference in GDP terms. Each indicator requires a different formula.

Rule	Benchmark	Latest available year	Reserves in excess, % GDP
Total reserves in months of imports	3 months	XXX	XXX
Greenspan–Guidotti rule	1.0	XXX	XXX
Foreign exchange reserves to the total foreign debt	40%	XXX	XXX
Foreign exchange reserves to money and quasi-money	5–10%	XXX	XXX

The estimation of the reserves in excess according to the “month of imports” criterion may be done using the following equation:

$$\Delta months = \frac{\text{total reserves in US\$} - \text{reserves required to cover 3 months of imports}}{\text{nominal GDP in US\$}}$$

For example, if reserves are US\$500, the months of import is five and the GDP is US\$20,000, then the level of reserves in excess is 1 per cent of GDP.

²⁸ The use of three- or five-year averages avoids extreme fluctuations or extraordinary values that may appear in one particular year.

The second indicator, the Greenspan–Guidotti rule, defines the optimal level of reserves as 100 per cent coverage of the short-term external debt. In this case, the equivalent indicator in GDP terms corresponds to the expression below. If the coefficient of reserves to short-term debt falls below 1, the country has no excess according to that indicator. The mathematical expression of this is:

$$RiE_{GG} = \frac{(\text{coefRD} - 1) * \text{total reserves in US\$}}{\text{nominal GDP in US\$}}$$

where RiE is the level of reserves in excess according to the Greenspan–Guidotti rule and coefRD is the coefficient of reserves to short-term external debt. For instance, if the coefficient is 1.2 with total reserves amounting to US\$500 and the GDP being US\$20,000, then the RiE_{GG} would be 0.5 per cent of GDP.

The third indicator relates reserves with total external debt. The optimal level is, according to the literature, 40 per cent of the debt. Thus, the formula to estimate the level of excess is:

$$RiE_{ED} = \frac{(\text{coefext} - 0.4) * \text{total reserves in US\$}}{\text{nominal GDP in US\$}}$$

with RiE_{ED} being the reserves in excess associated to the external debt indicator and coefext being the level of reserves as a percentage of the total external debt. If coefext is less than 0.4, no excess exists.

If, for example, the coefext is 0.5, the level of reserves is US\$500 and the GDP is US\$20,000, then the level of over-reserves would be estimated at 0.25 per cent of GDP.

The final indicator refers to the relationship between foreign exchange reserves and money and quasi-money (M2), with values between 5 per cent and 10 per cent considered optimal. As in the previous cases, the formula is expressed as:

$$RiE_{M2} = \frac{(\text{coefM2} - 0.05 \text{ or } 0.10) * \text{total reserves in US\$}}{\text{nominal GDP in US\$}}$$

where RiE_{M2} is the level of reserves in excess associated with the monetary aggregate and coefM2 is the share of reserves to money and quasi-money. If this indicator is assumed to be 25 per cent of money and quasi-money, given the same parameters used in the previous examples, then the excess would range between 0.25 per cent and 0.50 per cent of GDP.

For illustration purposes, table 13 presents the results for Uzbekistan. The estimated outcomes indicate that the country may have reserves in excess in the order of 16.6 per cent of GDP (average), with a minimum estimated level of 15.7 per cent of GDP.

Table 13. Estimated reserves in excess in Uzbekistan (as a percentage of GDP)

Rule	Benchmark	Past 5 years	Reserves in excess (%GDP)
Total reserves (in months of imports)	3	15.1	17.8
Greenspan–Guidotti rule	1.0	3.3	15.7
Foreign exchange reserves to the total foreign debt	40%	145.9%	16.4

Source: Authors' elaboration.

Due to the COVID-19 pandemic and especially with increasing inflation rates that appeared in the past years, foreign exchange levels in several emerging countries dropped substantially because they were used to protect their own currency from depreciation as inflation grows.

Once the four estimates of the reserves in excess levels are calculated, the results can be used in two ways for policy recommendations: as an average of the four results or taking the lowest as the most prudent alternative. Review of the legislation on the use of foreign reserves is critical in the overall feasibility assessment of this fiscal space option.

Fiscal reserves

In the case of fiscal reserves, the analyst or consultant should explore potential sources of funds that could be used for social protection purposes. This list may include **government budget surpluses, profits of state-owned entities, privatization-based revenues, royalties and rents from natural resources** (Ortiz et al. 2019). Also, a country may already have an established **sovereign wealth fund** (created from commodity and non-commodity sources). If there is no such fund, the analyst or consultant may consider this as a potential recommendation, with the understanding that the country has a permanent source of resources to accumulate. The Fondo de Estabilización Económica y Social in Chile is an example of an existing fiscal reserves fund that can be explored for social protection analysis purposes.

The literature on optimal reserves (either fiscal or foreign exchange) is less comprehensive, making it difficult to identify parameters of reference. In general, the available literature is limited and with inconclusive recommendations, providing wide ranges of what “optimal” may imply. For instance, Gorina et al. (2019) mentioned that recommendations on the subject typically pointed to the need to keep a large amount of reserves to counteract budget imbalances with no punctual parameter. Kriz (2015), in his review of the literature on optimal reserves, highlighted the limited number of studies on this topic and the broad range of recommendations that had emerged from the empirical analysis. For instance, the author mentioned a wide range between 10 per cent and 93.6 per cent of municipal revenues. Other authors like Figuet and Nenovsky (2006) talked in terms of 12 per cent of the current account deficit. In the case of the Fondo Mexicano de Petróleo, Sierra-Juárez and Méndez García (2017) indicated that the fund should range between 3 per cent and 4.7 per cent of GDP in a fiscal year.

c) Sources of data

Any central bank database should provide information that may be used for the purposes of this alternative option. Information included in the balance of payments and reports on monetary aggregate stocks are the focus of this option. Also, central banks typically provide information on the limits for the use of foreign reserves. Similarly, legislation and annual reports on the use and evolution of special fiscal reserve funds should be considered.

A basic source of information is the [World Development Indicators database](#), from where five indicators may be selected:

- ▶ total reserves in months of imports;
- ▶ short-term debt (percentage of total reserves);
- ▶ total reserves (percentage of total external debt);
- ▶ broad money to total reserves ratio (should be used inversed); and
- ▶ GDP in current US dollars.

d) Special considerations

The use of foreign exchange reserves is one of the most controversial fiscal space alternatives discussed in the literature because it is usually considered a tool that should be used for purposes other than financing programmes. It is possible that reserve utilization is limited to one single round and not working as a permanent source. The following singles out other arguments against the use of reserves for social protection purposes:

- ▶ Excess reserves would be a stock to use once or over some years, after which it is gone, in contrast with perpetual revenue from taxation.
- ▶ Large reserves reduce the perceived risk of default on debt in foreign exchange, thus, reducing reserves will raise interest rates to compensate for the extra risk, which then reduces the fiscal space every year, even after the reserves have been spent.
- ▶ If the exchange rate was allowed to fluctuate freely, no reserves would be needed in principle. But a serious fall in the exchange rate would increase debt servicing in home currency, reducing the fiscal space and possibly forcing default. Therefore, there is need for a confidence-inspiring level of reserves, even with a freely fluctuating exchange rate.

- ▶ If the exchange rate is pegged, there is need for the reserves to cover shortfalls in receipts. Even if there are capital controls, it is hard to prevent capital flight through banks and other financial institutions if there is a loss of confidence in the macro policy.
- ▶ Usually developing countries build up reserves when international finance finds the financial markets in the country attractive. But minds can quickly change and the money can flow out. Even discussing tapping reserves during the inflow period may itself start the outflow period and the loss of those reserves.
- ▶ Use of reserves is at best a temporary solution to a long-term financing need. Politically, it is a non-starter because the reserves (at least part of them) are usually the property of the central bank and commercial banks and are not available to the government for fiscal purposes. Recent experiences in Latin America are not encouraging at all for this alternative option.

When analysing this option, some of the issues to incorporate into the assessment are:

- ▶ existing legislation regarding the use of reserves, because limitations to their use may be established by law;
- ▶ the position of the central bank; and
- ▶ not all of the stock of foreign reserves is disposable for financing purposes. A share of the reserves usually belongs to the central bank or to commercial banks.

In the case of fiscal reserves, the assessment should consider the following aspects:

- ▶ identification of potential sources of funds, their size and possible evolution in the next few years;
- ▶ existing legislation on the use of any fiscal surplus, including competing earmarked destinations;
- ▶ capabilities of institutions that may administer the fund; and
- ▶ initial ideas of the reserve investment strategy.

Managing debt – borrowing or restructuring sovereign debt

a) Concept

Because most countries are not able to cover all their fiscal outlays with taxes and other revenues, debt becomes a complement to keep programmes actively working. Continuous indebtedness, however, cannot be forever. Despite the positive perspectives associated to the use of debt for social protection financing, the post-COVID-19 pandemic years have seen a substantial growth in debt service payments that considerably reduce the possibility of using this alternative in any meaningful way. According to the World Bank (2022), member countries paid US\$62 billion in debt service in 2022, the highest figure since 2000. Wolf (2023) indicated, for example, that the external debt of developing countries of Latin America and sub-Saharan Africa was between 40 per cent and 45 per cent of GDP, without counting domestic debt. As a result, bond issuance among developing countries fell US\$250 billion in 2022.

There are, in short, four issues regarding debt that are relevant for social protection financing: First, debt may be a valuable alternative option for financing social protection in the short and medium terms. Because social protection has proved to be critical for economic growth and social development, a case can be made for indebting a country to finance this type of initiative, given the social and economic multipliers.

Second, in certain exceptional contexts (like pandemic situations), initiatives (like those ones aimed at investing in institutional and governance improvements that allow increasing revenue and fighting fraud and corruption) and countries, debt represents the only way to finance the expansion of social protection because other alternatives, such as taxation, may face political and legal barriers for their implementation until a concerted effort is made to remove those barriers.

Third, it is important to recognize that debt has its limits, beyond which a country may encounter problems in repaying its commitments (sustainability). This may cause a negative impact on social protection. Resources that should be allocated to social programmes could become oriented to interest and amortization payments. Also, debt crises are associated with expenditure cuts, especially transfers and salaries. Thus, to promote the sustainability of social investments, adequate debt management should be part of the overall financing equation.

Fourth, it is quite important to consider the composition between domestic and external debt because each component provides specific insights into the adequate assessment of debt. For instance, countries with high levels of external debt may face exchange rate risks and volatilities (including interest rate movements) that may elevate the burden of financial debt in the event that the local currency depreciates. Also, it is important to analyse the average debt cost because this may provide inputs to evaluate whether external debt is cheaper than domestic debt.

Creating fiscal space for social protection purposes may take several forms, depending on the specific conditions of a country. In countries with a low debt-to-GDP ratio, there are some possibilities to expand debt to finance programme expansion in the short run – for a limited number of years – while other fiscal space options are activated.

Debt management is critical in this process. Lowering the average interest rate currently paid by a government may free resources that can be used for social protection. This type of strategy, however, is usually implemented with the objective of reducing the fiscal deficit and not as a way to reallocate funding for other purposes. Following this path requires strong political negotiation.

Fiscal deficit control is a way to alleviate debt accumulation, but this may imply controlling big spending components, including social protection. In net terms, this may not contribute to overall sectoral financing.

b) Method of estimation

There are four alternative ways discussed here to assess fiscal space for social protection using debt and debt-related issues: (a) debt as a short-term alternative to partially cover financing gaps; (b) management options of the existing debt; (c) debt restructuring; and (d) assessment of alternative financing options for social protection.

Borrowing for social protection

One of the most controversial fiscal space alternative options is the use of public debt to finance social protection programmes. On one hand, there is the so-called Golden Rule of Public Finance, according to which a government should only borrow to finance investments, not current spending (Honjo 2007). Ortiz et al. (2019) and ILO (2018), however, considered it appropriate to seek debt as a possibility of creating fiscal space – as long as a country accesses low-cost sources and other favourable conditions.

To analyse this alternative option, the analyst or consultant should pay attention to the concept of “room to borrow”. Although the traditional approach establishes that public debts at more than 60 per cent of GDP is unsustainable, the truth is that the debt ratio is particular to each country, and therefore other ways must be used to assess the room-to-borrow space. For example, the United Nations Conference on Trade and Development (2011) pointed out that debt can be considered beneficial in the long term, to the extent that interest payments lag behind nominal GDP growth. In addition, the important thing is to know if the potential financiers of said debt are willing to continue the financing, based on the capacity shown by a government to make the payments effective.

To assess the conditions that guide future decisions on indebtedness, the analyst or consultant should make use of the **IMF and World Bank Debt Sustainability Framework**. As defined by the IMF, “the Debt Sustainability Framework is designed to guide the borrowing decisions of low-income countries in a way that matches their financing needs with their ability to repay now and in the future” (IMF, n.d.). The Debt Sustainability Framework forecasts the debt of a specific country for the next ten years and classifies nations into three categories (strong, medium and weak). The results of the model include such indicators as:

- ▶ external debt projections;
- ▶ public sector debt;
- ▶ external debt to GDP;
- ▶ present value of public and publicly guaranteed external debt-to-exports ratio;
- ▶ public and publicly guaranteed debt service-to-exports ratio;
- ▶ public and publicly guaranteed debt service-to-revenue ratio;
- ▶ present value of public debt-to-GDP ratio;

- ▶ present value of public debt-to-revenue and grants ratio; and
- ▶ debt service-to-revenue and grants ratio.

For a complete list of all the results and indicators, the analyst or consultant should visit the web page of the Debt Sustainability Framework (see footnote 28) and check the **interactive guide** and project reports or the Debt & Fiscal Risks Toolkit.²⁹

Information from this type of study should be used to assess whether borrowing is an alternative to financing social protection. The ensuing recommendations to a government or institution should be based on the conclusions about room-to-borrow availability. In case of having a favourable criterion in the matter, the next step could include the existing debt options. Among the possible alternatives, the analyst or consultant could incorporate:

- ▶ government securities and bonds;
- ▶ domestic loans; and
- ▶ external loans.

Debt management opportunities

The objective of this section is to explore ways in which the associated cost of the debt (payment of interest or principal) or the current debt structure can be managed to generate savings in favour of the social protection sector. Based on Yescombe (2007), efforts to improve the overall debt profile of a country (aimed at reducing its overall cost) can take the following forms:

- ▶ reducing the interest cost;
- ▶ increasing the debt amount;
- ▶ extending the debt repayment terms; and
- ▶ any other effort to improve loan terms.

The following singles out a few variables that should be included in the evaluation of the potential alternative options.

- ▶ **Total debt service and its composition.** This issue requires a rapid assessment of the composition of debt service by component, such as interest and amortization payments. A time series approach may be needed (in GDP terms). In addition, this first insight should move into the composition between domestic and external debt and the possibility of facing risks associated with interest and exchange rate movements.
- ▶ **Average interest rate.** Special attention should be paid to those loans with above-the-average rates and their specific conditions.
- ▶ **Term structure of the public debt.** This issue refers to the composition of debt between short-, medium- and long-term debts.
- ▶ **Composition by borrower.** The focus is to analyse the debt structure by type of borrower (private sector, development organizations, banks, bilateral entities, etc.).
- ▶ **Currency management options.** The analyst or consultant should explore the strategies that the government must use to reduce the risk associated with foreign exchange fluctuations and their impact on the stock and composition of public debt.

Debt restructuring and debt relief

In practice, there are five main options available to governments to restructure sovereign debt: (a) renegotiating debt; (b) achieving debt relief or forgiveness; (c) debt swaps or conversions; (d) repudiating debt; and (e) defaulting. These measures are usually considered as last-instance alternatives and generally apply to countries with high indebtedness and low socio-economic levels.

²⁹ See www.worldbank.org/en/programs/debt-toolkit/dsf.

A sovereign debt restructuring process refers to “an exchange of outstanding sovereign debt instruments, such as loans or bonds, for new debt instruments or cash through a formal process” (Das, Papaioannou and Trebesch, 2014: 594). In other words, as Aboneaj, Estes and Landers (2022) elaborated, debt restructuring mainly refers to a negotiation between either two governments or between one government with the private sector, with the objective of making debt service payments more manageable (maturities change, additional grace periods, reducing the principal, reducing the interest rate, debt service suspension, etc.). This debt restructuring process could take two orientations: debt rescheduling (lengthening of maturities of the old debt) or debt reduction (drop in nominal value of the old debt).

Debt relief is a process in which a country’s bilateral or commercial debt is partially cancelled. Debt relief is usually processed through initiatives, such as the Paris Club, the London Club or the Heavily Indebted Poor Countries Initiative executed by the IMF and the World Bank. Any country not already a part of these initiatives could follow a different mechanism.

Debt swaps, debt conversions or debt-for-development exchanges are “the sale of a debt by a creditor to an investor (usually a non-profit organization) who purchases the debt at a discounted price and then exchanges it with the indebted government for shares in a state-owned company or for domestic currency to finance a specific project” (Ortiz et al. 2019: 155).

Debt repudiation emerges when there is “a unilateral disclaiming of a debt instrument obligation by a debtor” (IMF 2003: 266). In this case, there is no bilateral agreements like the ones described previously. According to Christian Aid (2007), opting for debt repudiation should be conditioned on a series of previous assessments, including the effects of debt service on the financing of basic services, the specific identification of debt components that are sensible to repudiation, the share of the total debt that may be classified as legitimate and the possibility of suppressing payments to increase investments in other services.

Finally, a default occurs when a country is unable to repay the different debt obligations it is committed to. Usually, under pre-default conditions, the country experiences insufficient cash flow that prevents it from paying back interest or principal owed. See box 2 for an example of a default used to finance social protection.

► Box 2. Debt defaulting for social protection purposes in Ecuador

Ecuador is an example of a country that defaulted its illegitimate debt and converted those funds into fiscal space for social protection. In 2008, the Government conducted a debt audit that concluded that two of its bonds violated debt-related principles and thus decided to suspend payments during the financial crisis in December 2008. Ecuador then bought the bonds back at the going price of 35 cents on the dollar and retired them. As a result, the country achieved important reductions in interest payments, from 1.5 per cent of GDP in 2008 to 0.9 per cent in 2009 (a 0.6 per cent of GDP gain). Savings for 2008–30 were estimated at US\$7 billion.

The freed resources were used to support the financing of health, education and social assistance programmes while minimizing the impact of the 2008–09 financial crisis on the economy. In particular, the additional funds allowed for a 50 per cent growth in the total housing loans due to the increasing budget of the Bono de la Vivienda scheme and the concessional mortgage loans issued through the Social Security Institute. The investment in the Bono de Desarrollo Humano (the country’s cash transfer programme) doubled, from 0.7 per cent to 1.8 per cent of GDP.

In addition to the core impact on housing and the monetary cash transfer programme, several side-effects were also reached. The expansion of the Bono de Desarrollo Humano contributed to a sharp increase in the number of vaccinated children, from 2.5 million in 2008 to 3.6 million in 2010; and more than 3 million prenatal examinations were performed.

c) Sources of data

Information for estimating the primary balance sustainability gap may come from annual debt reports of the ministry of finance or the central bank. Data to be collected include the items cited in table 14.

Table 14. Information required to prepare a debt management assessment for fiscal space

Variable	Source
Long-run real interest rate	Ministry of finance
Long-run GDP growth rate	Central bank Statistics agency Ministry of planning
Weighted interest rate	Ministry of finance
Portfolio composition	Ministry of finance
Term-structure	Ministry of finance
Total payments, interest	Ministry of finance
Total payments, amortization	Ministry of finance
Internal and external debts	Ministry of finance

Other sources of data

- ▶ [European Network on Debt and Development \(EURODAD\)](#)
- ▶ [Latin American Network on Economic and Social Justice](#)
- ▶ [Africa Forum and Networks on Debt and Development](#)
- ▶ [IMF, Historical Public Debt Database](#)
- ▶ [World Bank, Quarterly Public Sector Debt](#)
- ▶ Joint External Debt Hub
- ▶ Public Expenditure and Financial Accountability Assessment reports

d) Special considerations

The following singles out several issues to consider when assessing debt as a potential source of fiscal space.

- ▶ Debt is one of three main sources of funding for social protection, but it should be regarded as a short-term alternative with certain limits to its expansion.
- ▶ Each country has its own optimal debt ratio according to historical characteristics and the existing profile of its public sector debt.
- ▶ As might be expected, multiple sectors would opt to compete for debt-based fiscal space creation. Once debt expansion is an alternative, it becomes relevant to analyse the political economy of indebtedness to evaluate the likelihood of social protection benefiting from debt financing.
- ▶ The terms “debt restructuring” or “debt renegotiation” should be used cautiously because they may cause negative reactions towards a country that announces it is embarking on such processes.
- ▶ When the average cost of a debt is reduced (as measured by the weighted average interest rate), a critical question remains about the destination of the savings: Will they be used to reduce the fiscal deficit or will they be used for social protection financing?

Increasing aid and transfers

a) Concept

Official development assistance (ODA) flows are critical in low- and middle-income countries as a **complement** to other sources of financing. ODA may take the form of grants, concessional loans, debt relief and other related mechanisms that bring resources.

Despite calls for enhanced ODA and an agreed target commitment of 0.7 per cent of gross national income (GNI), donor countries have fallen woefully short of this commitment. In fact, ODA currently represents only 0.36 per cent of the combined GNI of the member countries of the Development Assistance Committee, let alone the proportion of ODA dedicated to decent work and social protection (OECD, n.d.) .

With the emergence of the COVID-19 crisis, the vision for and perspectives on ODA flows have transformed. From some perspectives, the critical role of social protection and health during this period has made international partners more conscious that ODA for these sectors should be expanded and protected, or at least that there should be no cuts during macroeconomic complications (OECD 2020).

b) Method of estimation

When evaluating the potential of ODA flows for social protection, it is critical to first observe whether the available information refers to total ODA flows or to ODA flows for social protection.

c) Sources of data

Information to analyse the potential of ODA in fiscal space creation can come from the following links (for the corresponding country or group of nations under assessment).

- ▶ Official and private flows at [OECD International Development Statistics](https://stats.oecd.org/Index.aspx?DataSetCode=CRS1) (see also <https://stats.oecd.org/Index.aspx?DataSetCode=CRS1>); request DAC-5 Codes 120, 121 and 122 (health) and DAC-5 Code 160 and CRS Code 16010 (social protection)
- ▶ [World Development Indicators](#), World Bank (keyword ODA)
- ▶ Country-specific ODA reports

Several countries publish annual or regular reports on the level, dynamics and distribution of ODA flows received. This should be checked with the ministry of finance, the ministry of planning, the ministry of foreign affairs or the ministry of welfare, depending on the institutional structure of the local government.

ODA reports of agencies and donors

Individual development agencies and donors also publish periodical reports on their activities that may be relevant for the case under consideration. Some of the agencies with extensive presence include the World Food Programme, the Norwegian Refugee Council, Save the Children International, the United States Agency for International Development, the United Nations family of organizations (UNESCO, UNICEF, FAO, ILO, UNDP), the Danish Refugee Council, Action Against Hunger, CARE, Doctors Without Borders, Oxfam and World Vision, among others. A detailed list of non-government organizations and similar entities can be found at the Berkeley Library guide.³⁰

d) Special considerations

The following issues should be considered when analysing the suitability of ODA as a source of resources for social protection in the country or region of interest.

- ▶ Because ODA flows for social protection are small, the analyst or consultant should consider the use of this source in specific situations or for some particular activities, such as technical assistance, demonstration projects and temporary support in fragile, post-conflict or post-catastrophe situations.
- ▶ Potential macroeconomic effects of large ODA flows in a country, especially in the form of exchange rate appreciation and inflation, are usually a point of concern. However, it is important to remember

³⁰ See <https://guides.lib.berkeley.edu/c.php?g=496970&p=3626027>.

that inflows from ODA are often spread out over time, so the shock on the exchange rate may not be significant.

- ▶ Volatility and predictability of future inflows are by far the most important concern for the financing of social protection. Given the constant changes in the international realm, long-run planning of ODA may be difficult to predict.
- ▶ The institutional capacity of a country to manage expanding flows is another fundamental concern because money availability is just one piece of the puzzle. If the institutions are not able to adapt and adopt the procedures established by donors, under-execution will be the norm.

The analyst or consultant should also pay attention to the fiscal and institutional considerations of scaling up ODA-financed interventions and the implications for future social protection.

A more growth-oriented macroeconomic framework

a) Concept

More than a quantitative alternative option, the macroeconomic framework is a different approach to existing macro policies whereby austerity accompanied with strong fiscal deficit control and reduced inflation dominate the agenda of policymakers. A new strategy may imply several realities (Ortiz et al. 2019):

- ▶ A change in the concept of macroeconomic stability could include supporting growth, reducing unemployment and reducing poverty, in addition to controlling low inflation and fiscal sustainability.
- ▶ Strong fiscal austerity should be modified to give the government the chance to expand public expenditure in social programmes and physical investments. Higher but reasonable fiscal deficits should be allowed to finance social protection programmes, among other strategic interventions.
- ▶ Extended borrowing is accepted without jeopardizing overall stability. This point of equilibrium is country-specific and should not be subject to universal, one-size-fits-all macroeconomic standards.
- ▶ Setting inflation rates should be reconsidered so that targets are defined at higher rates than what inflation targeting models typically define.

b) Method of estimation

From a quantitative perspective, the space that the accommodating policies provide can be approximated by two means: The first to consider was previously discussed regarding debt management. It is clear that the lower the debt ratio, the greater is the space to finance social protection when using this mechanism. However, the analyst or consultant should not forget that if this alternative applies to social protection, it may also apply to other sectors, like health, the environment and education, just to mention a few. So, if there is a debt-related fiscal space, this may not go entirely to social protection, and the final distribution would depend on the political perspectives of the political party in power. Also, it is important to stress that using incremental debt to finance social protection may not be permanent, but it is a short-term, transitional way to do it while the government obtains funding from other type of sources.

The second means would be to consider historical inflation rates in the country and, based on that, define if there is some room to loosen the monetary policy and increase inflation targets. In practice, it seems that elevating the targeted inflation rate may be possible, but it usually has a low ceiling. If the country historically has a low inflation rate, the population won't accept increasing it. If the rate is usually high, people will push for a lower rate.

c) Sources of data

Inflation data may come from the statistical institute or the central banks, while debt is usually found in ministry of finance databases. If the analyst prefers a benchmark assessment, then the World Development Indicators or the International Monetary Fund databases may provide enough information for comparative performance across nations.

d) Special considerations

It is important to review the central bank legislation to understand the level of priority it gives to inflation control. Whatever the situation, it is important to stress the idea that a new macroeconomic policy is needed. This new approach should be oriented towards pro-jobs and job-friendly objectives that stimulate the creation of decent jobs, therefore creating in the medium term more solid fiscal space with more social contributions and taxes. The ILO (2022) and McKinley (2010) explored some of the alternatives that may exist in terms of pro-employment macroeconomic frameworks.

4. Feasibility analysis of fiscal space options

The final part of the fiscal space assessment involves preparing a feasibility analysis in five core dimensions (legal; political; institutional or administrative; social; and economic or technical).

The **legal feasibility** comprises an assessment of the alignment of the financing options with the normative and ethical framework ruling the country. The **political dimension** analyses the level of support that a determined option may have among the different social and political groups, including the government, employers, workers, potential beneficiary groups and other interested parties. This exercise aims at analysing the existence of support from the different socio-economic groups with direct or indirect interference in the dynamics of the respective alternative option, either as a beneficiary or financier.

The third dimension refers to the **institutional feasibility**, which entails an evaluation of the organizational capacity to adopt the selected option, including the resources to proceed and the expected timeline of implementation.

In the case of the **social feasibility** assessment, the main criteria include questions about norms, preferences for social programmes, willingness to contribute to social protection and perceptions about existing social protection programme management and outcomes, among others.

From the **economic** side, two criteria are relevant: sustainability and equity. Sustainability refers to the capacity of the source to generate sufficient funding in the long run. Effects on equity seek to assess the incidence of changes in funding sources to assess who would end up paying in each case and who would benefit from the different initiatives. In short, it is important to identify whether the option contemplated is progressive, regressive or neutral.

Table 15 presents a summarized perspective of the main results of each one of the alternative options assessed in this report. Two indicators are included in the matrix: the level of funding per alternative and the share of the financing gap that is covered by this option. In particular, this last indicator provides a complete map of the strength of each alternative, given certain initial design so it may work as an input to guide questions during the feasibility assessment. It is important to stress here that no direct comparison can be done between sources because the background assumptions of each case differs.

Table 15. Summary matrix of fiscal space results, by option

Option	Expected revenue generation (% GDP)	Gap closure (% of financing gap)
Social contributions		
VAT increment		
Income tax increment		
Financial transactions		
Tourism tax		
Debt management		
Illicit flows		
Budget reprioritization		
....		

The following are some guiding questions for each one of the five dimensions that should be considered at this stage.

Legal feasibility

- ▶ Is the proposed measure aligned with the existing normative framework in the country and the ILO Conventions and Recommendations?
- ▶ Is there any deep legal reform required to approve and implement this measure?
- ▶ Which changes should be added to the existing normative framework if this alternative is approved?
- ▶ Are the legal requirements of this option a barrier for its approval and implementation in the short term?

Political feasibility

- ▶ Which socio-economic groups may be interested and have some power to shape the decisions around this option?
- ▶ Which groups may not have channels for influencing the decision?
- ▶ What is the political position of the relevant actors that may be affected or favoured by this financing alternative?
- ▶ Which resources do relevant actors have to support or halt this specific option?

Institutional feasibility

- ▶ Does the responsible institution have the required structure to implement the selected option?
- ▶ Does this institution have sufficient competencies, experience and the human and technological resources to proceed?
- ▶ Is the approval of the option associated with changes in the organogram of the responsible entity?
- ▶ Is this option associated with a significant increment in the workload of the department or unit?
- ▶ Is this option associated with a significant increase in the budgetary requirements of the department or unit?

Social feasibility

- ▶ Which is the overall opinion about social programmes in this country, their management and outcomes?
- ▶ How likely is social group X willing to contribute to social protection financing?
- ▶ Which financing mechanism is historically preferred in this country?
- ▶ Which type of social protection programme is historically preferred in this country?
- ▶ Which are the expected benefits of intervention X in the society?
- ▶ Which negative effects, if any, are expected from expanding social protection?
- ▶ What is the level of involvement of the communities in the overall oversight of social programmes?

Economic feasibility

- ▶ Is the tax base of this option most likely to increase or decrease in the medium and long terms?
- ▶ Can the system expect a regular flow of resources over the next few decades?
- ▶ Can the system expect expenditures growing above resources generated by this option, driven by short-term or structural determinants?
- ▶ Who will pay for this financing alternative?
- ▶ Who will benefit from the social protection offered?

Based on the consultations with relevant actors, the different issues identified in the individual options and the questions posed, the analysis can proceed with the preparation of an assessment matrix using, for instance, a **stoptlight approach**. Following the matrix in table 16 for each fiscal space option, the analyst or

consultant should assign a colour that would be “green” if there is a high probability that criterion X will be met by option Y, “yellow” if the probability is moderate (“yes but...”) and “red” if the chances to fulfil the conditions or requirements are weak.

It is highly recommended to review the conclusions of this exercise during social dialogue activities to confirm the “colour” of each cell and add insights that had not yet been considered in the assessment.

Table 16. Stoplight approach to assess fiscal space options, by criterion (example template)

Option	Legal	Political	Institutional	Sustainability	Equity	Social
Tax revenues	Yellow	Red	Green	Green	Yellow	Green
Extended social insurance coverage	Green	Green	Yellow	Green	Green	Yellow
Elimination of illicit financial flows	Yellow	Green	Red	Yellow	Green	Green
Debt expansion and management	Green	Green	Green	Red	Green	Green
Reallocation of public expenditure (functional)	Yellow	Red	Green	Yellow	Yellow	Red
Reallocation of public expenditure (economic)	Yellow	Yellow	Green	Yellow	Yellow	Red
Management and renegotiation of debt	Yellow	Green	Green	Yellow	Yellow	Yellow
Fiscal and foreign exchange reserves in excess	Red	Red	Green	Yellow	Green	Green
Macroeconomic criteria that support economic growth without jeopardizing stability	Yellow	Yellow	Green	Yellow	Green	Green
Overseas development assistance	Green	Green	Green	Red	Yellow	Yellow

5. Outline for country reports

The following guidelines present the recommended structure and contents of a standard report on fiscal space for social protection.

In short, at this point, the analysis should have completed the following issues, which thus forms the template of each country report that should be produced.

1. **Preface:** overall description of the process, people and institutions involved with roles and responsibilities and flow of activities conducted during the preparation of the document.
2. **General conceptual fundamentals:** brief description of what fiscal space is and a presentation of the options that would be explored during the assessment.
3. **Overall methodological approach to fiscal space analysis:** a step-by-step presentation of how the exercise was conducted.
4. **General context in which social protection operates**
 - a. Macroeconomic context
 - b. Fiscal tendencies
 - c. Labour market performance
 - d. Demographic characteristics
 - e. Social evolution
5. **Legal, institutional and policy framework in the country**
 - a. Legislation regulating contributory and non-contributory schemes
 - b. Description of the relevant organizations in charge of managing the main programmes
 - c. Brief analysis of the main policy documents in place
6. **Analysis of social protection investments**
 - a. Brief description of main social protection programmes
 - b. Distribution of programmes (total and percentage) per contributory and non-contributory conditions
 - c. Distribution of programmes by social protection function
 - d. Social protection coverage performance
 - i. total number of beneficiaries by contributory and non-contributory
 - ii. total number of beneficiaries per social protection function
 - iii. coverage rates per potential beneficiary group (disability, children, old age, etc.) and per programme
 - e. Social protection financing and budgetary performance
 - i. Analysis of sectoral revenues (source, composition, type, etc.)
 - ii. social protection spending characteristics (percentage of GDP, per capita, percentage of public sector expenditures, composition)
 - iii. Analysis of expenditure composition by social protection function
7. **Estimation of the social protection financing gap**
 - a. Estimation of baseline cost, total and per population group
 - b. Estimation of target cost, total and per population group

c. Social protection financing gap estimation

8. Fiscal space assessment

a. Taxation

b. Social contributions

c. Illicit financial flow

d. Reallocation of public expenditure

e. Use of fiscal and central bank reserves

f. Managing debt

g. Accommodating macroeconomic framework

h. Increasing aid and transfers

i. Feasibility assessment (legal, political, institutional, governance)

9. Conclusions and recommendations

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