

To Earmark or Not to Earmark? Allocating Revenue from Health Taxes

Joint Learning Network Webinar
Pro-Poor Earmarking of Health Taxes for Domestic Resource Mobilization

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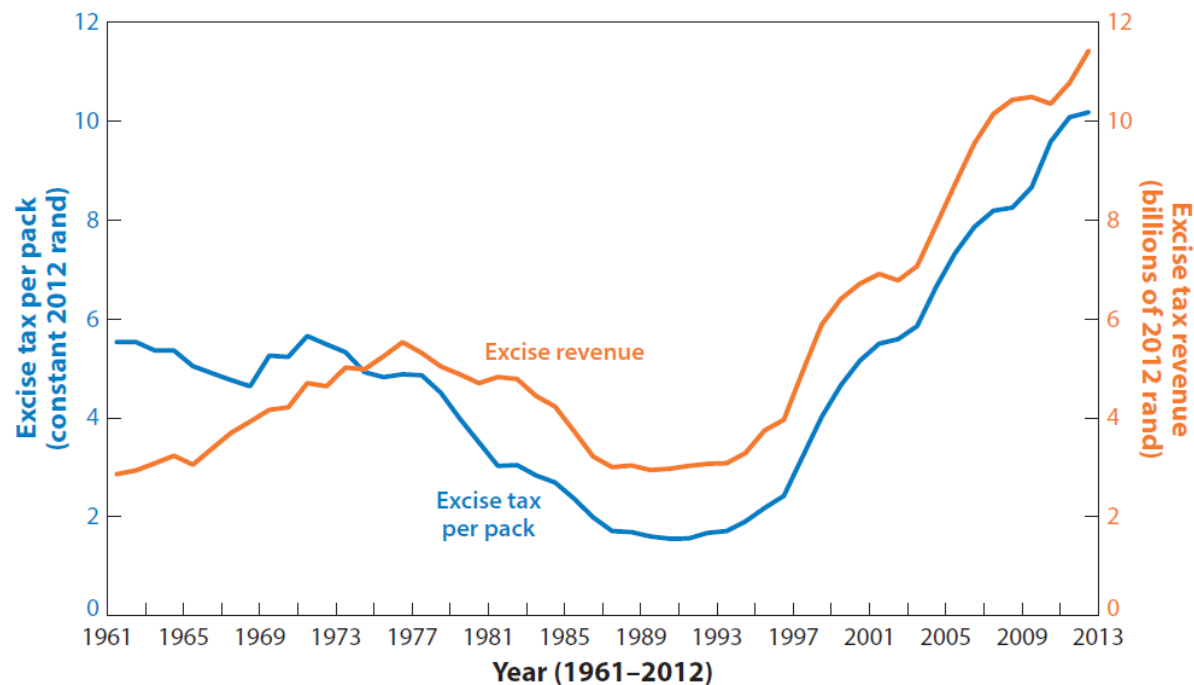


**RESULTS FOR
DEVELOPMENT**

Health tax revenue

Health taxes are “**corrective taxes**”—they encourage behavior change and generate revenue, often a lot of revenue.

Cigarette excise tax revenue in South Africa



Source: Chaloupka et al. 2019 Annu. Rev. Public Health



Allocating health tax revenue

How can governments allocate health tax revenue?

- Offset new burdens created by the tax (e.g. if the tax is regressive compensate the poor with transfer programs)
- Further the goal of the tax (e.g. allocate the tax to health promotion efforts)
- Compensate people who bear the cost from the taxed activity (e.g. allocate to the health sector in general)
- Fund unrelated public priorities



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Dedicated expenditure purpose → Earmarking

Earmarking is very common globally

64 countries
 earmark payroll
 taxes for social

3 countries
 earmark a portion
 of VAT

General revenue
 Earmarked shares
 of general revenue
 (2 countries), inter-
 governmental
 transfers (3
 countries)

Global Earmarking Practices for Health

At least 80 countries are using earmarking for health

Countries use income or payroll tax to fund healthcare for the population or formal sector workers in a public scheme.

Countries earmark a portion of their value-added tax (VAT).

Countries specify the share of total government spending that should be allocated to health.

Countries earmarked funds from debt relief.

Countries earmark all or a portion of revenues from tobacco taxes.

Countries earmark tax revenue from sales of alcohol.

Countries earmark taxes on other goods that can negatively affect health (e.g. sugar-sweetened beverages).

Countries earmark all or a portion of revenue generated from lotteries.

Countries earmark a portion of transfers from the national government to subnational governments for health spending.

Country introduced an earmarked levy on foreign personal money transfers and mobile phone company turnover.

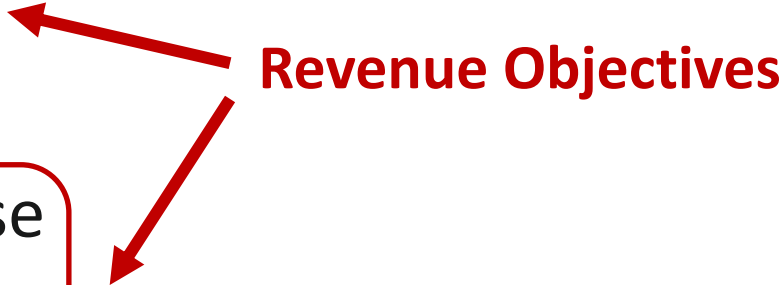
24 countries earmark tobacco taxes

20 countries earmark other health taxes

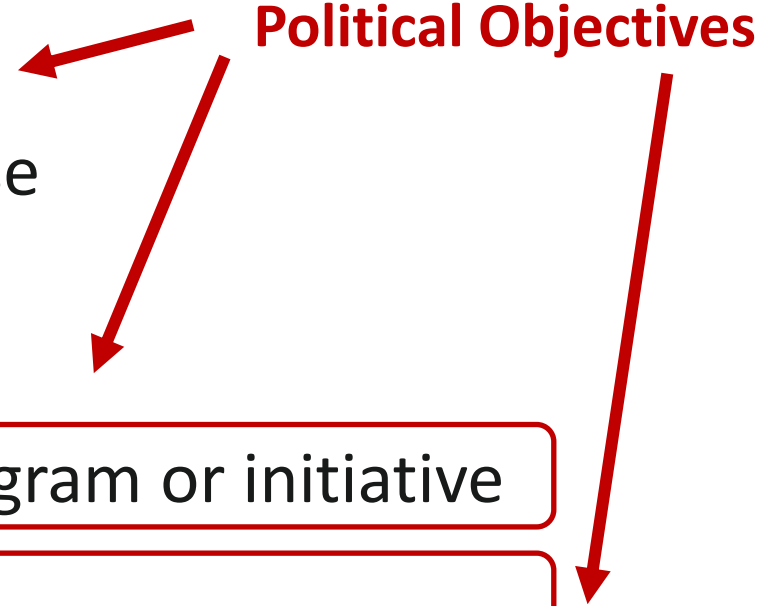
Other instruments
 Lotteries, mobile phone companies, and foreign personal money transfers



Countries have different objectives for earmarking

- Increase revenue overall for the country
 - Increase political acceptability of a tax increase
 - Increase revenue for the expenditure purpose
 - Health sector
 - A specific program in the health sector
 - Show political commitment to a popular program or initiative
 - Improve transparency in funding allocation
- Revenue Objectives**
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Pros and Cons (theoretical)



Increase revenue
Efficiency
Public support
Accountability
Cost awareness
Flexibility

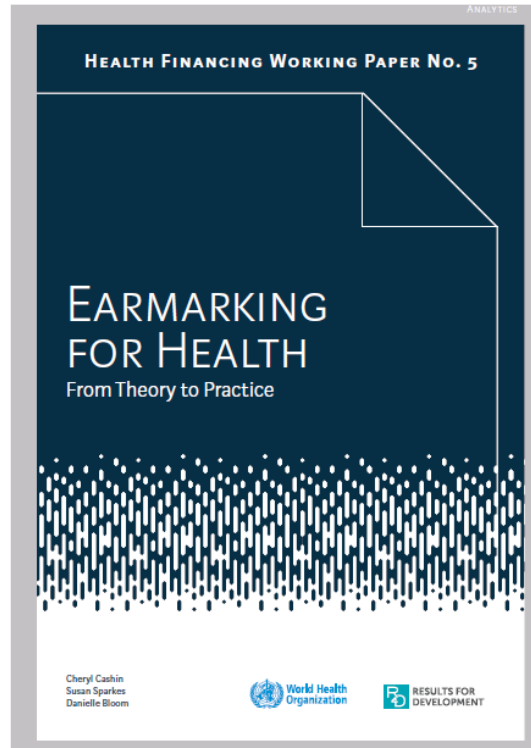


Budget rigidity
Economic distortion
Pro-cyclicality
Fragmentation
Decreased solidarity
Susceptibility to special interests

Potential Pitfalls (in practice)

- Off-setting in the budget
- Misperceptions of adequate funding
- Earmarked revenue becomes a “ceiling” for the expenditure purpose
- Defunding of other priorities

What does earmarking look like in practice?



- Earmarking typology to tease out features of design, implementation, and results
- Review of literature, published examples, and 6 country case studies of different types of earmarking for health (Estonia, Ghana, Indonesia, Philippines, South Africa, Vietnam)
- Understand whether and how earmarking is effective for meeting political and revenue objectives

Cashin C, Sparkes S, and Bloom D (2017). Earmarking for health: from theory to practice. WHO/R4D Health Financing Working Paper No.5

Does earmarking work to increase (net) revenue for the expenditure purpose?

It depends

How the earmark is designed and implemented

Underlying PFM system

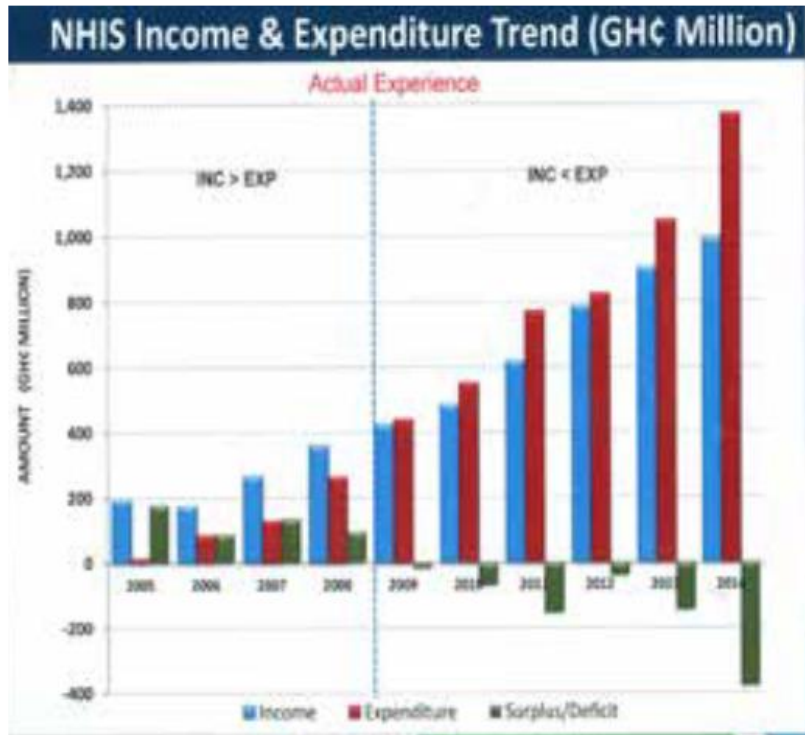
Political priorities

Time horizon

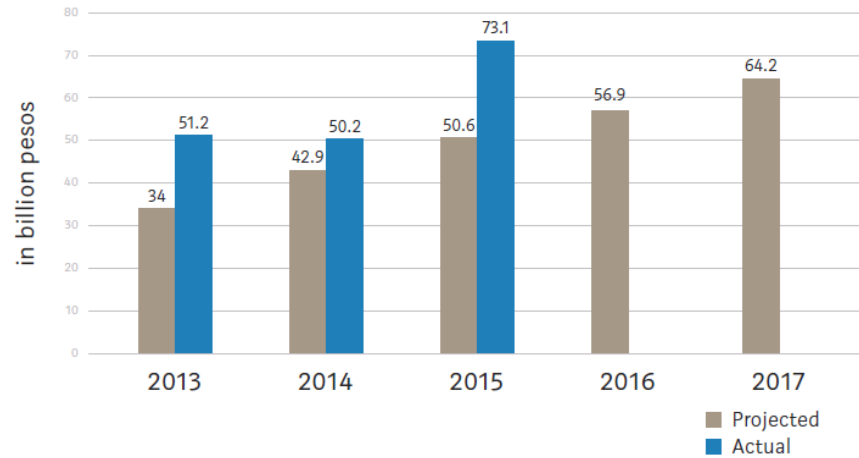


Increase in revenue from the earmark in absolute terms

Ghana



Philippines



Source: Philippines Bureau of Internal Revenue and Philippine Statistics Authority (2017)

Vietnam

2014 revenue = 299 billion Vietnamese dong (0.5% of national health budget)

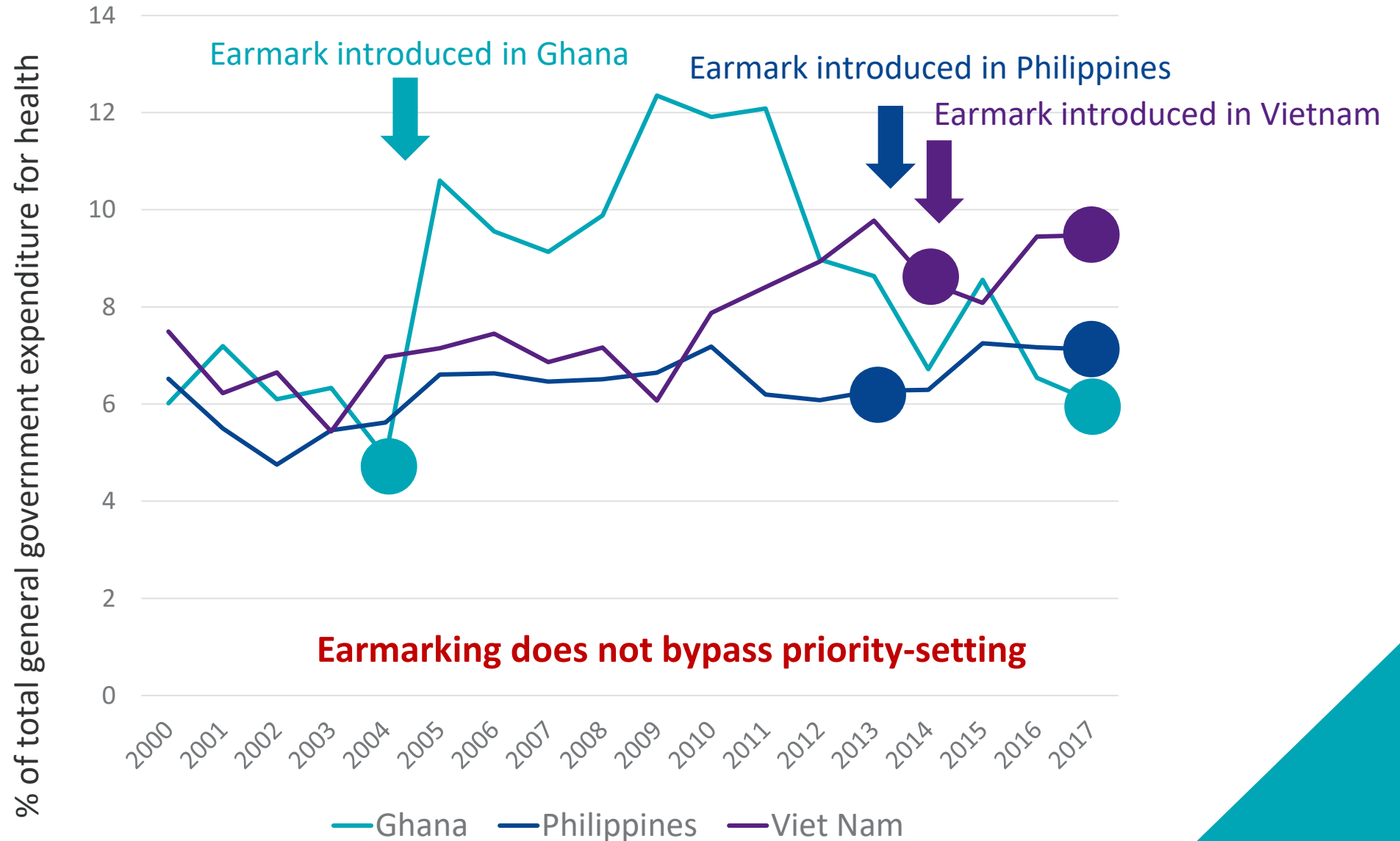


Less dramatic impact on share of the general budget allocated to health

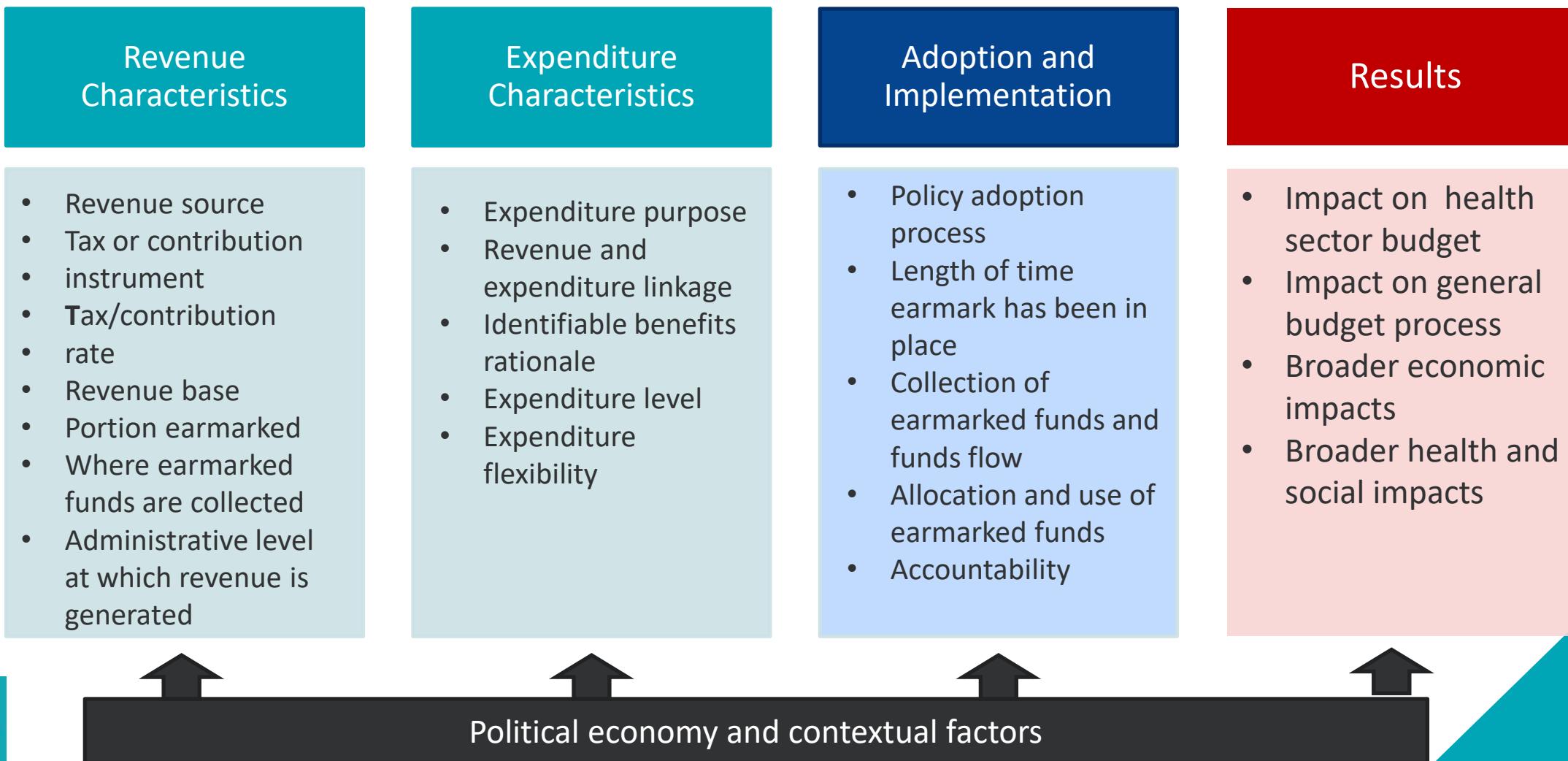
Ghana: 2.5 percentage points of VAT in 2004

Philippines: Earmarked portion of alcohol and tobacco tax increase

Vietnam: 1% of factory price of cigarettes earmarked for health promotion



Earmarking Typology



So should revenue from health taxes be earmarked for health?

- If the budget process is effective and health is prioritized, allocating the revenue from health taxes to the general revenue fund should lead to a proportional increase in the health budget—**no earmark needed**
- But—if the budget process fails to generate allocations to health that match priorities or if earmarking will make the tax more politically acceptable, **earmarking may be useful** (at least in the short term)
- It is important to avoid rigidity, fragmentation and lack of transparency
- And remember, the more successful a health tax is, the less revenue it will generate



What design features make earmarking more effective?

Soft earmarks

- **Expenditure purpose** narrow enough to be enforceable, reduce fungibility, and link funding clearly to activities **but** broad enough not to exacerbate rigidity
- Strong but flexible **revenue-expenditure link**
 - Avoid extremes of revenue entirely determining expenditure (*earmark is a revenue ceiling*) **or** expenditure driving revenue (*expenditure drives increase in tax rates*)
- “**Release valves**” allow some of the earmarked funds to be reallocated to other priorities
- “**Sunset clauses**” or at least periodic review
- Earmark funds **part of consolidated government budget** for accounting purposes

Hard earmark → all earmarked revenues must be allocated to the expenditure purpose, no more no less

Soft earmark → earmarked revenue can be diverted to other purposes or additional funds can be allocated to the expenditure purpose beyond the earmarked revenue



So you want to earmark? Here's a checklist

Support for the expenditure purpose

- Does the policy or programme to be funded with the earmark support the country's broader development objectives?
- Does the policy or programme to be funded with the earmark have broad-based support and commitment from politicians, policy-makers and the public?
- Were finance authorities part of the discussions from an early stage?

Definition of the expenditure purpose

- Is the policy or programme to be funded with the earmark defined narrowly enough for the earmark to be enforced and broadly enough to be flexible?
- Does the expenditure purpose help advance certain health sector priorities without detracting from others?

Alternative revenue sources

- Can revenue needs for the policy or programme be met through the existing budget process?
- Have alternative sources been explored for their revenue-raising potential?

Impact on health sector efficiency and equity

- Will the earmark improve or inhibit the government's ability to manage health expenditure, including implementing strategic purchasing approaches?
- Will the earmark facilitate pooling of health funds or introduce fragmentation and limit the ability to pool health funds across sources, leading to equity concerns?

Spending flexibility

- Are mechanisms in place to ensure efficient spending of earmarked revenues?
- Can earmarked revenues be spent flexibly within the expenditure purpose, or are restrictions in place related to line-item budgets or other PFM rules?
- Can unspent earmarked revenues be carried forward into the next fiscal year?

Time horizon

- Will the earmark be temporary or permanent?
- If the earmark is intended to be temporary, will it come with a "sunset clause," mandatory periodic reviews or a transition plan?
- Will the revenue source be sustainable relative to the intended expenditure purpose?

Revenue-expenditure link

- Does the policy or programme to be funded with the earmark have sufficiently diversified revenue sources so it will not completely depend on the earmarked revenue?
- Will a release valve or contingency option be put in place to reallocate earmarked funds if other urgent needs or priorities arise?
- Are expenditure management mechanisms in place to prevent overspending?

Fiscal and public financial management (PFM) impact

- Will the earmark improve or impede the efficiency of budget allocations?
- Will the earmark mitigate or exacerbate distortions or inefficiencies in the underlying revenue source?
- Will the earmark mitigate or exacerbate the equity impacts of the underlying revenue source?
- Have simulations and scenario testing been done to analyse:
 - Impact on the health sector budget
 - Impact on the total government budget
 - broader fiscal, economic and social impact
- Will the above analyses be updated periodically?

Managing earmarked funds

- Will the funds flow through the treasury or a consolidated fund into an extrabudgetary fund, or will they go directly to an implementing agency?
- Will the institution that spends the earmarked revenues be prepared for the inflow of funds?
- Will a reserve fund or contingency fund be created to manage revenues in excess of expenditure needs?

Accountability

- Have assessments been conducted at all levels of the system to ensure sufficient capacity to manage and monitor the flow of earmarked funds?
- Can earmarked revenues be accounted for at every step, from collection to expenditure?
- How will the institution that spends the earmarked revenues be accountable for results or outcomes?



Thank you

