



# UNION OF THE COMOROS

## SELECTED ISSUES

January 2024

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# UNION OF THE COMOROS

## SELECTED ISSUES

December 1, 2023

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# COSTING AND FINANCING OF SOCIAL DEVELOPMENT GOALS IN COMOROS<sup>1</sup>

## A. Executive Summary

*Comoros is committed to achieve Social Development Goals, but progress has been limited. The substantial cost of achieving SDG, 18.8 percent of 2030 GDP, is due to the country's very low starting point and the inherent difficulties associated with its small size – that limited economies of scale in delivering public services. The persistently very weak domestic resources are another reason for the substantive cost of achieving SDGs. The ongoing commitments of the authorities in the ECF program, with a focus on enhancing domestic revenue mobilization is a key to achieve better outcomes in this area. The fiscal space generated by the program could be both used to restore debt sustainability and to accelerate the achievement of SDGs in Comoros.*

## B. Context

**1. Comoros is committed to achieving the Sustainable Development Goals (SDGs), but progress has been limited.** In the 2023 SDGs ranking, Comoros stands at 154 out of 166, and is the lowest ranked among small developing states. The evaluation reveals limited progress in 60 percent of the SDGs, with 26.7 percent showing a decline. Life expectancy, standing at 67.4 years, falls below the SDG red threshold<sup>2</sup> of 70 years, positioning Comoros among countries with lower life expectancy rates globally (Figure 1). Access to improved water sources is limited, with 25 percent of the population lacking such access, and with no progress since 2007. Comoros faces significant difficulties in establishing an efficient solid waste management system, jeopardizing environmental sustainability and public health.

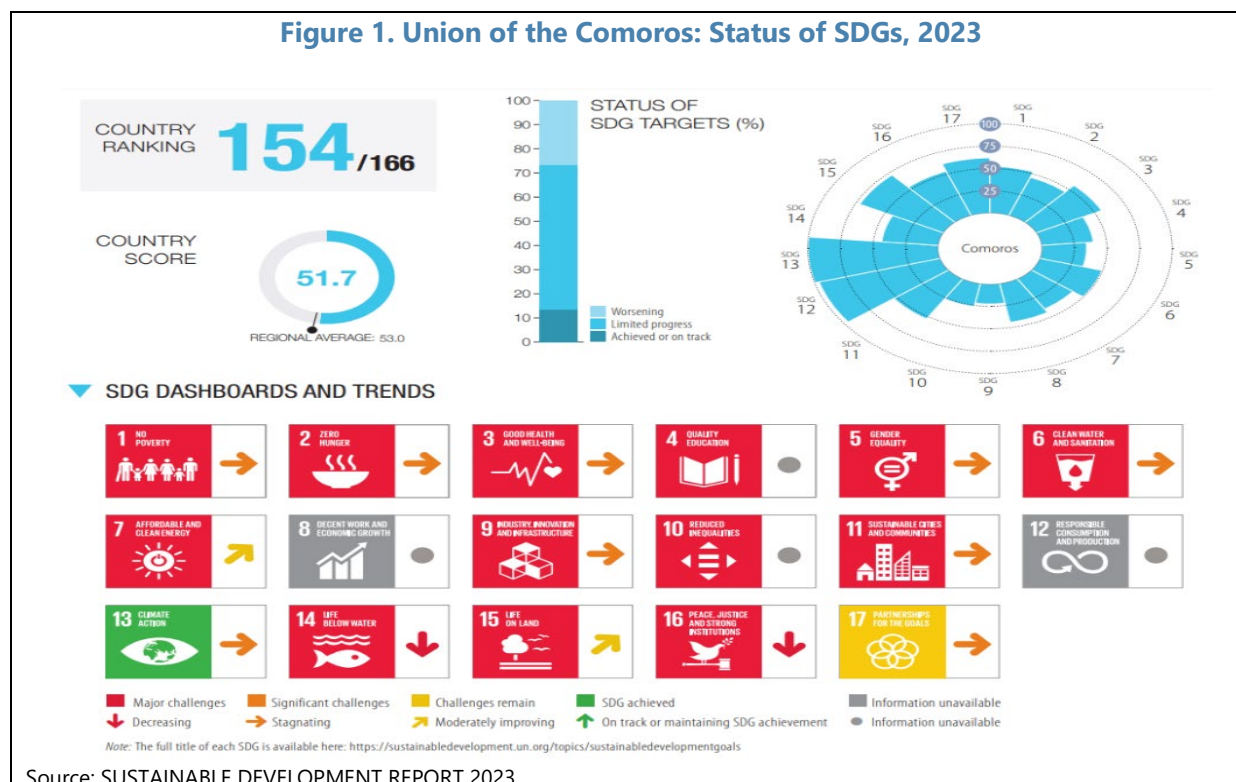
**2. Comoros has made limited progress in reducing poverty in recent years.** The nation's poverty rate stands at 36 percent.<sup>3</sup> During the COVID-19 pandemic, Comoros managed to lower its poverty rate mainly due to increased remittances and the successful implementation of the World Bank-funded cash transfer programs. However, the negative consequence from COVID-19 may materialize later on human capital accumulation as the most recent statistics have shown a lower school enrollment rate in 2022-23 and a lower vaccination rate during the pandemic.

<sup>1</sup> Prepared by Laila Drissi Bourhanbour. Helpful support provided by Mogues Tewodaj, Bounader Lahcen and Kim Yujin.

<sup>2</sup> The term "red threshold" refers to a critical level or limit that, if surpassed, indicates inadequate progress or failure to meet a specific target or indicator within the SDGs methodology.

<sup>3</sup> Poverty headcount ratio at \$3.65/day (2017 PPP, percent)

Figure 1. Union of the Comoros: Status of SDGs, 2023



3. This paper uses two models—a costing model and a financing model—to illustrate the large costs of reaching some of the SDGs related to social, human capital and infrastructure by the target year of 2030 and to highlight particular cost drivers. The cost to achieve the SDG outcomes of high-performing peers is about 18.8 percent of 2030 GDP. If the authorities tried to achieve the SDGs by 2040, the additional annual cost is estimated between 5.7 and 7.6 percent of GDP per year depending on the policy scenario.

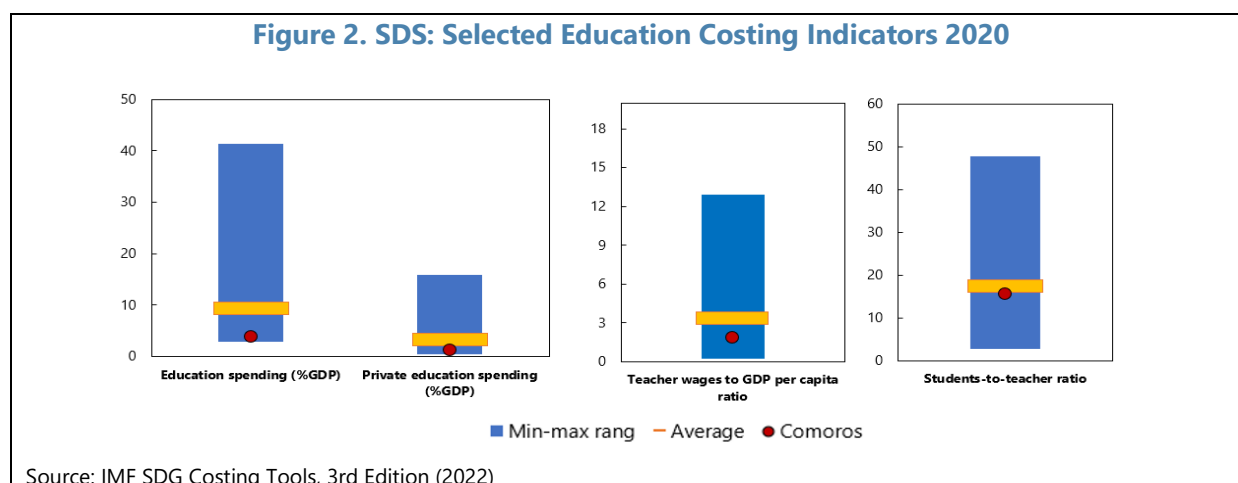
### C. Costing Model for Social, Human Capital, and Infrastructure SDGs

4. The costing methodology requires comparing Comoros with peer countries. The per capita costs of public goods tend to be higher in small countries, where a limited taxpayer base must cover these expenses. For example, small developing states on average allocate a higher proportion of their GDP to education and health, standing at 9.8 and 7.2 percent respectively compared to the world average of 6.5 and 6.9 percent. Given this, this study considers in Comoros' peer group the best performers among the small developing states (SDS) to provide a more accurate assessment of the costs of achieving SDGs<sup>4</sup>.

<sup>4</sup> The sample is chosen among the SDS of the WB and the IMF: Antigua and Barbuda, Bahamas, The Barbados, Belize, Bhutan, Botswana, Brunei, Darussalam, Cabo Verde, Comoros, Djibouti, Dominica, Equatorial Guinea, Eswatini, Fiji, Gabon, Gambia, The Grenada, Guinea-Bissau, Guyana, Jamaica, Kiribati, Lesotho, Maldives Mauritius, Micronesia, Marshall Islands, Namibia, Nauru, Palau, Samoa, Seychelles, Solomon Islands, St. Kitts and Nevis St. Lucia, St. Vincent and the Grenadines, Suriname, São Tomé and Príncipe, Tonga, Timor-Leste, Trinidad and Tobago, Tuvalu, Vanuatu.

## Education

**5. Progress in achieving better education outcomes remains limited.** The 2023 SDG evaluation does not include the assessment of the “SDG4 quality of education” due to missing data (see Figure 1). The most recent data, going up to 2018, indicate that within the SDS, Comoros is ranked second to last regarding access to pre-school and net enrolment in primary education. These data do not capture the impacts of Cyclone Kenneth in 2019, which destroyed or partially destroyed 38 percent of the country's classrooms and school closures during the COVID-19 pandemic. Indeed, following the pandemic, the Ministry of Education noted a significant drop in enrollment rates for pre-primary and primary levels<sup>5</sup>, consistent with UNICEF's warnings about extended school closures discouraging children from returning to school.



**6. Educational expenditure in Comoros is among the lowest in SDS,** amounting to 3.8 percent of GDP, while household contribution to education spending is similar to the SDS average (33.5 percent compared to 33.9 of total spending on education). Comoros boasts a favorable student-to-teacher ratio of 15.6 compared to the high-performing SDS' average of 18.6, overperforming the international standards. However, teacher wages in Comoros, 1.8 of the GDP per capita, stand at only half of the SDS average, which may negatively affect teachers' motivation and, consequently, education quality. Moreover, capital spending on education in Comoros only stands at 36 percent of the average SDS composition, which could hinder the availability of suitable infrastructure and educational facilities.

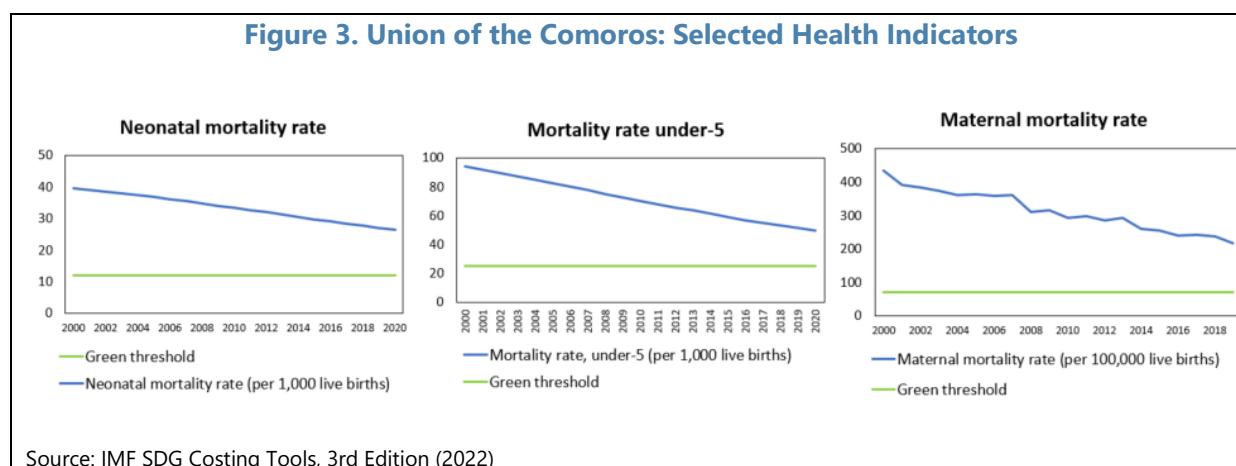
**7. Additional spending needs to achieve SDG4 (education) by 2030 are estimated to be about 4.2 percent of 2030 GDP.** The required spending reflects both a need to increase the teacher wage bill to improve teacher productivity and to raise capital spending for school construction and infrastructure improvement, such as the availability of bathrooms, electricity, drinking water, and school boundary walls. Two mitigating factors have helped contain these expenditures:

<sup>5</sup> Rapport final des consultations nationales en préparation du sommet sur la transformation de l'éducation (2022).

- (i) Aligning the currently favorable student-to-teacher ratio to the average of the SDS would not require hiring more teachers. Keeping the current ratio would have raised the additional financing by 0.4 percent of GDP. This favorable ratio is most probably attributed to a “ghost workers” presence in the education system. Authorities are actively working to address this concern within the ongoing ECF program.
- (ii) The demographic dividend resulting from a lower proportion of children requiring enrollment in schools translate into a saving of 0.5 percent of GDP.

## Health

**8. Health outcome indicators have improved but remain well below their thresholds.** Life expectancy improved by five years between 2000 and 2019, but at 67 years it remains well below the green threshold<sup>6</sup> of 80 years and all the mother and child indicators, despite improving, are still exceeding the green threshold (Figure 3). While the COVID-19 pandemic has claimed relatively fewer victims in Comoros, it remains to be seen if there will be long-run consequences related to the low vaccination rate.



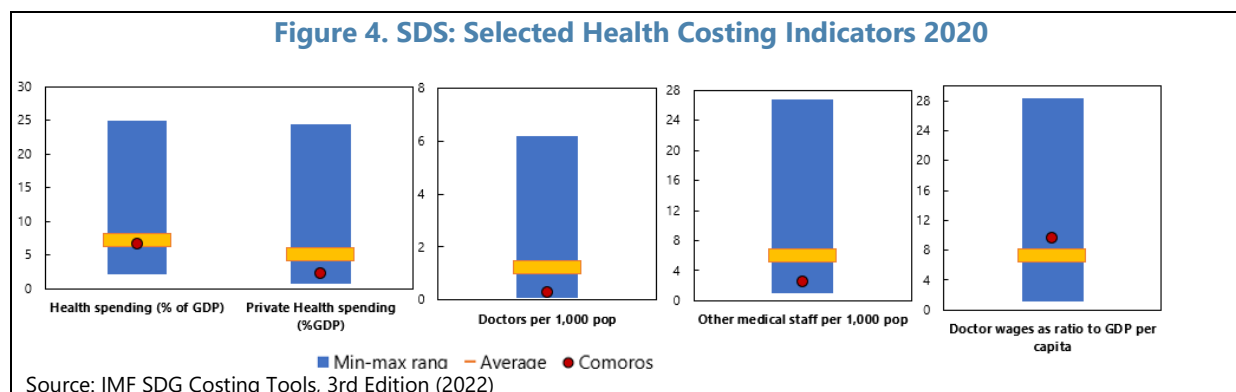
**9. Health spending in Comoros aligns with the average among SDS.** However, the ratio of doctors per 1000 habitants is among the lowest in the sample. Spendings primarily reflects a higher-than-average private expenditure: 66.4 percent of total health spending. However, this high level of private spending does not necessarily correlate with superior health outcomes. It is largely driven by health spending abroad, stemming from a shortage of high-quality domestic health services. This was one of the motivations for the government to embark on the major project to construct the El Maarouf national hospital, which has been the main driver of higher infrastructure spending in the health sector.

**10. The additional spending needs in health care are about 4.3 percent of 2030 GDP.** To achieve higher performance in the health SDG, the number of doctors should be increased tenfold.

<sup>6</sup> An indicator is green if it meets the target of the SDG methodology.



The number of other medical personnel, currently far below the high-performing countries, should be tripled from its current level. The only cost-mitigating factor here is the doctors' wages that could be limited to 7.3 instead of 9.6 percent of per capita GDP, as in high performers. However, the last WB report on public expenditure<sup>7</sup> point to a very low productivity of staff in the health sector both in the public and private sector<sup>8</sup> as manifested from the very low service use. Tackling this issue could be the most important cost-mitigating factor.



## Electricity

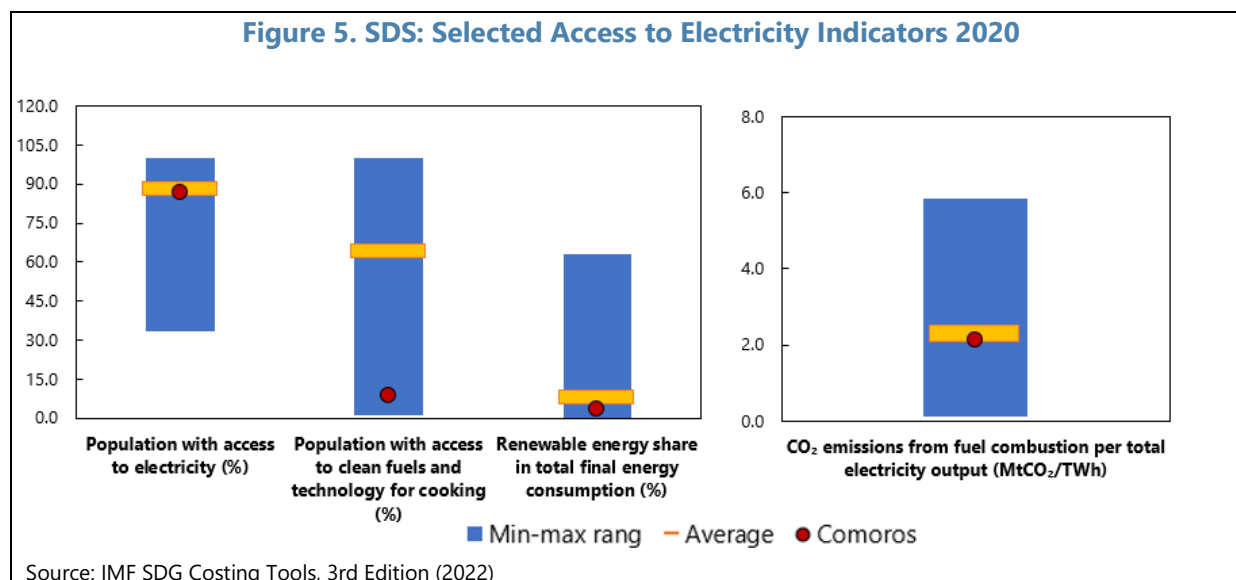
**11. While access to electricity is close to the average of the SDS, the per capita electricity consumption is the second lowest in the sample.** Inadequate infrastructure for power generation and distribution leads to frequent power cuts and an unreliable energy supply. Despite an installed generation capacity of approximately 44 MW, utilization is hampered by operational limitations and inadequate maintenance practices. Consequently, the country's energy consumption stands merely at 0.2 ton of oil equivalent per capita, significantly below its potential. The sector faces a structural challenge due to insularity and the small size of the market which does not promote economies of scale. The cost of electricity in Comoros is among the highest in Africa (0.30 US\$/kWh), mainly due to the inefficiency and amortization of the diesel generators. The high production costs are exacerbated by energy losses during the distribution exceeding 50 percent, the highest metrics of such losses on the continent. The lack of cost recovery, with merely about one-third of invoiced energy bills recuperated, constrain the national electricity company's financial situation, hindering its capacity to invest in infrastructure upgrades and expansion.

**12. Although Comoros has the potential for renewable energy, especially solar and wind, the utilization of these resources is still embryonic.** Following the community's rejection of a heavy fuel oil project in 2015, investments have focused on clean energy, reflecting both global

<sup>7</sup> World Bank. 2023. [2022 Comoros Public Expenditure Review](#).

<sup>8</sup> "A health professional in a public facility sees, on average, fewer than 2 patients a day. Productivity is slightly higher in the private sector, where providers see, on average, 4 patients per day, which is still extremely low. Similarly, the country's 587 midwives assisted 15,061 maternal deliveries in 2020, representing about 2 deliveries per midwife per month." World Bank (2023).

trends and local preferences for sustainable energy solutions. The two first solar energy stations<sup>9</sup> were implemented by two independent private producers and have added 5 MW to the total energy capacity of the country but they have very high operating costs due to inadequate technology.



**13. To achieve SDG7 by 2030, the associated cost is estimated at 3.7 percent of GDP per year.** This estimate reflects the expansion of electricity access from the current 86.7 percent to 100 percent of the population and elevating the average electricity consumption per user from 88.3 kWh to 1,463.9 kWh, aligning with the average consumption of the sample group. The investment costs per kW of energy produced, which include expenses for generation, transmission, and distribution correspond to investment cost of the ongoing solar energy project of World Bank's. Thus, the additional costs factor in cost of solar energy.

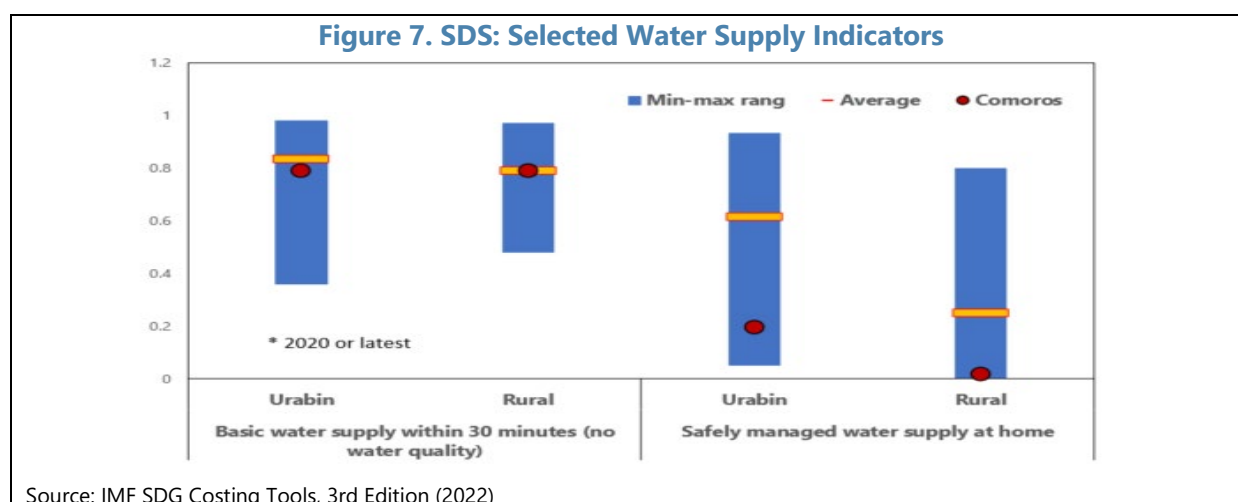
## Road and Water

**14. The road network in the Comoros is relatively limited, both in terms of coverage and quality.** Major towns and ports are connected by main roads, but many of them are in need of maintenance and upgrade. Paved roads are concentrated primarily in urban areas, while rural regions are often serviced by unpaved tracks that can become impassable during the rainy season. The narrow and winding nature of many roads, combined with occasional steep terrains, makes travel time-consuming. Poor quality infrastructure, mostly roads, and related services constitute one of the main constraints to economic diversification in Comoros. The rehabilitation and, to a lesser extent, extension of the national road network will contribute to the development of the tourism and fishing sectors identified as potential growth poles for the national economy. Increasing rural access from the currently low 24.3 percent to 75 percent by 2030 will require investing the

<sup>9</sup> The first station started operation in 2020 in Anjouan Island, and the second 2021 in Grand Comores. The second project was financed on online lending platform.

equivalent of 4.7 percent of GDP every year from now to 2030 on about 838 additional kilometers of all-weather roads which is more than doubling the current network.

**15. In the 2023 National voluntary report on SDGs achievement<sup>10</sup>, Comoros acknowledged substantial barriers in achieving SDG6 targets as universal access to drinking water is very low at 15 percent.** The level of access has not improved since 2012 and access to sanitation facilities is almost non-existent. Compared to the sample of peer SDS, the performance of Comoros is among the lowest regarding the safely managed water supply at home (see figure 7). The inherent scarcity of water resources in the archipelago is further exacerbated by stormy episodes and rising sea levels due to climate change, leading to saline intrusion and water turbidity after storms. Aiming to provide safely managed water and sanitation for all would require investing the equivalent of 1.92 percent of GDP every year from now to 2030.



### Total Costing

**16. Taken together, the cost for Comoros to achieve the human capital and infrastructure SDG outcomes of high performing peers by 2030 is 18.8 percent of GDP per year.** This exercise highlights the exceptionally low starting point and extraordinary spending that would be required to meet the SDGs by 2030 as well as persistent very weak domestic resources. This kind

Education	4.2
Health	4.3
Road	4.7
Water and Sanitation	1.9
Electricity	3.7
<b>Total</b>	<b>18.8</b>

<sup>10</sup> [Commissariat General au plan \(2023\). Rapport national volontaire sur la mise en œuvre des ODD en Union des Comores.](#)

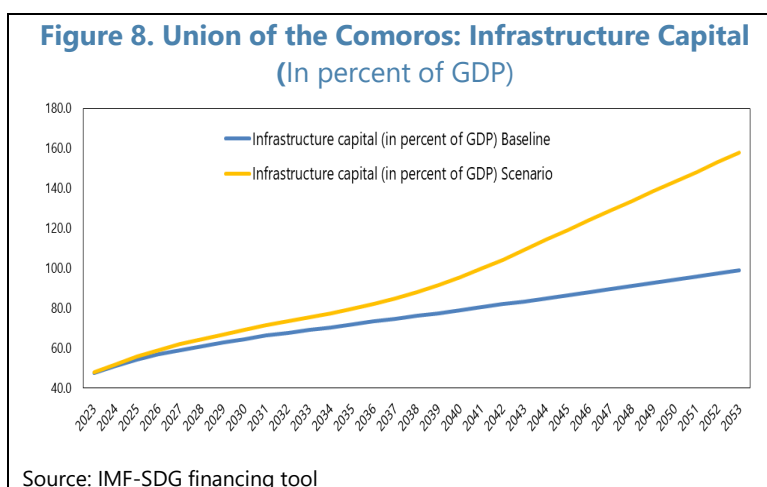
of spending is out of reach for the country, given limited resources and debt sustainability considerations. In the next section, we consider feasible macroeconomic and financing scenarios and explore the timeframe over which SDGs could be reasonably achieved in Comoros.

## D. Financing for the SDGs

**17. Although it is unlikely that Comoros could achieve the human capital and infrastructure SDGs by 2030, there are scenarios under which such progress could be achieved over a longer timeframe.** The SDG financing tool (Benedek, et al, 2021) is a framework that helps to identify such scenarios. It evaluates the financing needed to achieve the SDGs in a macroeconomically consistent and dynamic setting. The tool allows the user to take as given the SDGs' needs as outlined in the previous section and assesses the economy's capacity to generate alternative financing options, including domestic revenue mobilization, private sector funding, and support from the international community. In particular, the framework gauges whether and how the SDGs can realistically be achieved by 2030 and, if not by 2030, then by when. It then uses different scenario assumptions to determine how large the remaining financing gap is, on average, between the current and target years. The tool is dynamic, with projections up to 2053, and with a production function that assures that output is consistent with spending on human capital (education and health) and physical capital (roads, electricity, and water and sanitation). The simulations include a set of accounting identities throughout the real, fiscal, and external sectors to ensure macroeconomic consistency.<sup>11</sup>

### 18. We explore two scenarios: the non-program and the ECF scenarios:

- The non-program scenario reflects the macroeconomic assumptions at the completion of the Staff-Monitored Program (IMF Country Report No. 23/143). Under this scenario, a gradual fiscal consolidation would start in 2024, reducing the deficit by about 3.5 percent of GDP by 2027. But substantial financing gaps would emerge in 2023 and public external debt rises to around 40 percent

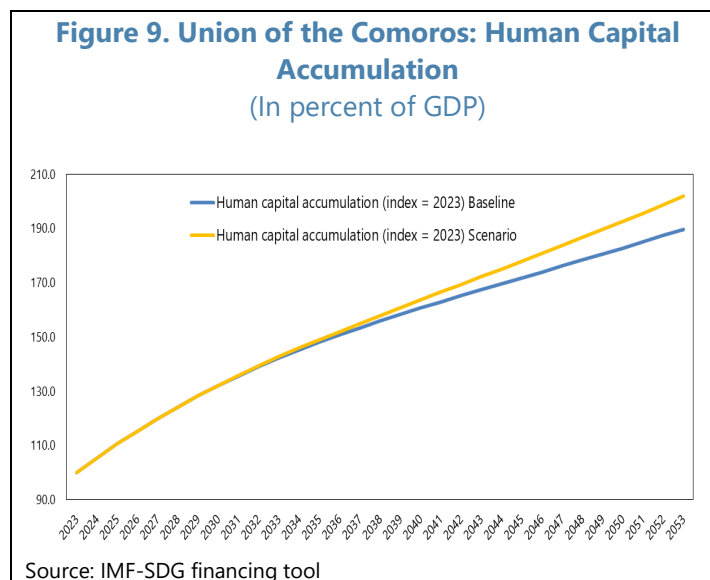


of GDP over the medium term, reflecting low expected revenue, the restructuring of SNPSF, and debt service obligations from non-concessional borrowing. Under this scenario, Comoros would

<sup>11</sup> Few caveats should be acknowledged. First, as is the case in exercises using dynamic models, the model results are sensitive to the assumptions. As such, the model results should be regarded as illustrative only. Second, the model by design provides an estimate of the financing needed to support the estimated costs to achieve the SDG thresholds but is not a policy prescription.

not be expected to reach the SDGs by 2053 (the final year considered by the financing tool). Alternatively, the country could achieve the SDGs by 2040, with additional annual spending of 7.6 percent of GDP per year.

- The ECF scenario builds on the SMP scenario by assuming a progressively higher tax revenue by 0.3 percent of GDP each year, during 2023–43, from the very low level of 8.6 percent in 2023 to 14.6 in 2043. The increase is achieved through: (i) phasing out of tax exemptions, commencing with the elimination of the sales tax exemption for construction materials, (ii) enhancing the efficiency of large and medium taxpayers' units, (iii) expanding the taxpayer base by 10 percent within the large and medium taxpayer offices and (iv)



strengthening risk management within the Customs administration and finalizing the customs procedures framework. The active program scenario affords the authorities greater fiscal space, that is used both to restore the debt sustainability and to build human and capital infrastructure (see figure 8 and 9). Under this scenario, it would still be impossible to reach the SDG before 2053 but the cost to achieve the SDGs by 2040 decline to 5.7 percent of GDP per year.

**19. The remaining financing gap from the ECF consistent scenario could be mainly fill with grant and concessional financing to achieve the SDG by 2040 while maintaining debt sustainability (figure 10 and 11):**

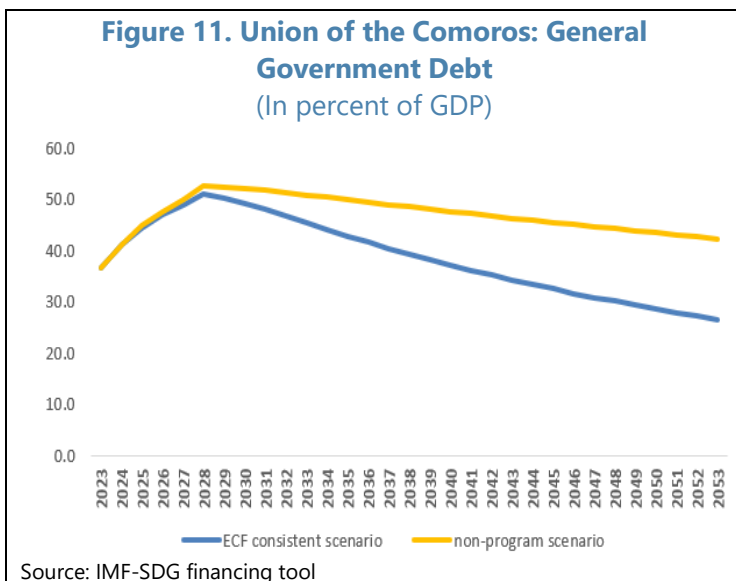
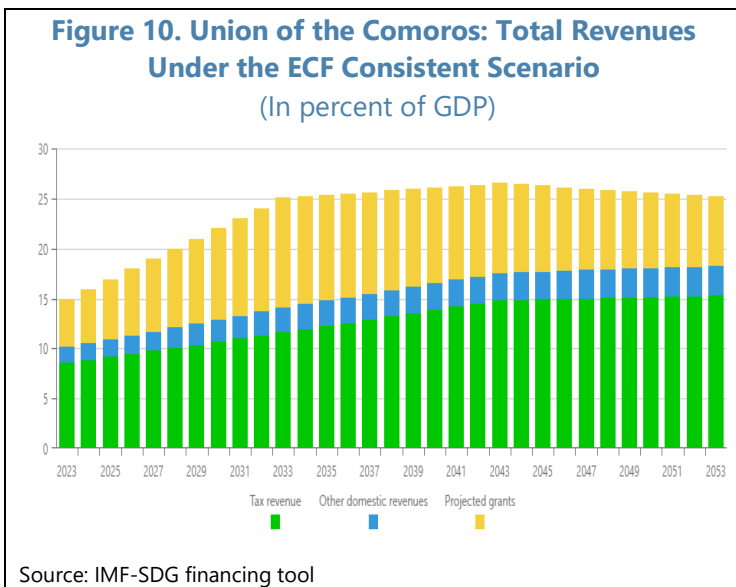
- Education: the sector used to mobilize around 1.4 percent of GDP as annual financing in the form of grants<sup>12</sup>. Despite the challenges linked both to Kenneth cyclone and the COVID-19 pandemic, grant mobilization has remained sluggish, constrained mainly by the capacity absorption of the country. Recently a local group of education partners<sup>13</sup> has committed to help Comoros achieve the SDG4. It is expected that the financing will be as in the past only grants.
- Health: Prior to the COVID-19 pandemic, the sector resource mobilization from partners was limited to 0.6 percent of GDP. This contribution jumped to 1.7 percent in 2020 and 3.4 percent in 2021. It is expected that partners' support to Comoros will continue especially from the multiple UN system agencies as well as World Bank and Agence Française de Développement (AFD).

<sup>12</sup> Data on grants are from OECD (2023), "Detailed aid statistics: Official and private flows", OECD International Development Statistics (database), <https://doi.org/10.1787/data-00072-en>.

<sup>13</sup> June 2023. The group include AFD, UNICEF, World Bank, Dubai Care.

Beside the ongoing disbursements for the El Maarouf Hospital included in the baseline, remaining additional cost would be financed by grants.

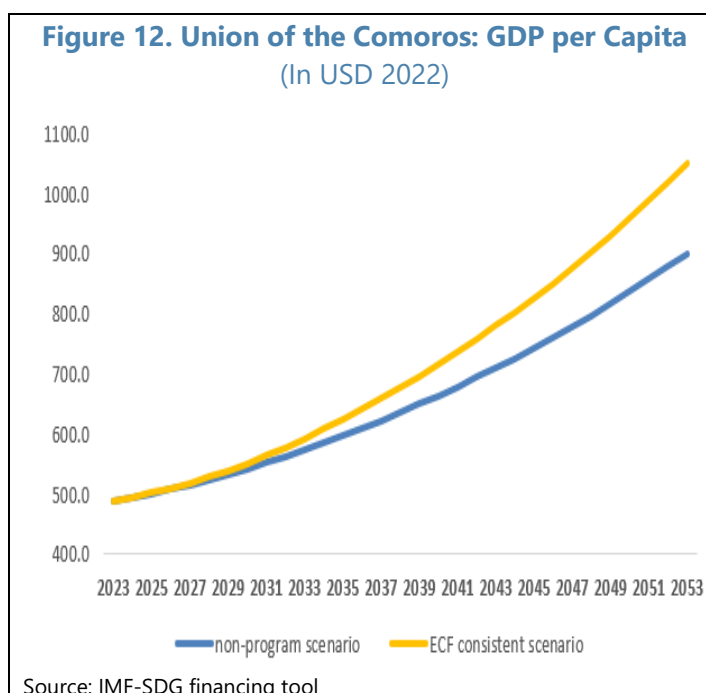
- Road: Grant financing to this sector is limited (0.3 percent of GDP per year). However, the sector benefits from concessional loan mainly from African Development Bank (AfDB) and Saudi Arabia. So, this sector is expected to benefit from small additional concessional loans and additional contribution from the private sector. According to anecdotal information the involvement of the diaspora in the infrastructure of the villages including roads is crucial (remittance is around 21.5 percent of GDP in 2022).
- Water and sanitization: Significant improvement of the situation could be expected from the UNDP project aiming to ensure climate resilient water supplies on the islands. With a budget of approximately USD 60.75 million as grants financing, the project seeks to bolster the resilience of water supply infrastructure for drinking and irrigation and directly benefit around 470,000 residents. In addition, 800,000 individuals are projected to reap the rewards of enhanced national and sub-national climate-resilient water governance in Comoros.
- Energy: The major ongoing project, the Comoros Solar Energy Access (CSEA), is financed by the World Bank, with an ambition to bolster the national energy grid with an additional 9Mw<sup>14</sup> of solar energy and a 19Mw<sup>c</sup> storage mechanism. The project has a total cost of USD 40 million, with half of the funding provided as a grant and the other half as a loan on IDA terms. Additionally, the



<sup>14</sup> Mw<sup>c</sup> is the equivalent of MW for solar energy. MW is a general unit of power, while Mw<sup>c</sup> is specific to the peak capacity of solar photovoltaic technology. The "c" in Mw<sup>c</sup> stands for "peak," indicating that it is a measure taken under optimal conditions.

UNDEP is currently developing another project focused on geothermal energy, which aims to provide a sustainable long-term solution for energy provision in Comoros. Based on available information, it is highly likely that the project will be fully funded by grant from a range of official donors, including the European Union (EU), Agence Française de Développement (AFD), and the Fonds d'Énergie Durable pour l'Afrique.

**20. Closing the financing gap by 2040 will also require additional efforts from the authorities.** The scope for improvements in the efficiency of public spending is significant, the fiscal space created by fiscal reforms can be directed toward spending in SDG sectors. Private investments could also fill the gap, in the alternative scenario. Private investments, especially in the villages would also help to achieve the SDGs; in the alternative scenario, we assume an additional spending from private investments of 2 percent of GDP, which would be possible thanks to the high influx of remittances (21.5 percent of GDP in 2022) and the higher level of GDP per capita (figure 12).



## E. Policy recommendation

**21. The foregoing exercises highlight the very large gaps towards the SDGs for Comoros and the urgent need to begin addressing them to improve the livelihoods of the Comorian population.** While it is unlikely that Comoros would be able to attain the SDGs by 2030 or even 2040, it is crucial that actions are taken:

- Enhancing efficiency in delivering public services is crucial. Addressing longstanding challenges such as ghost employees and absenteeism, particularly in education and health sectors stands out as a significant factor in mitigating costs.
- For the energy sector, a comprehensive strategy is needed to achieve the SDG07 "Affordable and clean energy". This strategy needs to be developed with the assistance of international experts and partners as the level of complexity in this sector is very high including in contract negotiation and planification.
- Domestic policies must prioritize creating fiscal space for investments in human capital and basic infrastructure. Under the authorities' economic program supported by the ECF, this includes

sound macroeconomic management, domestic revenue mobilization, and responsible financing strategies.

- Close engagement with international partners can further mobilize budget support and project financing for priority areas. Given the fragile context and already elevated debt sustainability risks, grant financing is the more appropriate form of support.



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# TRADE LIBERALIZATION AND TAX REVENUE MOBILIZATION IN COMOROS<sup>1</sup>

## A. Executive Summary

*Trade liberalization could be associated with higher or lower trade tax revenue. For countries that rely heavily on trade tax as a source of revenue mobilization, trade liberalization could potentially lead to lower revenue. To mitigate the revenue losses in the context of Comoros's ongoing WTO accession process, immediate policy options could include removing tax exemptions and strengthening tax revenue administration to improve tax collection and combat tax fraud. The policy options over the longer term could include increasing domestic direct taxes to replace trade taxes and adopting a more efficient goods and service taxation system. Finally, any revenue replacement strategy would not yield results without the lynchpin of sound macroeconomic and governance policies.*

## B. Context

**1. Trade liberalization brings many advantages for countries by increasing consumer choice and welfare, economic growth, and efficiency of resources allocation.** Evidence of this abounds in the literature, including some as follows. Sachs and Warner (1995) demonstrate that trade openness is associated with higher economic growth in many developing countries over the 1970-1989. This finding supports Dollar (1992) who argue that trade liberalization strongly improves economic growth in a large sample of 95 developing countries over the period 1976-1985. Similarly, Edwards (1992) examines cross-sectional data for 30 developing countries from 1970 to 1982 and finds a strong positive correlation between trade liberalization and growth. Wacziarg and Welch (2008) also demonstrate that trade liberalization fosters economic growth in developing countries partly through its positive effect on investments. Relying on a sample of developing countries, Dollar and Kraay (2001) show that trade liberalization leads to faster growth and poverty reduction in developing countries. Finally, Frankel and Romer (2017) show that trade liberalization robustly and positively affect income even though this effect is only moderately statistically significant.

**2. However, trade liberalization alone is not enough to improve economic growth** (Krueger, 1998; Chang et al., 2005). Trade liberalization must be supported by sound macroeconomic policies as well as strong institutions in order to have a positive impact on economic growth. As highlighted in Vamvakidis (2002), the positive effect of trade liberalization on growth also appears to depend on the period over which the liberalization took place, with positive and significant association with growth in 62 countries over the period 1970-1990 but not during 1950-1970.

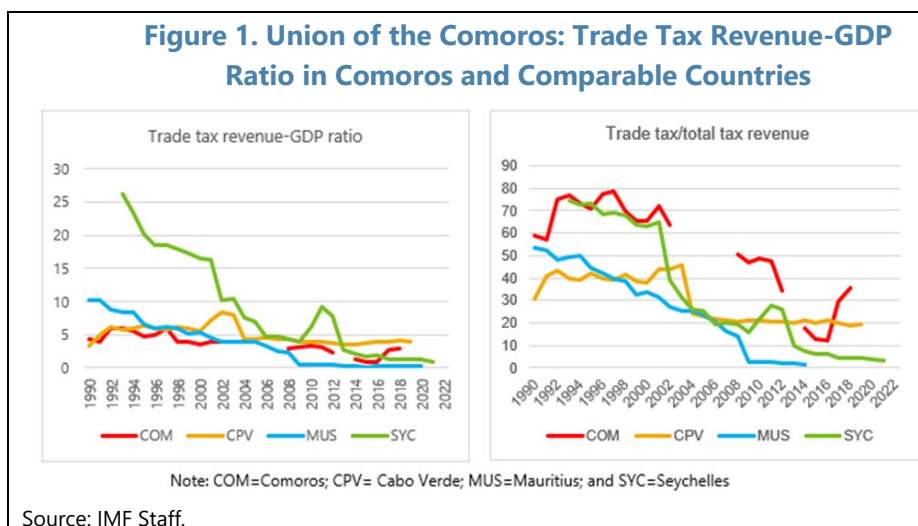
**3. Trade liberalization could also be associated with higher or lower trade tax revenue, depending on the initial effective levels of tariffs and the elasticity of import demand.** The

<sup>1</sup> Prepared by Pegdewende Nestor Sawadogo (AFR) with contributions from Benjamin Robert Kett.

evidence for the impact on government revenues of reduced border taxes is mixed, with some research pointing to an initial decrease in revenues which are only made up for after several transition years. Ebrill et al. (1999) show that tariff reduction leads to higher trade tax revenue if the initial tariff rate is high<sup>2</sup> because the price elasticities of imports are not constant. Similarly, tariff reduction may boost tax revenue collection by reducing tax fraud. Trade tax revenue also depends on the price elasticity of demand for imports. Both Ebrill et al (1999) and Agbeyegbe et al (2006), show that a higher price elasticity of demand for imports could lead to higher trade tax revenue if the volume of imports increases following trade liberalization. Over the long term, the revenue losses may be relatively low. For instance, the benefits of trade liberalization tend to be more important over the long term given that structural changes (industrialization, technologies advancements, etc.) are important drivers of economic growth. Accordingly, the elasticities for import demand tend to be higher over the long term given the potential positive effects of trade liberalization on economic growth.

**4. For countries that rely heavily on trade tax as a source of revenue mobilization, trade liberalization could potentially lead to lower revenue.**

Trade taxes constitute an important component of tax revenue in developing countries, particularly in small developing states (SDS), given these countries' high dependence on international trade.

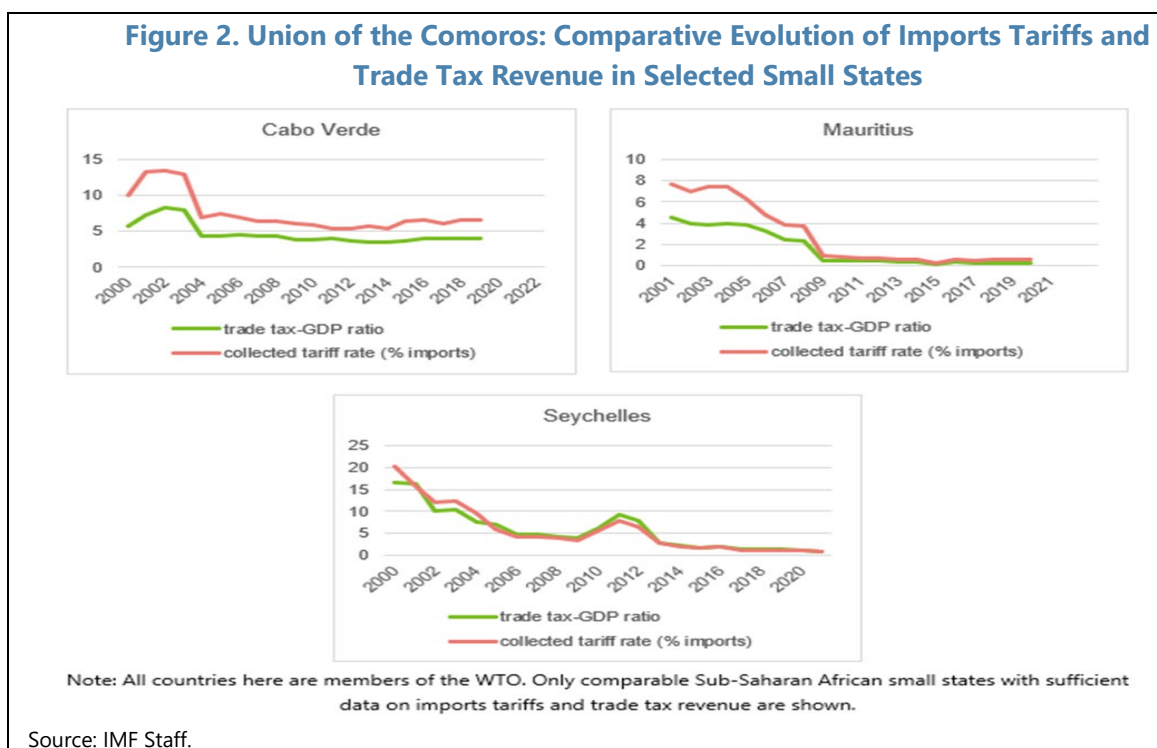


The strong reliance of SDS on trade tax may be explained by the small market size, the lower international competitiveness, and the narrow tax base<sup>3</sup>. Limited institutional capacity (weak supervision of the staff, weak management, vulnerability to corruption) may also explain the strong reliance on trade taxes which are relatively easier to administer. For SDS, trade liberalization and reductions of trade taxes have been associated with lower trade tax revenue (Peters, 2002; Agbeyegbe et al., 2006) and could pose a significant challenge for revenue mobilization. In Comoros, while the average trade tax to GDP ratio (3.69 percent over 1990-2022) has been among the lowest among the Sub-Saharan African SDS, the trade tax represents a major share of total tax revenue in the country (average of 53.94 percent over 1990-2022,

<sup>2</sup> They also show that trade liberalization raises trade tax revenue by reducing tariff dispersion (lowering the higher tariffs and increasing the lower tariffs rates).

<sup>3</sup> The high level of informality, the higher dependency ratio, and the strong reliance on agriculture sector, which is difficult to tax, lead to a narrow tax base in developing countries.

Figure 1). Figure 2 shows the evolution of imports tariffs and trade tax for selected small states (comparable to Comoros) that have acceded the WTO and seen lower trade tax revenues along with the lower import tariffs rates.



**5. This paper evaluates the potential impact on trade tax revenue in Comoros in the context of its ongoing accession to the WTO.** It also discusses trade tax revenue replacement by domestic tax revenue and suggests some policy options to mitigate the potential negative effects of trade liberalization on tax revenue in the country. The rest of the paper is organized as follows: Section 2 presents an overview and progress of Comoros accession to the WTO. Section 3 summarizes the advantages and potential revenue loss from Comoros accession to the WTO. Section 4 describes the estimates of import elasticities based on the gravity model. Section 5 discusses trade tax revenue replacement strategies. Section 6 suggests some policy options and concludes.

### C. Overview of WTO Accession and the Comorian Progress

**6. The WTO currently has 164 member countries and 24 more are in the accession process, including Comoros.**<sup>4</sup> Joining the organization necessitates signing up to a wide-ranging set of rules which aim to create a balanced playing field with respect to trade competition between countries, as well as to make trade policy predictable and transparent. The accession process has numerous steps which can be exigent and necessarily take time. 36 countries have acceded since the

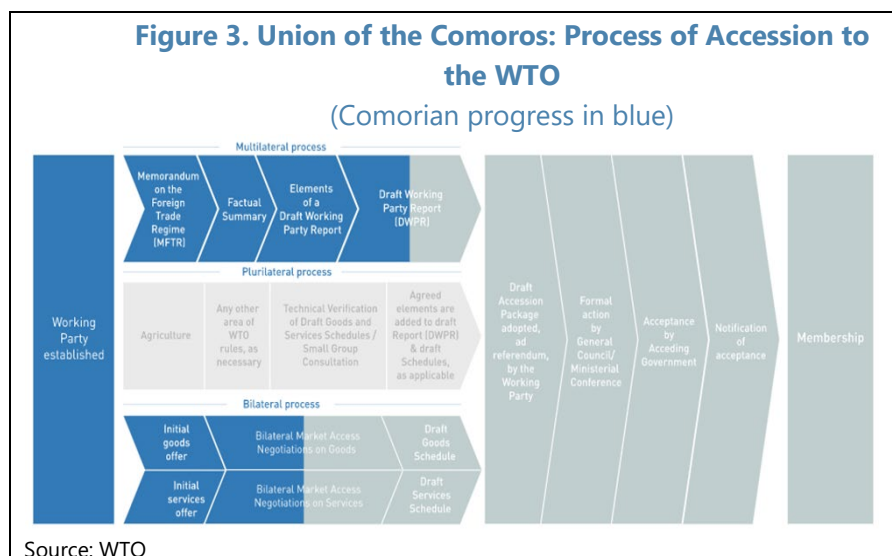
<sup>4</sup> Number of member countries: [WTO | Members and Observers](#). Acceding countries: [WTO | accession - Summary Table of Ongoing Accessions](#).

founding of the WTO in 1995, with the time taken varying from two years and ten months to 15 years and five months.<sup>5</sup> Some countries have still not successfully acceded despite having opened applications in 1995. The process, presented in Figure 3, consists primarily of negotiations between existing members and the applicant, meaning conditions for entry can vary by country, and current members have the final decision to approve accession. The process begins with the establishment of a country-specific Working Party, consisting of representatives from existing members and the acceding government, before moving to multilateral and bilateral negotiations which occur concurrently. The negotiations result in three documents: a draft working party report, a draft goods schedule, and a draft services schedule, which are then adopted by the Working Party before being voted on at the annual Ministerial Conference (needing a two-thirds majority of members).<sup>6</sup>

**7. The WTO contains provisions for Least Developed Countries (LDCs) meant to streamline the accession process.** Comoros is one of eight LDCs currently in the process of accession.<sup>7</sup> The Marrakesh Agreement (establishing the WTO) states in Article XI that “the least-developed countries recognized as such by the United Nations will only be required to undertake commitments and concessions to the extent consistent with their individual development, financial and trade needs or their administrative and institutional capabilities.”<sup>8</sup>

**8. Comoros started the accession process in February 2007 and is working to conclude both multilateral and bilateral negotiations.** The Working Party was established on October 9, 2007, with the first formal meeting occurring in December 2, 2016 and the most recent formal meeting having taken place on October 5, 2023.

Multilateral negotiations are concentrated principally on the domestic legislative reforms that are required to bring Comoros in line with the rules of the WTO, while bilateral negotiations focus on the



rules for access to the Comorian market for both goods and services from foreign producers.

<sup>5</sup> [WTO | Handbook on Accession to the WTO - CBT - The accession process - the procedures and how they have been applied - Introduction - Page 1](#)

<sup>6</sup> Article XII of the Marrakesh agreement speaks to accession: [WTO | legal texts - Marrakesh agreement](#)

<sup>7</sup> The list of LDCs is taken from the UN definition: [Sub-Committee on Least-Developed Countries \(wto.org\)](#)

<sup>8</sup> [wto\\_agree\\_art11\\_oth.pdf](#)

## D. Advantages and Challenges of the WTO Accession

**9. The WTO objective is to help its members use trade as a means to raise living standards, create jobs and improve people’s lives.** This objective is underpinned by several fundamental principles: non-discrimination between trading partners and between domestic and foreign products or services; opening trade; predictability and transparency; fair competition; support for LDCs; protection of the environment; inclusion (with respect to women and small businesses); partnerships with civil society and businesses; and digital trade<sup>9</sup>. The IMF aims to facilitate the expansion and balanced growth of international trade, and to contribute thereby to the promotion and maintenance of high levels of employment and real income and to the development of the productive resources of all members as primary objectives of economic policy. The WTO and the IMF collaborate on many levels including consultation, coordination, training/technical assistance, and on funding assistance related to trade liberalization<sup>10</sup>. Further, the IMF’s role in ensuring a stable international financial system supports international trade, while smoothly flowing trade helps contain the risks of balance of payments and financial crises.

**10. WTO membership can confer numerous benefits on members.** First, membership allows access to foreign markets for a country’s exports under WTO rules. These include elements such as: non-discrimination relative to domestically produced goods and services, which allows fair competition for exports; and “Most Favored Nation” treatment, which means that WTO members face the lowest tariffs on offer (outside of a preferential trade agreement). Second, membership provides a predictable rules-based system of trade which reduces risk for the private sector (both foreign and domestic) and thus can promote investment. Third, members have access to a dispute settlement mechanism where they can bring claims of unfair treatment to be resolved in an orderly manner. Fourth, membership provides support (particularly for LDCs) for improving the legal and institutional framework for trade, bringing countries up to best practice and increasing efficiency. Fifth, it protects countries against unfair competition from other countries’ exports, for example, through limiting government subsidies to exporting firms.

**11. For some countries including Comoros, the direct benefits from accessing other markets may be relatively limited.** As an LDC, Comoros currently benefits from unilateral (i.e., no requirement of reciprocation by Comoros) preferential access to a number of large markets: the European Union through the “Everything But Arms” (EBA) policy; the United States through the African Growth and Opportunities Act (AGOA); China through duty-free treatment for LDCs;<sup>11</sup> Korea through the preferential tariff for LDCs; and numerous others.<sup>12</sup> Comoros is also working towards integrating into the African Continental Free Trade Area, as well as the Common Market for Eastern

<sup>9</sup> [WTO | What is the WTO? - What we stand for](#)

<sup>10</sup> [The IMF and the World Trade Organization](#)

<sup>11</sup> [DUTY-FREE TREATMENT FOR LEAST DEVELOPED COUNTRIES - CHINA \(wto.org\)](#)

<sup>12</sup> There are a total of 24 countries/regions globally offering preferential access to Comorian exports, including the majority of the world’s largest markets.

and Southern Africa (COMESA) both of which greatly increase its potential for exporting tariff free even without WTO membership.

**12. The largest benefits from the WTO accession for Comoros are likely to come from the upgrading of Comorian legal and institutional frameworks for trade.** Such alignment with international standards confers its own set of benefits. Rules-based systems promote transparency and ease of doing business that could in turn encourage foreign and domestic investment and export diversification. Within the multilateral framework, Comoros as a small country would have the same bargaining power and be subject to the same rules as other members, protecting the country from potential impositions of disadvantageous trade practices by large trading partners.

**13. Reductions in, or eliminations of, certain border taxes can pose particular challenges.** Bilateral WTO negotiations will not likely dramatically impact Comorian customs duties, in part due to the fact that integration into the COMESA customs union already requires adopting the fixed common external tariff (CET). However, the elimination of “Other Duties and Charges” (ODCs) at the border is likely to be a requirement for accession. This requirement is based on the principles of simplicity and transparency of trading regulations for importers and exporters, as well as avoiding having nominally low tariffs while charging much higher rates on imports in practice. The Comoros government has in principle committed to eliminate the “Other Duties and Charges” (ODCs) upon the country’s accession to the WTO<sup>13</sup>.

- **ODCs in Comoros amount to around 3.5 percent on most imported goods, and with the possibility of totaling KMF 3.7 billion (USD 8 million) each year in government revenues.**<sup>14</sup> The charges include: a Regional Cooperation Tax (TCR) of 1 percent earmarked for paying contributions to regional and international institutions; a 1 percent tax on all products except ordinary rice and petroleum to support the Chamber of Commerce, Industry and Agriculture (CCIA) and to provide maintenance of warehouses/depots for imports; an import trade tax (patente d’importation, PI) at 1 percent for importers with a tax identification number and 10 percent for those without; and an advance tax payment (AI) of 1 percent that registered taxpayers could deduct from corporate taxes at the end of the year.
  - **Empirical analysis points to a potential loss of roughly 3.86 percent of tax revenue, or KMF 1.7 billion (USD 3.7 million), in the short-term once the potential for increased import volumes is integrated.** Using a standard import demand trade elasticity with respect to tariffs sourced from gravity estimates (see next section), we calculate the increase in import value associated with the elimination of these ODCs. Although the revenue losses are expected to be visible in the short-term once the potential for increased import volumes

<sup>13</sup> Under the now outdated Order N° 21-060/MFBCB/CAB of November 29, 2021, all ODCs would be eliminated by 2025 with the specific provisions of the Order to be transposed into the Finance Laws of 2023, 2024 and 2025.

<sup>14</sup> 3 percent is calculated as the sum of the TCR, CCIA and PI taxes (see later in the paragraph). This assumes importers have a tax identification number and are paying corporate taxes and hence receive the AI reimbursed at the end of the year. The maximum rate for an importer without a tax identification would be 14 percent.

is integrated, they could likely be lower in the long run to reflect structural changes and their associated benefits for the country.

## Next Steps for Comoros

**14. Comoros is considered among the most advanced countries on the path to accession, but some hurdles remain.** The requirements for accession, even for LDCs, can be demanding which explains the extended time between the start of the Comorian accession process and today. Laws must be adapted, and in some cases replaced, and domestic policies which protect or subsidize certain companies/industries need to be adjusted. The drafting of the laws can require significant technical assistance, and certain changes can face internal resistance due to domestic political economy considerations. These efforts take both financial resources, for example to pay for experts, and draw human resources away from other governmental initiatives. At the time of writing, both the multilateral and bilateral negotiations are ongoing and need to be concluded in order to move onto the next stage of the process.

- Regarding the multilateral process, several key trade-related laws remain to be drafted and adopted into Comorian law, in part due to a need for technical assistance expressed by the Comorian authorities (see below for more details). Several policies relating to tax collection and trade in goods also need to be modified. Indeed, the remaining elements include: (i) the adoption of the principle of equivalence agreements and other types of sanitary agreements, as well as the principle of transparency, zoning and compartmentalization; (ii) the adoption of the following laws: Veterinary Sanitary Police Act, draft decree on veterinary sanitary police and draft law on veterinary public health; and (iii) draft regulations on policies affecting trade in goods.
- On the bilateral side, negotiations have been completed with almost all countries, but some issues are yet to be finalized. The tariff schedule is largely concluded, in part due to limited space for negotiation given Comoros in the process of integrating into the COMESA customs union with a pre-defined common external tariff (CET). The terms of access to the Comorian market for foreign services is also featured in ongoing discussions.

**15. The Comorian authorities held a round table to solicit extensive support for technical assistance on January 13, 2022.**<sup>15</sup> Development partners and Comorian government officials came together with aim of discussing the capacity building and technical assistance needs related to the accession process. The needs outlined covered non-tariff barriers, trade facilitation, technical barriers to trade, and the sanitary and phytosanitary (SPS) system. Representatives from the international community indicated their readiness to work with the authorities on the identified needs.

**16. The IMF continues to provide significant capacity development relevant to the accession process.** Organized through the Fiscal Affairs Department (FAD) and the Regional Technical Assistance Center for Southern Africa (AFRITAC South – AFS), the IMF works intensively

<sup>15</sup> [WTO | 2022 News items - Comoros discusses accession, post-accession technical assistance with development partners](#)



with the Comorian customs authority. This support covers customs valuation, risk management, post-clearance audit, legislation for the effective implementation of the customs code, and control of excise regimes, and aims to be in line with the requirements for WTO accession where relevant. The authorities' engagement with the IMF under the Extended Credit Facility (ECF) also provides a framework for strengthening revenue administration and tax policymaking capacities, which would cushion the effect of trade tax reductions as a result of the WTO accession.

## E. Estimation of Import Demand Elasticity

**17. This section estimates the impact on the volume of imports associated with tariff reduction.** The estimate is done for small states, based on a standard gravity model. The estimation strategy relies on the empirical gravity model for trade flows coined by Tinbergen (1962) and theoretically developed by (Anderson, 1979; Anderson and van Wincoop, 2003; Anderson and van Wincoop, 2003; Baier and Bergstrand, 2009). Following this literature, we include the importer and exporter "multilateral resistance terms" (MRTs).

**18. Using an OLS estimator, the effects of bilateral trade tariff on trade flows are estimated from a standard gravity model from 1990 to 2021.** The standard gravity model is given by:

$$\ln Trade_{ijt} = \psi_0 + \psi_i X_{ijt} + \alpha_X Z_{ijt} + d_i + d_j + d_t + \vartheta_{ij,t} \quad (1)$$

where  $Trade_{ijt}$  represents the total imports (or exports) from country  $i$  to country  $j$  in year  $t$ .  $X_{ijt}$  is a set of control variables including standard gravity variables (i.e., bilateral tariff, and distance). The bilateral tariff captures the effects of tariff barriers on trade flows. The distance variable represents the distance between the most populated cities in partner countries. These gravity variables capture the effects of trade barriers on bilateral trade flows. We capture historical and cultural linkages between trading partners by including a dummy variable which take the value of 1 if two partners countries have a common language. We also include the gross domestic product (GDP) to proxy economic development both for importer  $j$  and exporter  $i$ .  $d_i$ ,  $d_j$ , and  $d_t$  are importer  $j$ , exporter  $i$  and time  $t$  dummies, respectively. The paper uses data from two main sources, namely the CEPII<sup>16</sup> gravity database (Conte et al., 2021) and the ESCAP<sup>17</sup><sup>[2]</sup>-World Bank trade cost database.

## Empirical Results

**19. Estimation results are shown in Table 1, with all control variables showing the expected signs.** Economic development proxied by GDP is a significant determinant of bilateral trade. A strong economic activity significantly drives bilateral trade flows. Bilateral trade flows tend to be greater across less distant partners as well as for partners that share the same official language. Bilateral tariff is a significant (negative) determinant of bilateral trade flows. These results

<sup>16</sup> Centre d'Études Prospectives et d'Informations Internationales.

<sup>17</sup> Economic and Social Commission for Asia and the Pacific.

are consistent with the literature on gravity models since bilateral trade flows between countries depend on their wealthiness as well as transportation costs (Kassa and Sawadogo, 2021; Carrere, 2006; Francois and Manchin, 2013). The coefficient of interest is that on bilateral tariff, which provides the estimate for import demand elasticity to changes in tariffs.

## 20. The results for small states are of particular relevance for Comoros.

Based on the above estimates, a 1 percentage reduction of tariffs in small states (ODCs in the case of Comoros) would increase import volume by 1.03 percent. Applying this import demand elasticity to the reduction of ODCs to liberalize trade yields an estimated revenue loss in Comoros of around 1.7 billion KMF (or 0.3 percent of 2023 GDP and 3.86 percent of tax revenue).

### Sensitivity Analysis

## 21. A sensitivity analysis is performed, and the results show that the revenue loss is negatively correlated with the import demand elasticity.

The potential revenue loss is assessed with respect to the levels of elasticities for import demand. Higher import demand elasticities are associated with lower revenue losses. The revenue loss is zero when import demand elasticity is equal to -3.82. Beyond this value, the increase in imports due to the lower tariffs outweighs the loss from tariff reduction and results in higher overall revenue collection.

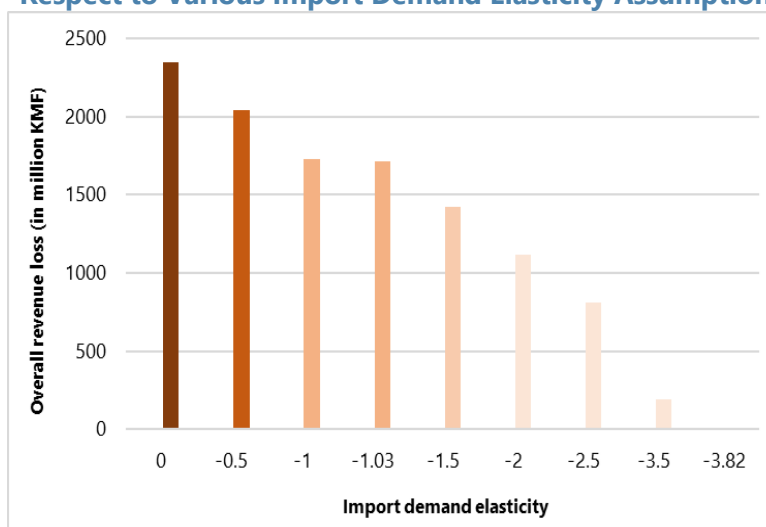
**Table 1. Union of the Comoros: Gravity Model Estimates**

	Ln(exports) small states	Ln(exports) developing	Ln(exports) other developing	Ln(imports) small states	Ln(imports) developing	Ln(imports) other developing
Ln (GDP importer)	0.82*** (0.09)	0.52*** (0.02)	0.50*** (0.02)	0.72*** (0.07)	0.67*** (0.02)	0.65*** (0.02)
Ln (GDP exporter)	0.82*** (0.09)	0.38*** (0.02)	0.35*** (0.02)	0.29*** (0.06)	0.23*** (0.02)	0.22*** (0.02)
Ln (distance)	-1.18*** (0.04)	-0.94*** (0.01)	-0.94*** (0.01)	-1.65*** (0.03)	-1.13*** (0.01)	-1.07*** (0.01)
Common language	0.43*** (0.07)	0.65*** (0.02)	0.60*** (0.02)	0.87*** (0.05)	0.66*** (0.02)	0.64*** (0.02)
Ln (1+bilateral tariff)	-2.82*** (0.05)	-2.61*** (0.01)	-2.54*** (0.01)	-1.03*** (0.03)	-1.78*** (0.01)	-1.76*** (0.01)
Constant	Yes	Yes	Yes	Yes	Yes	Yes
Importer/FE	Yes	Yes	Yes	Yes	Yes	Yes
Exporter/FE	Yes	Yes	Yes	Yes	Yes	Yes
Time/FE	Yes	Yes	Yes	Yes	Yes	Yes
Observations	13084	130315	121099	14552	134290	123901
R <sup>2</sup>	0.661	0.750	0.751	0.711	0.735	0.741

Standard errors in parentheses \*  $p < 0.10$ , \*\*  $p < 0.05$ , \*\*\*  $p < 0.01$

Source: IMF Staff

**Figure 4. Union of the Comoros: Overall Revenue Loss with Respect to Various Import Demand Elasticity Assumptions**



Source: IMF Staff

Note: Following the literature on gravity models, we assume different levels of import demand elasticities to potential assess the revenue loss. The revenue loss is negatively correlated with the import demand elasticity since higher elasticities are associated with lower revenue loss in Comoros. The revenue loss is zero when import demand elasticity is equal to -3.82. Beyond this value, the positive effects of tariffs reduction in terms of higher revenue collection outweighs its negative effects in terms of revenue loss.

## F. Revenue Replacement Following Trade Liberalization

**22. This section assesses the potential for revenue replacement following trade tax reduction in small states.** The empirical evidence on trade tax replacement with domestic tax revenue is mixed since some studies show that there is no evidence on trade tax replacement (Baunsgaard and Keen, 2005) while others argue that there is possible replacement of trade taxes by domestic tax revenue following trade liberalization (Keen and Mansour, 2010). Drawing upon this literature and relying on a sample of 16 small developing states<sup>18</sup> which are members of the WTO over the period 1990-2022, this paper estimates the effects of trade tax revenue on domestic tax revenue. The estimated equation is as follows:

$$DT_{it} = \psi_0 + DT_{it-1} + \psi_1 TT_{it} + \psi_2 X_{it} + \vartheta_{it} \quad (2)$$

where  $DT_{it}$  is domestic tax revenue for country  $i$  at time  $t$ ,  $TT_{it}$  is trade tax revenue, expressed in percent of GDP, and  $X_{it}$  is a vector of control variables. Estimators used are fixed-effects and system-GMM. The coefficient associated with trade tax is expected to be negative, implying that trade tax is replaced by domestic tax revenue. Country and year dummies are also included.

**23. The econometric results for SDS show no robust evidence that trade taxes would be replaced with domestic tax revenue.** The estimated coefficient of the control variables shows the expected signs. GDP per capita growth and control of corruption are expected to positively correlate with tax revenue given that strong economic growth enlarges the tax base and improves tax revenue collection. The share of agriculture to GDP is expected to be negatively associated with revenue because agriculture is harder to tax, particularly in developing countries where the agriculture sector is informal. The inflation rate, FDI inflows, remittances received, and the degree of trade openness can positively or negatively affect tax revenue.

**Table 2. Union of the Comoros: Effects of Trade Tax on Domestic Tax Revenue in Small States**

Non-trade tax	[1]	[2]	[3]	[4]	[5]	[6]
	Fixed Effects			System-GMM		
Lag Non-trade tax	0.657*** (0.0699)	0.658*** (0.0715)	0.650*** (0.0738)	0.947*** (0.0799)	0.951*** (0.0906)	0.948*** (0.0765)
Trade tax	-0.176* (0.0973)	-0.174 (0.134)	-0.175 (0.111)	-0.0304 (0.0603)	-0.0263 (0.0636)	-0.0221 (0.0597)
GDP pc growth	0.0220 (0.0214)	0.0228 (0.0261)	0.0235 (0.0305)	0.0690* (0.0392)	0.0677* (0.0363)	0.0669* (0.0379)
Trade openness	0.00408 (0.0108)	0.00461 (0.0104)	0.00583 (0.0110)	-0.00171 (0.00415)	-0.00171 (0.00568)	-0.000986 (0.00446)
Inflation	-0.0289 (0.0263)	-0.0282 (0.0267)	-0.0360 (0.0275)	0.00850 (0.0335)	0.00644 (0.0337)	0.00966 (0.0330)
Agriculture (GDP)	-0.197* (0.106)	-0.200** (0.0984)	-0.213*** (0.0969)	-0.00694 (0.0375)	-0.00236 (0.0394)	-0.00546 (0.0370)
Control of corruption	0.606 (0.702)	0.599 (0.761)	0.611 (0.741)	0.0558 (0.704)	0.140 (0.738)	0.166 (0.717)
FDI inflows		-0.00611 (0.0313)			0.00295 (0.0291)	
Remittances (GDP)			-0.0461 (0.0357)			0.0142 (0.00919)
Constant	7.535*** (1.953)	7.501*** (1.927)	7.926*** (1.906)	1.421 (2.228)	1.231 (2.514)	1.117 (2.269)
N	242	242	241	242	242	241
R2	0.882	0.882	0.883			
AR1				0.012	0.012	0.012
AR2				0.788	0.797	0.758
Hansen				0.346	0.339	0.391
Number of groups				16	16	16
Number of Z				14	15	15

Standard errors in parentheses \*  $p < 0.10$ , \*\*  $p < 0.05$ , \*\*\*  $p < 0.01$

Source: IMF Staff.

**24. These results point to the possible difficulty for Comoros in mobilizing domestic revenue to offset potential losses in trade tax revenue following trade liberalization.** The experience of other small states highlights the importance of developing a strategy for alternative sources of revenue that would

<sup>18</sup> The list of countries in the sample is shown in the Appendix (Table A2).

need to be implemented alongside accession efforts. The authorities currently have the window to do so, as the transition period following the WTO accession will allow for a gradual reduction of ODCs. Notwithstanding this transition period, it is important that a policy approach to replace the revenue losses from abolition of ODCs is decided upon and legislation enacted to implement any agreed new tax policy approach in advance of WTO accession.

## G. Policy Options and Concluding Remarks

**25. While trade liberalization can offer many benefits, it will be important for Comoros to have a strategy to offset the potential drawbacks associated with lower tax revenue.** Although the empirical evidence for small developing states shows that replacement of lost trade tax revenue following trade liberalization may be a challenge, Comoros' small starting tax base offers a large upside for domestic revenue mobilization. With careful planning, the country may well be able to benefit from trade liberalization while also achieving higher domestic revenue. Three main policy options could be designed to boost tax revenue collection in the country.

**26. First and foremost, strengthening tax revenue administration to improve tax collection and combat tax fraud is crucial.** This could be done by strengthening the human resources in charge of monitoring and by initiating administrative reforms including digitalization, simplification of procedures to improve tax compliance. Enhanced revenue administration capacity is a prerequisite for other tax reforms as it mitigates informality and tax fraud.

**27. Second, policymakers should consider removing tax exemptions and increasing domestic direct taxes to replace trade taxes.** A first step could include: (i) limiting tax exemptions by setting clear criteria to provide tax benefits and removing unjustified tax benefits, and (ii) replacing some exemptions with cost-based incentives - such as accelerated capital cost allowances and investment tax credits (see IMF et al., 2015). Increasing direct taxes could be considered as a medium-term policy option. There are limitations to the resources that can be mobilized with direct taxation given the potential difficulties for developing countries to collect these taxes (it is difficult for example to identify the population/taxpayers and to enforce tax payment in the case of personal income tax). However, this could be achieved with a sound tax policy design (such as the use of final withholding at source and a simple presumptive income tax regime for small unincorporated businesses) coupled with sufficient political will.

**28. Third, mechanisms to replace the lost tax revenue should also include indirect taxes.** Immediate policy options could include introducing and/or increasing excise duties on certain low-tax and non-taxed products (alcohol, tobacco, drugs, luxury products), and widening and developing new tax bases. The policy options over the longer term could include the adoption of the VAT system. Several studies find that indirect taxes offer untapped revenue potential in developing countries. Chambas (2005) shows that VAT is the most appropriate among indirect tax instruments because of its deductibility and its capacity to ensure greater economic neutrality. However, the structure of the VAT is significantly more complex than the structure of the trade tax. The system is susceptible to fraud if not underpinned by very strong administration capacity. A good design is crucial to implement a sound VAT system. Some prerequisites are needed before the VAT can be

effectively implemented. These include, for example, the development of a single tax identifier system to facilitate cooperation between the various tax authorities, a clear identification of the structure in charge of managing the VAT system (VAT collection and VAT refund), upgraded tax codes, and a robust IT system supported by the capacity to employ it.

**29. Finally, any revenue replacement strategy would not yield results without the lynchpin of sound macroeconomic and governance policies.** Macroeconomic stability supported by prudent fiscal and monetary policies ensures strong economic activity that in turn generates taxes. A strong public governance framework would also improve the transparency and effectiveness of tax spending which would further bolster economic activity while increasing citizens' willingness to pay taxes.

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## Appendix I. List of Variables and Countries

<b>Variables</b>	<b>Descriptions</b>	<b>Sources</b>
Ln (exports)	Trade flows as reported by the origin country	The CEPII Gravity Database (Conte et al., 2021)
Ln (imports)	Trade flows as reported by the destination country	
Ln (GDP exporter)	Gross domestic product of the origin country	
Ln (GDP importer)	Gross domestic product of the destination country	
Ln(distance)	Distance between most populated cities	
Common language	Dummy equal to 1 if two countries have the same official or primary language and 0 if not	
Ln (1 + bilateral tariff)	Bilateral tariff between partner countries	ESCAP-WB trade cost database

Source: IMF Staff

<b>Sample of Countries</b>	
Antigua and Barbuda	Maldives
Barbados	Mauritius
Belize	Samoa
Cabo Verde	Seychelles
Dominica	Solomon Islands
Eswatini	Suriname
Fiji	Tonga
Guyana	Vanuatu



# STATE-OWNED ENTERPRISES: OIL AND GAS IN COMOROS<sup>1</sup>

## A. Executive Summary

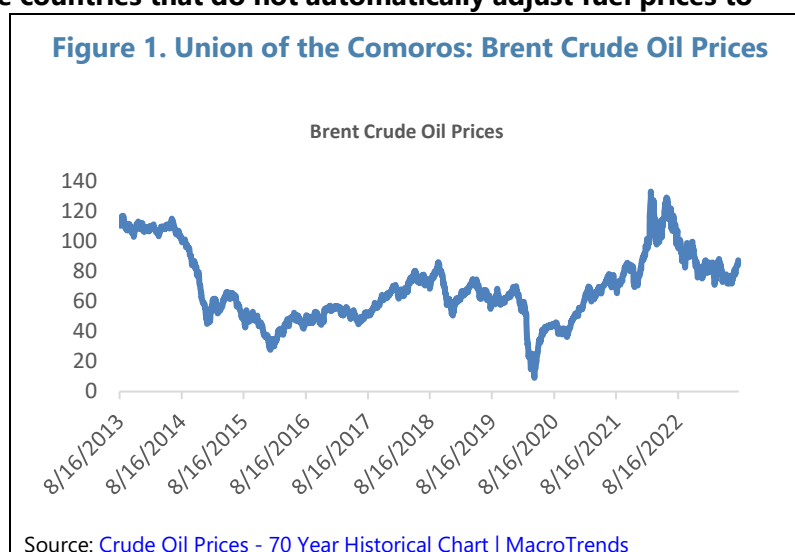
The Comorian state oil and gas company (*Société Comorienne des Hydrocarbures, SCH*) must contend with increasing demand for energy in a context of high oil prices and an increasingly difficult financial situation. In recent years, SCH's share in government revenue has steadily declined. Despite the increase in administered fuel prices in June 2022 at service stations, SCH's losses are estimated at 2.5 percent of GDP in 2022. Moreover, fiscal costs from tax subsidies (including exemption from the domestic oil and gas tax, TIPP) combined with subsidies from the underpricing of oil and gas products totaled up to 3.2 percent of GDP in 2022. The state electricity company (*SONELEC*) received the largest share of the subsidies. Urgent measures to stabilize SCH's financial position, secure government revenue, and ensure good governance practices for this public corporation are needed in the short term. A plan to revise the subsidy policy in the energy sector is needed in the medium term.

## B. Introduction

### 1. Comoros is among the countries that do not automatically adjust fuel prices to international oil prices.

Until 2022, the prices charged by SCH were high enough to generate relatively substantial profits, making it the leading state-owned enterprise (SOE) in terms of contribution to tax revenue (almost 20 percent of the country's total tax revenue in 2021) and payment of dividends (close to one-third of dividends paid by SOEs).

The sharp rise in the price per barrel in 2022, the result of the conflict in the Ukraine, forced the authorities to abruptly raise pump prices in June 2022. But these adjustments could not prevent the substantial losses posted by SCH during 2022. This situation, combined with other governance issues at all SOEs and at SCH in particular call for urgent fiscal consolidation measures, comprehensive reform of subsidies applied in the Comorian energy sector, and a focus on good international practices in SCH governance.



<sup>1</sup> Prepared by Ibrahim Ahamada under the supervision of Rima Turk.

**2. This paper reviews in detail the oil and gas situation in Comoros.** It quantifies the influence of SCH in economic activity in terms of volume of imports (Section C) and contribution to government revenue (Section D). The analysis of the pricing structure at SCH reveals heavy losses (Section E), giving rise to costly subsidies by the government (Section F). In light of the financial difficulties faced by SCH (Section G), short- and medium-term recommendations are proposed for effective reform of subsidies in the energy sector (Section H).

### C. Principal Imports by SCH

**3. SCH holds a monopoly on the import of petroleum products in Comoros.** It distributes diesel fuel to SONELEC; it delivers gasoline, diesel, and kerosene to private service stations; it supplies the general government, including the army, with fuel; and it also handles the delivery of aviation fuels. The bulk of imported diesel fuel is absorbed by SONELEC (54 percent) while 88 percent of all imported kerosene is channeled to domestic use, essentially by poor households, for cooking and lighting. Petroleum storage capacity represents roughly 45 days' consumption, which requires on average six to eight petroleum shipments per year to Comoros. The islands Ngazidja and Anjouan receive shipments directly from oil companies, while Mohéli is supplied by small boats coming from the other islands.

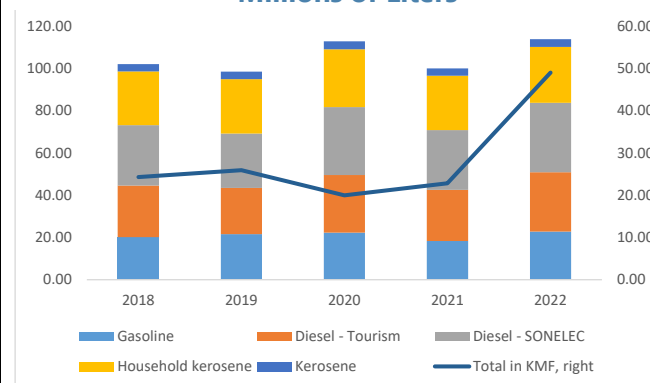
**Table 1. Union of the Comoros: SCH Activities**

1. Distribution of gasoline and diesel fuel for transport
2. Distribution of diesel fuel to SONELEC
3. Supply of household kerosene to service stations
4. Distribution of aviation fuel (Jet A-1)
5. Domestic gas production (recently)

**4. Demand for fuel in Comoros is growing at an ever-faster pace.** The volume of oil and gas imports is estimated to have increased by roughly 24.5 percent between 2018 and 2023 (Figure 2). Imports observed in 2022 and anticipated in 2023 have increased successively since 2021 (+14 percent in 2022 compared to 2021, and +11.5 percent in 2023<sup>2</sup> relative to 2022). This increase is explained in part by the increased number of automobiles on Comorian roads.

**5. SONELEC alone absorbs a significant and increasing share of imported oil and gas.** Of the more than 100 million liters of oil and gas imported annually on average during the last five years, diesel delivered to SONELEC represents 20 percent of the total; household kerosene, 25

**Figure 2. Union of the Comoros: Imports in Millions of Liters**

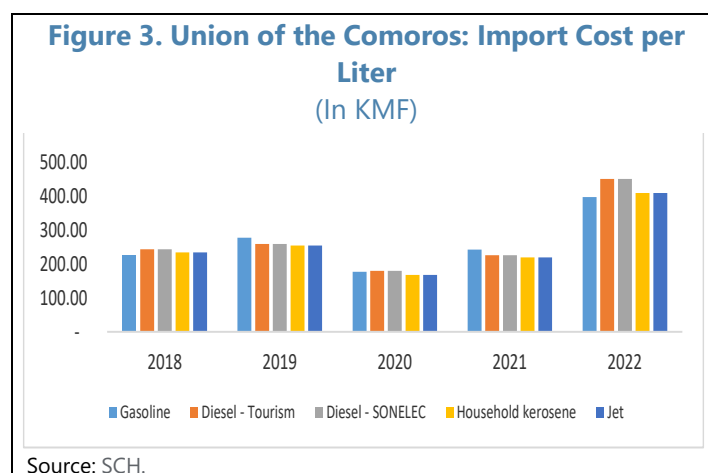


Source: SCH.

<sup>2</sup> Data provided by SCH for 2023 are not stable and indicate that imports increased between 5 percent and 12 percent between 2022 and 2023.

percent; diesel fuel for transport, 24 percent; gasoline, 20 percent; and jet fuel, 3 percent. More recently, SONELEC purchases of diesel fuel jumped significantly, from 28.4 million liters in 2021 to an anticipated 35.6 million liters in 2023, or an increase of more than 25 percent. The impact of the introduction of solar-powered electricity plants is not yet visible, as SONELEC demand for fossil fuels has yet to show signs of slackening.

**6. Amid strong demand for energy, oil prices have soared.** The cost of oil and gas imports nearly doubled between 2018 and 2022 (Figure 3) and the energy bill continues to increase. The average annual cost (roughly KMF 23 billion in recent years) is relatively high in regard to the country's total imports (over KMF 100 billion FOB on average during the same period). In 2022, the cost of energy imports increased abruptly, to 49 billion, representing nearly one-third the value of all imports. The increase was largely due to the war in Ukraine. For a number of years, energy supplies have been financed by drawings from the Islamic Trade Finance Corporation (ITFC). However, with the spike in the Brent price, the ITFC funds no longer suffice to fully cover the financing of imports, and SCH is now obliged to supplement the financing of its purchases with other sources of financing (equity, bank loans).



## D. SCH's Contribution to Government Revenue

**7. SCH is the largest contributor of public revenue of all Comorian SOEs, accounting for nearly 19 percent of domestic revenue in 2020 (Tables 2 and 3).** It contributes to government revenue by transferring:

- *TIPP*. This *Taxe Intérieure des Produits Pétroliers* (TIPP) is the largest component of SCH contributions to government revenue. It is assessed on all products except diesel fuel sold to SONELEC, household kerosene, and jet fuel.<sup>3</sup> The TIPP includes excise and consumption taxes. It represented 87 percent or more of the tax revenue SCH transferred to the Treasury, or close to 18 percent of total tax revenue, in 2020.
- *Corporate profits tax (IS)*. The IS is based on total profits generated by SCH, fixed at a rate of 35 percent. SCH paid up to 78 percent of the total IS paid by all SOEs in 2021.

<sup>3</sup> The TIPP is a single tax initially intended (according to the authorities) to represent all taxes normally assessed on an enterprise. However, it was found that once the TIPP was applied, there was still room to apply traditional taxes; hence the assessment of corporate taxes and wages and salaries tax.

- *Wages and salaries tax (IGR)*. This tax is withheld at the source unless expressly exempted by special provisions. The IGR liability represented up to 17 percent of total IGR at all SOEs in 2021.
- *Dividends*. SCH shares 50 percent of realized profits with the government. The dividends paid by SCH represented up to 47 percent of total dividends paid to the government by all SOEs in 2020.

**Table 2. Union of the Comoros: Revenue from SCH.**

	2020	2021	2022	2023: First half
<b>Total SCH tax revenue in KMF</b>	8,220,485,703	8,798,996,235	7,271,004,562	3,944,024,728
<b>Domestic oil and gas tax (TIPP) in KMF</b>	7,166,370,067	6,024,906,600	6,077,607,730	3,909,440,250
<b>Wages and salaries tax (IGR) in KMF</b>	72,715,636	74,089,635	77,347,249	27,724,119
<b>Corporate tax (IS) in KMF</b>	981,400,000	2,700,000,000	1,116,049,583	6,860,359
<b>SCH nontax revenue for the government (dividend), in KMF</b>	931,000,000	-	611,548,145	
<b>Total SCH tax and nontax revenue in KMF</b>	9,151,485,703	8,798,996,235	7,882,552,707	3,944,024,728
<b>SCH tax revenue as % of total tax revenue</b>	20.34	19.26	16.39	8.00
<b>SCH nontax revenue as % nontax revenue</b>	11.46	-	5.11	
<b>Total SCH revenue as % total domestic revenue</b>	18.85	16.00	13.99	6.56
<i>For reference, in KMF:</i>				
<i>Tax revenue</i>	40,411,000,000	45,695,000,000	44,357,000,000	49,321,000,000
<i>Nontax revenue</i>	8,127,000,000	9,288,000,000	11,970,000,000	10,782,000,000
<i>Total domestic revenue</i>	48,538,000,000	54,983,000,000	56,327,000,000	60,103,000,000

Source: Authorities.

**8. In recent years, however, SCH's share in total government revenue has declined significantly.** This appears to be the result of two factors: (i) the overall increase of domestic public revenue (+16 percent between 2020 and 2022), and (ii) the significant decline of IS, which confirms the financial difficulties SCH has experienced in the last two years (IS paid by SCH in the first half of 2023 is negligible compared to previous years; see Table 3). The 2024 budget law provides for IS in the amount of roughly KMF 2.7 billion, but this represents repayment of a tax liability from previous years.

**Table 3. Union of the Comoros: Non-TIPP Taxes and Dividends Paid by SCH as % of Totals Paid by SOEs**

	2020	2021	2022	2023: First half
Wages and salaries tax	14.0	17.0	15.9	9.3
Corporate tax	27.0	78.0	60.4	2.96
Dividends	47.3	-	32.1	-

Source: Authorities

**9. Moreover, the amount of taxes paid does not necessarily reflect SCH activities.** For example, the TIPP did not vary significantly between 2021 and 2022, although imports increased significantly during that period (+24 percent for gasoline and +16 percent for diesel for transport). Also, the IS paid in 2022 (KMF 1.1 billion) does not reflect the financial difficulties observed in the same year (KMF 14.5 billion in losses), although it is likely that the IS paid in 2022 included prepayments based on the 2021 tax situation.

**10. The amount of TIPP varies substantially according to the institution that records the amount of tax collected (Table 4).** These variations demonstrate the need for the government to secure this tax revenue.

**Table 4. Union of the Comoros: TIPP in KMF Billions according to Different Sources, 2022**

Treasury, TOFE	Customs	SCH
6.01	4.9	8.2

Source: Authorities

## E. Pricing structure and impact on SCH losses

**11. The structure of oil and gas prices in Comoros is unique.** In simplified form, the structure of selling prices is as follows:

- a) CIF price, per liter
- b) TIPP, per liter
- c) SCH operating cost, per liter
- d) **Cost price**, per liter: (a) + (b) + (c)
- e) Price charged by SCH to service stations, or **selling price**, per liter: set by the government
- f) SCH margin, per liter: (e) - (d)
- g) Service stations' margin, per liter: set by the government
- h) Price charged by service stations, per liter: (e) + (g)

**12. SCH generates profits on oil and gas products whose cost price is below the selling price set by the authorities.** The government administers the prices for SCH sales to private service stations and SONELEC and for aviation transport. It also sets the prices charged by service stations and SONELEC to end consumers. The prices imposed by the government may be above or below the cost price, resulting in either a surcharge or subsidy for the end consumers.

**13. The selling price adjustment has been discretionary until now.** In fact, prices remained unchanged from 2016 to June 2022. In light of the abrupt rise of the Brent price in early 2022, the authorities substantially raised the prices of certain products in June 2022 (Table 5).

**Table 5. Union of the Comoros: Price (5) and TIPP per Liter**  
(In KMF)

	Selling price before June 2022	Selling price after June 2022	TIPP
Gasoline	575	725	230 (211)**
Diesel - Tourism	430	630	115 (95)**
Diesel - SONELEC	315	315	-
Household kerosene	245	345	-
Jet	400	700	-

Source : SCH.

\* Reduced TIPP.

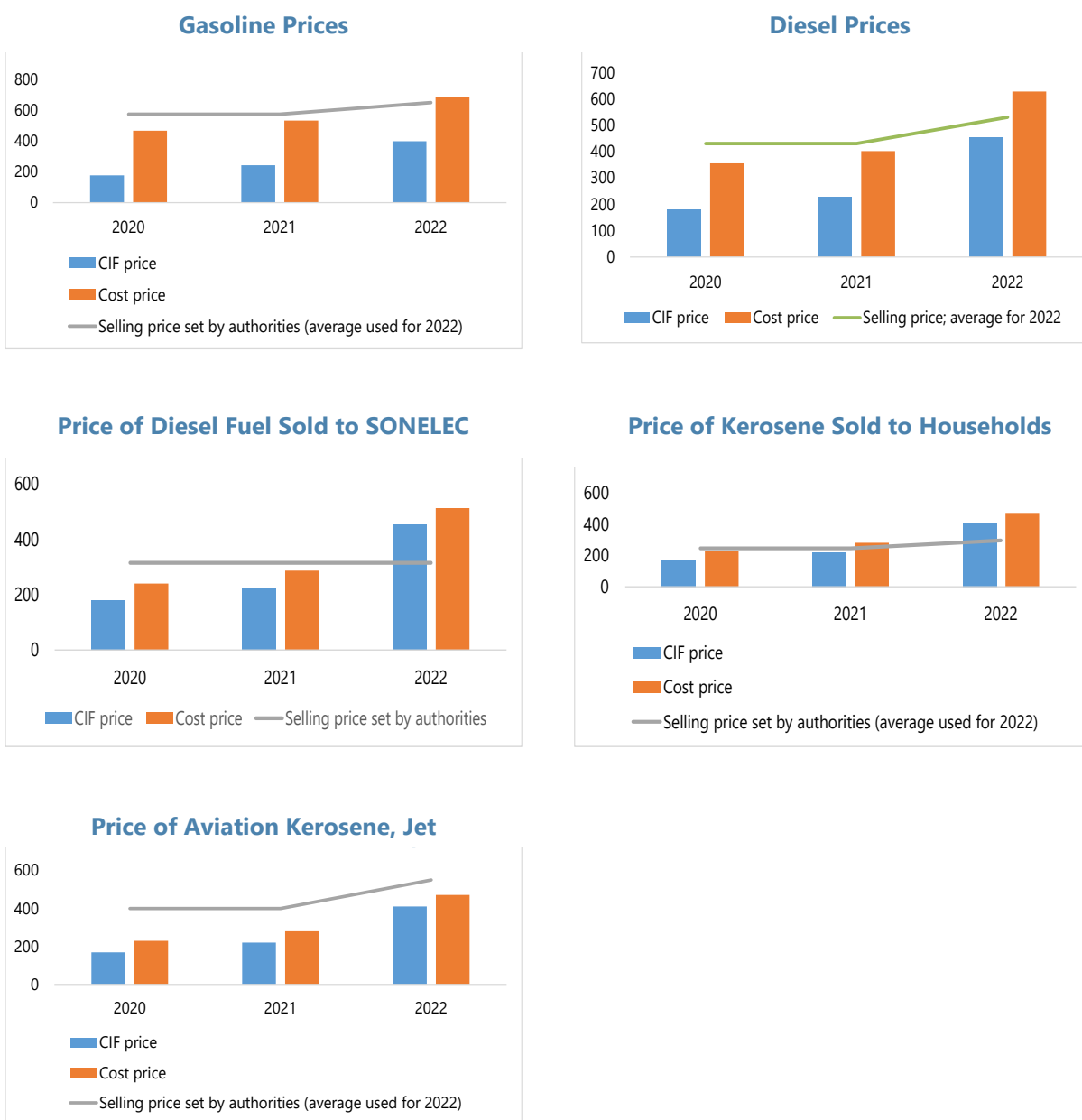
**14. Until 2022, the prices set by the government enabled SCH to cover its costs, but recent price adjustments have been insufficient.** Before the international price increase, SCH was able to cover import costs and even the cost price of most petroleum products. Figure 3 shows that:

- With the exception of household kerosene, all prices (CIF price and cost price) were on average below the selling price until 2021.
- For gasoline and diesel for transport, the upward adjustment of selling prices in 2022 sufficed to cover the CIF price but not necessarily the cost price.
- The June 2022 increases in the selling price of jet fuel easily covered the cost price.
- The June 2022 increase in the price of household kerosene applied by the authorities was insufficient to cover the CIF price of the product. The difference between the selling price and cost price is quite significant.
- The selling price of diesel fuel delivered to SONELEC was not increased in 2022 despite sharp increases in the cost price. The gap between the prices remains quite substantial. And although the price of fuel sold to SONELEC did not rise, the price of electricity was raised in June from 132 KMF/KWH to 198 KMF/KWH.

**15. Selling price adjustments in Comoros do not reflect changes in international prices.**

Table 6 shows that the price increases applied by the authorities in June 2022 would have captured 41 percent of the change in the CIF price of gasoline and 47 percent of the change of CIF price of diesel, jet fuel, and kerosene if the adjustment had been made in early 2022. The adjustments would have had a greater impact on the change in cost prices than the change in CIF prices. This is because there was little or no change in the taxes included in the cost price.

**Figure 4. Union of the Comoros: Comparative Price Trends**  
(In KMF/liter)



Source: SCH

**Table 6. Union of the Comoros: Elasticities: Repercussions of June 2022 Price Changes Calculated for the Period 2021-2022**

	$\Delta(\text{selling price})/\Delta(\text{CIF price})$	$\Delta(\text{selling price})/\Delta(\text{[] cost price})$
<b>Gasoline</b>	41%	90%
<b>Diesel - Tourism</b>	47%	83%
<b>Diesel - SONELEC</b>	0%	0%
<b>Household kerosene</b>	47%	60%
<b>Jet A1</b>	87%	110%

Source: calculated by the authors.

**16. Despite this, oil and gas prices in Comoros are relatively high.** The June 2022 price increases imposed by the authorities put gasoline and diesel prices in Comoros (other than in Mayotte) slightly above those observed in neighboring countries (Figure 5).

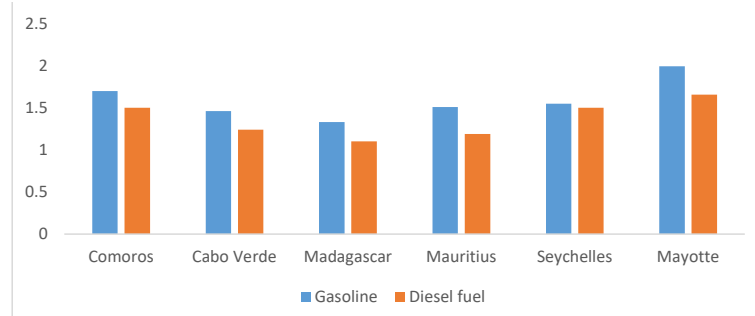
**17. An in-depth analysis shows that SCH posted recent and significant losses on sales**

**of diesel to SONELEC and household kerosene.** Table 7 shows the pricing structure of the five products sold by SCH to allow profits and losses since 2020 to be calculated by product. The following findings emerge:

- In 2020, the cost prices were on average below the selling prices for the five categories of products sold by SCH. This resulted in significant margins of roughly KMF 7.9 billion (1.5 percent of GDP)
- In 2021, only the cost price of household kerosene was above the selling price on average, but the margins generated by other products covered the losses posted on kerosene. In 2021, SCH posted a net margin of roughly KMF 1.8 billion (0.3 percent of GDP).
- In 2022, losses totaled KMF 14.5 billion (2.5 percent of GDP). Note that all margins were negative except for jet fuel (aviation fuel). The losses were particularly steep on diesel sold to SONELEC (KMF 6.5 billion, 445 percent of losses) and kerosene (KMF 4.65 billion, or 32 percent of losses). These two products alone represent 77 percent of recent SCH losses. These figures would be much smaller if they accounted for sales of products taxed at a reduced TIPP rate (for example, gasoline and diesel for tourism). If TIPP were excluded from the cost price, the costs would represent roughly KMF 6 billion, or 1 percent of GDP (Table 8).

**Figure 5. Union of the Comoros: Fuel Prices in August 2023**  
(In \$/liter)

Source : GlobalPetrolPrices.com





**Table 7. Union of the Comoros: Evaluation of Losses**

	2020					2021					2022				
	Gasoline	Diesel fuel	SONELEC	JET	Household kerosene	Gasoline	Diesel fuel	SONELEC	JET	Household	Gasoline	Diesel fuel	SONELEC	JET	Household
Average CIF price in KMF/liter	177.7	180.5	180.5	169.1	169.1	243.2	227.0	227.0	220.1	220.1	398.62	452.61	452.61	410.61	410.61
Import tax	230.0	115.0				230.0	115.0				230.00	115.00			
SCH operating cost (35+25=60)*	60.0	60.0	60.0	60.0	60.0	60.0	60.0	60.0	60.0	60.0	60.00	60.00	60.00	60.00	60.00
COST PRICE	467.7	355.5	240.5	229.1	229.1	533.2	402.0	287.0	280.1	280.1	688.62	627.61	512.61	470.61	470.61
SELLING PRICE before June 2022	575.0	430.0	315.0	400.0	245.0	575.0	430.0	315.0	400.0	245.0	575.00	430.00	315.00	400.00	245.00
SELLING PRICE after June 2022											725.00	630.00	315.00	700.00	345.00
UNIT MARGINS	107.3	74.5	74.5	170.9	15.9	41.8	28.0	28.0	120.0	-35.1					
Quantities imported (millions of liters)	22.2	27.4	32.1	3.7	27.4	18.3	24.2	28.4	3.5	25.7	22.76	28.11	33.00	3.61	26.49
Total sales (KMF billions)	12.8	11.8	10.1	1.5	6.7	10.5	10.4	8.9	1.4	6.3	14.80	14.90	10.39	1.99	7.81
Margins (KMF billions)	2.4	2.0	2.4	0.6	0.4	0.8	0.7	0.8	0.4	-0.9	-0.88	-2.74	-6.52	0.29	-4.65
Margin analysis % of GDP															

\*Operating costs are provided by SCH. They include the cost of transporting products to service stations and reimbursement for evaporation.

Source: SCH and Authors.

**Table 8. Union of the Comoros: Evaluation of Non-TIPP Losses in Cost Prices**

	2022				
	Gasoline	Diesel fuel	SONELEC	JET	Household kerosene
Average CIF price in KMF/liter	398.62	452.61	452.61	410.61	410.61
Import tax					
SCH operating cost (35+25=60)	60.00	60.00	60.00	60.00	60.00
Cost price	458.62	512.61	512.61	470.61	470.61
Selling price before June 2022	575.00	430.00	315.00	400.00	245.00
Selling price after June 2022	725.00	630.00		700.00	345.00
Unit margins					
Quantities imported (millions of liters)	22.76	28.11	33.00	3.61	26.49
Total sales (KMF billions)	14.80	14.90	10.39	1.99	7.81
Net margin (KMF billions)	4.36	0.49	-6.52	0.29	-4.65
as % of GDP					

Source: SCH and Authors.

## F. Fuel subsidies

### 18. Losses posted by SCH result in subsidies due to underpricing of petroleum products.

SCH does not receive a government subsidy in connection with its investments or its operating costs. However, as indicated above, SCH can find itself selling some of its products at a loss. In such cases, those losses can be considered fuel price subsidies for SCH's customers, or subsidies for underpricing. The subsidies could have impacts on SCH's financial position and/or tax revenue. For a closer analysis, we will consider subsidies before and after taxes (IMF, April 2013):

$$\text{Total fuel subsidy} = \sum_k \Delta P(k)V(k) \quad (1)$$

$\Delta P(k)$  represents the difference between the selling price of petroleum product  $k$  ( $k$  = gasoline, diesel for transport, diesel for SONELEC, household kerosene, and jet fuel) and the respective cost price. The volume consumed is  $V(k)$ . The calculated subsidy will be considered the "after-tax subsidy" if the cost price includes TIPP. The calculated subsidy will be considered the "pre-tax subsidy" if the cost price does not include TIPP. This calculation methodology takes account of offsets in terms of costs between subsidized and non-subsidized products. The fuel price is

subsidized if expression (1) is negative (there is a surcharge to consumers if the expression is positive)

**19. Collectively, subsidies linked to underpricing of petroleum products represented 2.5 percent of GDP in 2022, or roughly KMF 14.5 billion** (Table 9). Roughly 45 percent of the subsidy (KMF 6.52 billion) profited SONELEC directly, and 32 percent concerned underpricing of household kerosene (KMF 4.65 billion), see Table 6.

**Table 9. Union of the Comoros: Fuel Price Subsidy as % of GDP**  
(Negative amounts)

	2020	2021	2022
<b>Margin before TIPP</b>	3.1	1.6	-1.05
<b>Margin after TIPP</b>	1.5	0.3	-2.51

Source: Authors.

**Table 10. Union of the Comoros: Cost of Subsidy Represented by Foregone TIPP on Diesel Sold to SONELEC**  
(TIPP at 115/liter)

	2020	2021	2022
Total TIPP subsidy, KMF	3,696,403,761	3,265,330,960	3,794,515,054
as % of TIPP collected	51.6	54.2	62.4
As % of tax revenue	9.1	7.1	8.6
For information, if the subsidy were parti	3,053,550,933	2,697,447,315	3,134,599,393

Source: SCH.

**20. In addition to underpricing, the de facto exemption from TIPP results in tax subsidies representing close to 1 percent of GDP.** The government also contributes to the price subsidy by foregoing TIPP on diesel fuel sold to SONELEC and on household kerosene. Theoretically, there will also be subsidies associated with the application of the reduced TIPP, but according to the authorities, the reduced TIPP is not applied in practice. By foregoing TIPP on diesel fuel sold to SONELEC, the government loses from 51 percent to over 60 percent of TIPP collected each year (Table 10), representing on average slightly more than 8 percent of annual tax revenue. In 2022, tax subsidies on fuel delivered to SONELEC totaled close to KMF 3.8 billion, or 8.6 percent of tax revenue (0.8 percent of GDP).

**Table 11. Union of the Comoros: Ratio between Energy Expenditures by the Wealthiest Households and Poorest Households in Sub-Saharan Africa**

	Diesel expenditure	Expenditure, gasoline	Expenditure, kerosene	Electricity expenditure
Ratio (Q5/Q1)	20	27.4	1.8	17

Source: IMF, April 2013.

**21. It appears that the fuel subsidies mainly benefit the most well-off households rather than the most vulnerable.** There are no statistics on the distribution of oil and gas consumption in Comoros according to income level. Studies have shown, however, that in sub-Saharan Africa (SSA) (Table 11), the richest households may spend 27 time more on gasoline than poorer households (ratio of the fifth to first income quintile, Q5/Q1). Also, roughly 45 percent of fuel subsidies benefit

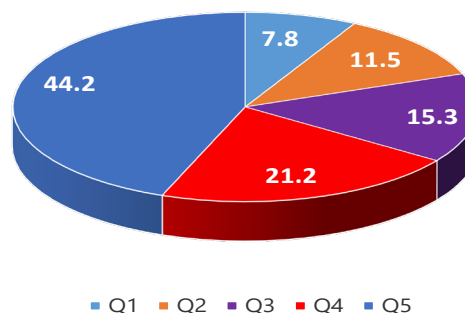
households in 20 percent of the highest income brackets, while households in the 40 percent of lower income brackets (first and second quintiles) received only about 20 percent of subsidies (Figure 6). As a result, it is the wealthiest households that profit the most from universal fuel subsidies. With respect to kerosene, it also seems to benefit lucrative activities (not only vulnerable households) such as fishing boats to which none of the taxes apply.

## G. SCH financial position

### 22. SCH's financial position is vulnerable.

According to figures provided by the authorities, SCH receivables covered only roughly 40 percent of its liabilities at the end of 2022. Liabilities represented roughly 56 percent of SCH total sales at end-2022 (Table 12). Most (46 percent) of the liabilities are owed to financial institutions (ITFC and Exim Bank), one-third are tax liabilities, and 21 percent represent prior dividends not paid to the government.<sup>4</sup> The accumulation of tax arrears and debt representing unpaid dividends also helped to finance fuel deliveries.

**Figure 6. Union of the Comoros: Distribution of Benefits of Fuel Subsidies in Sub-Saharan Africa**  
(In percent)



Source: FMI, 2013.

**Table 12. Union of the Comoros: SCH Debt Indicators on December 31, 2022.**

	As % of total debt	As % of total sales
Liabilities to financial institutions	46	26
Tax liability	33	18
Dividend liability	21	12

Source: SCH.

### 23. SCH's financial position is further weakened by its interconnection with SONELEC.

Most of SCH receivables (over 85 percent) are held with SONELEC. In view of SONELEC's persistent quasi-fiscal deficits (see box below), SONELEC continues to contribute negatively to SCH performance.

#### Box 1. National Electric Company (SONELEC) Quasi-Fiscal Deficit

SONELEC, which is wholly owned by the government, handles the production, distribution, and commercialization of electric energy in Comoros. The production is almost entirely thermal. SONELEC currently produces approximately 125,000 MWH per year. Since end-2020, SONELEC has supplemented its energy production with two independent producers of solar energy, each contributing 3 million GWH on Grande Comore. Another project is under way to instruct a 6 million GWH solar plant, so that a total of 12 million GWH is expected by 2024 on Grande

<sup>4</sup> For a long time, SCH has financed its deliveries with the ITFC. But with the rise of the Brent price in 2022, drawings from the ITFC were supplemented with financing from other financial institutions (Exim Bank)

### Box 1. National Electric Company (SONELEC) Quasi-Fiscal Deficit (continued)

Comore. Two solar plants, each contributing a total of 6 million GWH, are also under way in Anjouan. And demand in Mohéli is fully covered by the 1 million GWH already distributed.

SONELEC is theoretically subject to consumption tax and corporate tax. Despite considerable financial support from the government in the form of various subsidies, SONELEC operates with regular substantial deficits. For example, the financial statements indicate negative annual earnings of -KMF 2.2 billion in 2021 (17 percent of total sales) and -KMF 3.3 billion in 2022 (22 percent of total sales).

Electricity rates in effect, which are well below the elevated production costs, substantial outstanding invoices, significant production losses, and numerous instances of embezzlement, such as frequent thefts of diesel fuel (see August 24, 2020 Gazette des Comoros; June 20, 2023 Al Watan), contribute significantly to SONELEC's continual deficit.

In view of its regular deficits, SONELEC is obliged to prioritize spending, in particular the irreducible and substantial cost of maintaining its generators. In 2023, it will conduct a general review of 11 generators at a cost of more than KMF 100 million per generator, to be borne by the government.

Prices are not automatically adjusted but are negotiated between SONELEC and the government. The most recent electricity rate increase occurred on June 6, 2022. Rates increased from 132 KMF/KWH to 198 KMF/KWH, which is still insufficient to cover SONELEC's elevated production costs, roughly 350 KMF/KWH, even though the price of fuel sold to SONELEC did not increase.

Direct subsidies provided by the government include:

- Investments (purchase, maintenance of generators)
- Operating subsidy (ex-free diesel fuel, cash payment by the government of part of the diesel fuel needed to operate generators)
- Tax-free fuel (TIPP)
- Consumption tax: reduced rate of 3 percent as opposed to 10 percent
- Exemption from customs taxes and duties
- The price of fuel sold to SONELEC may be below the CIF cost
- Minimal corporate tax: Rarely paid (although payable)

Quasi-fiscal deficit (QFD). Analyses of subsidies in the electricity center often refer to a unified indicator to capture explicit subsidies (formal subsidy relating to underpricing) and implicit costs (outstanding invoices, losses in the electricity distribution network, etc.). This indicator provides an idea of electricity production companies' deficit covered almost entirely by the government. The QFD is calculated as follows:  $QFD = K(P^* - P) + KP(1 - r) + KP(L - L^*)$ , where

K is the total quantity of electricity invoiced to all categories of consumers,

P\* is the average cost of production of one GWH of electricity, including capital asset depreciation,

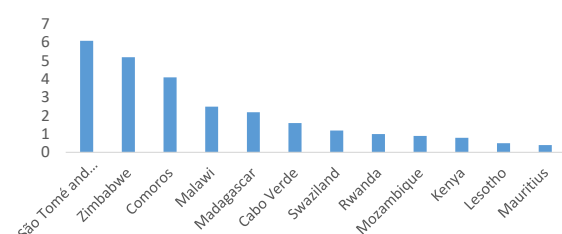
P is the average effective rate per KWH charged by the electricity company,

r is the invoice collection rate

L represents the distribution loss as a percentage of total electricity consumption, and

L\* is the normal rate of distribution losses (10 percent in SSA, according to specialists)

Thus  $K(P - P^*)$  represents losses due to tariff subsidies,  $KP(1 - r)$  are losses due to non-collection, and  $KP(L - L^*)$  represents losses due to network inefficiency. Figure 1 shows that Comoros were already among the countries with a large QFD (4.1 percent of GDP), and Table 1 shows that the situation deteriorated further in 2021 (4.6 percent of GDP) and 2022 (5.2 percent of GDP).

**Box 1. National Electric Company (SONELEC) Quasi-Fiscal Deficit (concluded)****Box Figure 1. Quasi-Fiscal Deficit as Percent of GDP.**

Source: World Bank, 2016.

**Box Table 1. SONELEC Quasi-fiscal Deficit, 2021 and 2022.**

	2021	2022
K, in KWH	97,092,501	126,275,346
P*, in KMF	350	350
P, in KMF	132	198
r	0.77	0.77
L	0.3	0.3
L*	0.1	0.1
QFD in KMF	26,677,136	29,944,935,622
QFD as % of GDP	5	5.2

Source: IMF staff calculations.

**H. Recommendations****In the Short Term****24. The recommendations for short-term reforms aim to help reduce SCH cash flow pressures:**

- *Develop a credible plan to clear the SONELEC debt to SCH.* This will significantly ease SCH cash flow pressures, given that the SONELEC debt accounts for the largest share of SCH receivables.
- *Negotiate a credible plan to clear SCH's tax and dividend liabilities to the government.* These debts represented 56 percent of SCH debt at end-2022.
- *Raise the price of diesel fuel sold by SCH to SONELEC.* This product receives a double subsidy: (i) tax-free prices, and (ii) prices below the CIF prices.
- *Put an end to fuel advances.* SCH sometimes advances fuel to gas stations, to be paid after the products are sold, often creating cash flow pressures. Consumers are often injured by these conflicts because they must wait for the conflict to be resolved before they are able to buy fuel.
- *Put an end to improper practices based on the use of deductions.* SCH directly deducts the amount of corporate tax and dividends from earnings by posting them to a third-party account. SCH also pays the army a portion of the TIPP collected for maintenance payments (instead of remitting it to the Treasury account at the central bank), in addition to providing the army with fuel as payment in kind. The correct practice would be to require SCH to pay the full amount owed for taxes and dividends to the Treasury before the government allocates those amounts to other expenditure items.

**25. The short-term reforms should also improve management and collections of tax revenue generated by SCH.** The revenue expected from SCH and provided in the budget should reflect its profitability as determined under tax law. Revenue should no longer be dictated by

government cash flow pressures but by the company's financial statements. Payments of corporate taxes (KMF 1.16 billion) and dividends (KMF 0.611 billion) in 2022 do not reflect the significant losses posted by SCH (roughly KMF 14.5 billion). To require SCH to pay more than it should undermines its financial health and thus its capacity to pay more taxes in the future. However, the collection of tax revenues should be secured, their accounting improved and the traceability of TIPP payments to the Treasury strengthened (see paragraph 10 which shows significant discrepancies between customs, TOFE and SCH figures).

**26. To improve SCH governance in the short term, it should also:**

- *Ensure that the board of directors meets on a regular basis.* The boards of directors of public companies, including at SCH, were dissolved in 2016. Although SCH's governance had been centralized at the Ministry of Finance, its management is currently handled by one managing director and his staff. SCH should hold regular meetings of a board of directors that includes independent directors, and should produce audited financial statements in accordance with international (OHADA) standards.
- *Modernize the law governing public corporations.* A proposed law was approved during an interministerial meeting of the ministers in charge of public corporations, and is expected to be presented to the legislature for approval.
- *Begin publishing the SCH financial statements, including the government subsidies.* This will promote transparency and help improve the company's performance.

**In the Medium Term**

**27. The recommendations for medium-term reforms aim to establish a plan for reform of subsidies.** Countries that have conducted effective reforms to control the volume of subsidies in the energy sector have taken the following steps (IMF, April 2013):

- *An in-depth analysis of subsidies should precede price reforms.* A rigorous distributional incidence analysis will facilitate the evaluation of costs, the procedures for distribution, and the impacts of eliminating subsidies. Such a study would identify the principal beneficiaries of the subsidy for household kerosene. In 2005, Ghana relied on the conclusions of an analysis of impacts on poverty and social arrangements to convince stakeholders to accept reforms, enabling the authorities to further increase fuels prices that had previously been raised in 2003. Such an approach would allow the subsidies to be focused on the poorest and avoid the high costs associated with universal subsidies. In Comoros, the involvement of the National Institute for Statistics and Economic and Demographic Studies (INSEED) in such an analysis should be beneficial, and the results should be communicated to the public to promote a general understanding of the reforms' legitimacy. In Niger, the introduction of fiscal costs relating to subsidies in the budget law made the population aware of the magnitude of the subsidies.

- *Consultation of the stakeholders (SONELEC, road transport union, consumer associations, etc.) could help create a consensus in favor of the subsidy reforms.* In Namibia, the national energy board created a national task force in 1996 to consider the regulation of fuel prices.
- *The stakeholders should agree on a credible timetable for the phases of the reform.*
  - i. A gradual approach should be adopted in implementing reforms, particularly since the various subsidies provided for SONELEC and the sale of kerosene have been in place number of years. Such an approach will allow SONELEC to adapt gradually and give it time to formulate measures to compensate the most vulnerable households. For example, Namibia spread the reduction of fuel subsidies over several years after adopting an official strategy by consensus on the deregulation of fuel prices. In Kenya, electricity subsidies were eliminated over a period of seven to eight years after numerous rounds of negotiations with stakeholders.
  - ii. The reforms could take place during periods of stability in the international economy, allowing consumers and public authorities to adapt in an environment relatively free of shocks. The June 2022 fuel price increase in Comoros was particularly difficult for the population because it occurred in a context of high inflation, particularly for staple foods.
- *The reforms should be preceded by a public outreach campaign.*
  - i. Consumers are likely to demand information to justify the price increase, particularly given the general perception of SCH as a prosperous company able to withstand shocks. However, the public is unaware of the magnitude of SCH losses on sales of diesel fuel to SONELEC and the taxes forgone by the government. A number of countries have conducted large-scale outreach campaigns prior to launching energy subsidy reforms (Nigeria 2011-2012; Ghana 2005; Niger 2010).
  - ii. Consumers also expect credible, tangible mitigation measures. Since fuel price hikes affect tariffs for transport used extensively by the poor population (students, persons from villages working in the capital, etc.), they will expect to be compensated for the price increase. The authorities should respond credibly, since they previously justified the use of fuel taxes to finance the maintenance of roads that remain in very poor condition today.
- *SCH should improve the quality of its services.* Queues frequently form in front of service stations regardless of international economic conditions, and the public cannot understand the lack of investment in storage tanks. A number of protests over the quality of fuels also took place in June and July 2022. These problems must be overcome before a consensus can be achieved on the reform of fuel subsidies.
- *Finally, measures should be developed to promote the longevity of the reforms:*
  - i. Monitor and disseminate information on the use of the savings resulting from reduced subsidies.

- ii. Depoliticize the price setting process by creating an independent office to administer energy prices.
- iii. Establish a transparent and systematic price adjustment mechanism.

**28. Medium-term recommendations should also take into account the need to reform SONELEC.** In particular, the diesel supply system/mechanism of SONELEC should be reformed, so that the burden does not fall solely on the SCH.



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# PROMOTING FISCAL GOVERNANCE IN COMOROS BY ENHANCING TRANSPARENCY AND CITIZEN PARTICIPATION<sup>1</sup>

## A. Executive Summary

*This paper examines the issue of improving fiscal governance in Comoros through transparency and citizen participation. It identifies gaps in the Public Financial Management (PFM) system and proposes short-term actions, including additional information in budget proposals and publishing essential documents. Medium and long-term measures involve incorporating tax expenditure quantification, medium-term fiscal forecasts, and promoting public engagement. Collaboration among key stakeholders is crucial. By implementing these recommendations, Comoros can achieve enhanced fiscal transparency, increased accountability, and citizen participation in PFM.*

## B. Context

**1. Fiscal governance plays a pivotal role in promoting economic stability and ensuring good governance in a country.** Effective fiscal management is crucial for sound budget execution, controlling public debt, and optimizing resource allocation. By implementing sound fiscal policies and transparent budgetary practices, governments can instill confidence among investors, businesses, and citizens alike. Some empirical studies, such as Caldas Montes et al. (2019) demonstrate the critical role of fiscal transparency in reducing public debt and improving government effectiveness and spending efficiency. Prior to that, other empirical studies highlight the importance of fiscal transparency in fostering effective policy formulation and budgetary risk management, ensuring governments provide more accurate information to the public (IMF, 2012). Enhanced transparency in managing public accounts significantly optimizes fiscal performance and sustainability while mitigating corruption, market volatility, and strengthening economic forecasts (Kopits and Craig, 1998; Islam, 2006; Alt and Lassen, 2006a, b; Glennerster and Shin, 2008; Kolstad and Wiig, 2009; Peat et al. 2015; Arbatli and Escolano, 2015). Furthermore, improved fiscal transparency would narrow credit spreads in 23 emerging economies, especially benefiting countries with smaller and less liquid debt markets (Glennerster and Shin, 2008).

**2. There is a positive correlation between fiscal transparency and government effectiveness<sup>2</sup> and control of corruption in a country.** The first chart shows the average of fiscal transparency and overall government effectiveness. The results reveal that countries with high levels

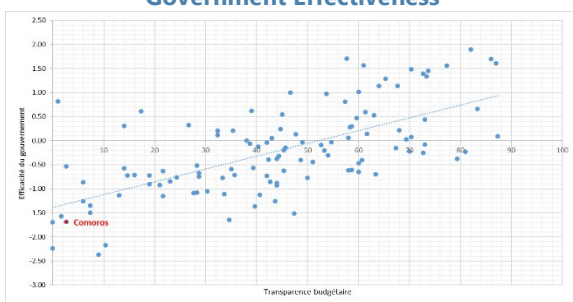
<sup>1</sup> Prepared by Guy Dabi Gab-leyba (AFR).

<sup>2</sup> The Government Effectiveness indicator, part of the World Governance Indicator (WGI), evaluates the quality of public services, the civil service's capacity, its independence from political influence, and policy formulation quality. To compute this, data from various sources are first aligned with six aggregate indicators, then standardized to a 0 to 1 range. A weighted average for each country is derived using an Unobserved Components Model (UCM), considering source correlations. The final governance estimate used in this document ranges from -2.5 (weak) to 2.5 (strong) governance performance.

of transparency in their fiscal practices also demonstrate strong government performance. The second chart highlights the noteworthy correlation between improvements in fiscal transparency and the degree of corruption control. Countries that have adopted measures to strengthen their fiscal transparency have concurrently witnessed a reduction in corruption levels. This highlights the fundamental role of transparency in mitigating corrupt practices and fostering effective governance. The third chart compares the transparency indicator of the CPIA from the World Bank for the year 2021<sup>3</sup>. It reveals that Comoros ranks among the lowest countries in Africa in terms of transparency, accountability, and public sector corruption, with a score of 1.5 while the African average stands at 3.5. The last chart illustrates a decline in Comoros' score for transparency, accountability, and public sector corruption, dropping from 2 in 2004 to 1.5 in 2021. This trend indicates a decrease in transparency in Comoros, aligning with conclusions drawn from the IBP notation and the World Governance Indicator. These dynamics emphasize the importance for policymakers and authorities to prioritize fiscal transparency, leading to more accountable and efficient governance.

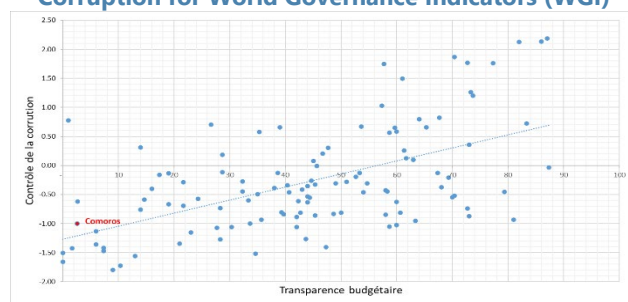
**Figure 1. Union of the Comoros: Relation Between Fiscal Transparency and Relevant Other Variables**

**Relation between Fiscal Transparency and for Government Effectiveness**



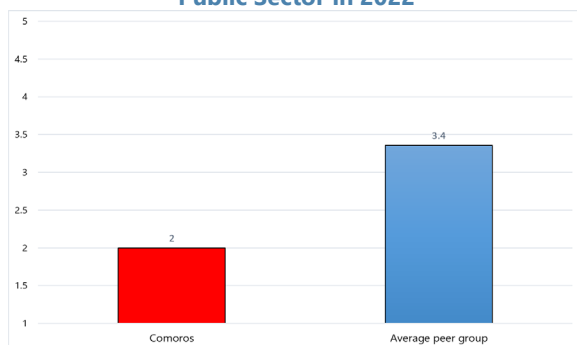
Source: IBP database for fiscal transparency and World Governance Indicators (WGI) for Government Effectiveness

**Relation Between Fiscal Transparency and Control of Corruption for World Governance Indicators (WGI)**



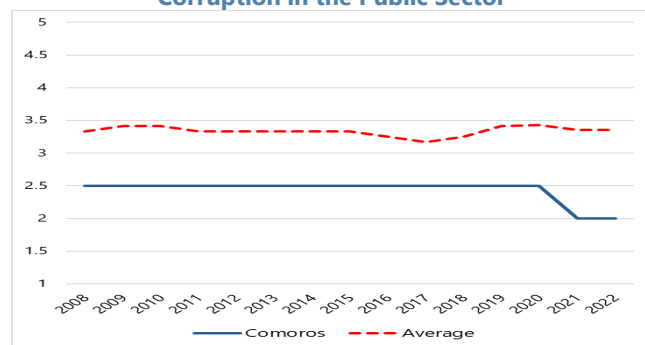
Source: IBP database for fiscal transparency and World Governance Indicators (WGI) for Control of Corruption

**Transparency, Accountability, and Corruption in the Public Sector in 2022**



Source: CPIA Database of World Bank

**Evolution of Transparency, Accountability, and Corruption in the Public Sector**



Source: CPIA Database of World Bank

<sup>3</sup> The CPIA rating, which ranges from 1 (low) to 6 (high), measures the accountability of the executive branch, particularly in financial matters. It evaluates the executive's responsiveness to various governing bodies and the transparency of public affairs. Additionally, it examines the potential influence of vested interests on state operations. Sourced from the World Bank Group's CPIA database, this rating focuses on the quality of a country's policies and institutional setups, emphasizing internal factors over external influences. The CPIA aims to determine how well a country's framework supports sustainable growth, poverty reduction, and effective use of development aid.

## C. Challenges in Fiscal Transparency and Citizen Participation

**3. In Comoros, the Public Financial Management (PFM) system would benefit from extensive reforms.** The country's PFM is organized by the amended version of the Law on the Financial Operations of State (LOFE) released in 2012 under the supervision of the Ministry of Finance. Over the past decade, two significant assessments of Public Financial Management (PFM) have been conducted: a self-evaluation of the Public Expenditure and Financial Accountability (PEFA) in 2016 and a more recent Public Expenditure Review (PER) by the World Bank in 2022. The World Bank assessment reveals that the country's PFM system is inadequate for effectively implementing government policies, and unfortunately, no overall improvement has been observed between 2016 and 2022. The identified challenges in the PFM system encompass issues such as low budget transparency and credibility, insufficient control over budget execution and risk management, and the lack of public dissemination of budget execution monitoring reports. Additionally, the draft Settlement Law that allows the National Assembly to oversee the outcomes of the previous year's execution before deliberating on the upcoming finance law credits and objectives is transmitted late and in a fragmented manner to the Supreme Court's Accounts Section. These findings underscore the substantial room for improvements to enhance the effectiveness and transparency of the country's fiscal process.

**Table 1. Union of the Comoros: Evolution of IBP Index in Comoros**

Index (of 100)	2017	2019	2021
Fiscal transparency	8	0	0
Public participation	0	0	0
Budget oversight	33	35	33

Source: IBP Index 2017,2019 and 2021

**4. The 2021 classification of the International Budget partnership (IBP) ranks Comoros among the worst-performing countries in the world in terms of fiscal transparency<sup>4</sup> and public participation (Table 1).** The country's fiscal transparency index achieved the highest score of only 8 out of 100 in 2017 but has since fallen to zero despite some reforms implemented by the Ministry of Finance. To improve on this front, the Ministry of Finance's General Directorate of Budget

<sup>4</sup> According to the 2018 IMF Fiscal Transparency Handbook, fiscal transparency relates to the information accessible to the public about the government's policymaking process. This encompasses the clarity, reliability, frequency, timeliness, and relevance of public fiscal reporting, along with the openness of this information. The Budget transparency score, also known as the Open Budget Index, is IBP's measurement of fiscal transparency. It relies on a rigorous and objective methodology that undergoes independent peer review. The survey includes 228 questions, out of which 109 questions evaluate the public accessibility of the eight essential budget documents. These documents collectively offer a comprehensive view of the generation, allocation, and expenditure of public resources in the budget year. The score ranges from 0 to 100. For documents to be deemed "publicly available," they must be published online within an appropriate timeframe, containing comprehensive and practical information consistent with best practices.

(GDB) would need to publish and respect a timely calendar of publication of documents related to the fiscal process. While some of these documents are already produced, they are not available online or produced within the specified timeframe considered by international standard in terms of transparency. Table 2 provides a summary of the documents that are normally produced during the budget process, and the challenges underlying the lack of fiscal transparency in Comoros. The release of the Citizen Budget in 2023, which is a simplified version of a government's finance law, is expected to improve the classification of the country in terms of fiscal transparency and public participation<sup>5</sup>.

**Table 2. Union of the Comoros: Publication of Documents Related to the Fiscal Process in Comoros**

Document	Availability online	Challenge related to their production
<b>Pre-Budget Statement</b>	Not available	Not produced
<b>Executive's budget proposal</b>	Not available	Produced for Internal Use Only
<b>Enacted budget</b>	Not available	Published Late <sup>1</sup>
<b>Citizen budget</b>	Not available	Published Late <sup>2</sup>
<b>In-year report</b>	Not available	Produced for Internal Use Only
<b>Mid-year review</b>	Not available	Not produced
<b>End-year report</b>	Not available	Produced for Internal Use Only
<b>Audit report</b>	Not available	Produced for Internal Use Only

Source: Based on discussions with authorities and 2021 IBP report

1/ [DÉCRET N°23-002 /PR PORTANT PROMULGATION DE LA LOI N°22-012/AU DU 27 DÉCEMBRE PORTANT LOI DE FINANCES 2023](#)

2/ [BUDGET CITOYEN 2023](#)

**5. Comoros lags behind most of its peer counterparts in terms of fiscal transparency (Figure 2).** The data underscores the urgent need for Comoros to make substantial improvements in fiscal transparency to align with the global average and peer countries<sup>6</sup>. Heterogeneity in the scores reflects the varying degrees of transparency in the fiscal practices across countries. A limitation of this indicator is his reliance on perception, as the IBP's use of independent experts and government representatives for questionnaire reviews introduces subjectivity into the results.

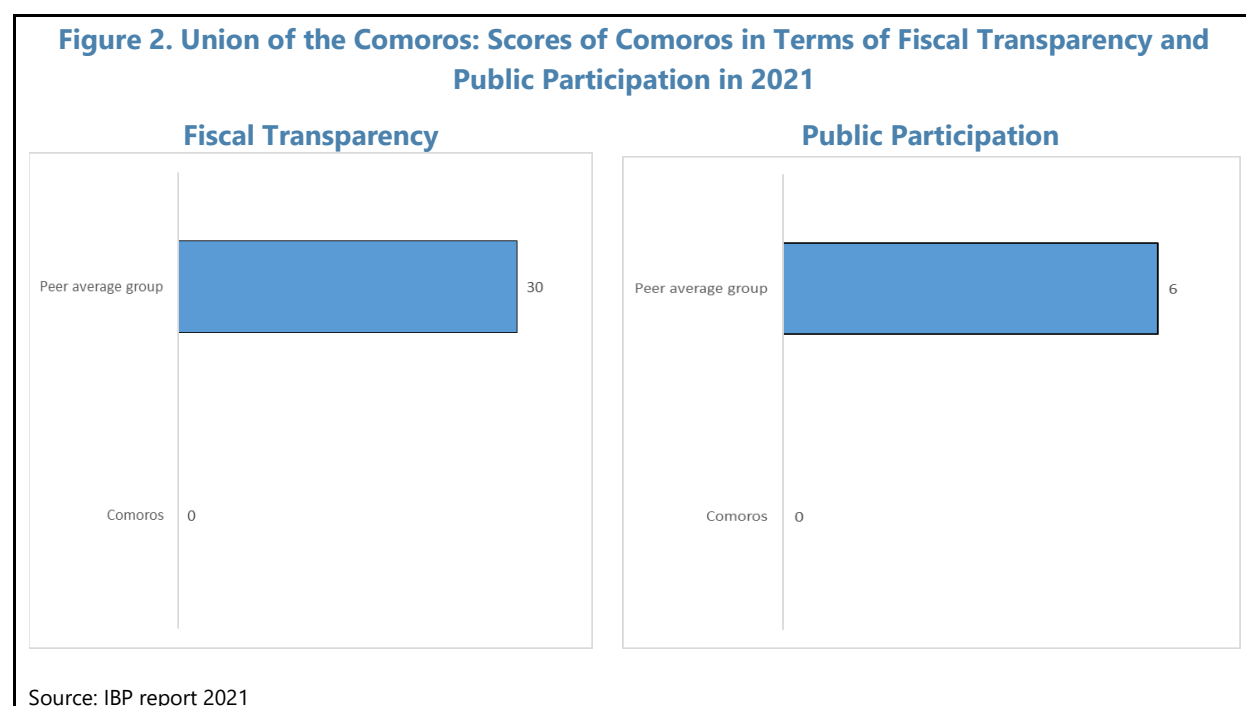
**6. Comoros also sees a low score for public participation in the fiscal process, compared to other peer countries<sup>7</sup>.** While some countries have made efforts to improve public engagement

<sup>5</sup> That document is designed to be easily understandable by the public. It breaks down complex financial information and government expenditures into clear and simple language, graphs, and charts, making it accessible to citizens who may not have a background in finance or economics. The process of reviewing the 2023 index is ongoing and the result should be published by end 2023.

<sup>6</sup> Peers are Sao Tome and Principe, Timor-Leste, Solomon Islands, Tonga, Samoa, Fiji, Cabo Verde, and Seychelles, as these shared similar features with Comoros.

<sup>7</sup> The scale used to measure public participation ranges also from 0 to 100, with higher scores indicating higher levels of public engagement in decision-making processes. The global average for public participation in 2021 was 14.

in budgetary processes, Comoros continue to face significant challenges in fostering public participation in fiscal decision-making. Based on discussions with authorities, ongoing efforts to involve Non-Governmental Organizations and Civil Society Organizations (NGO/CSO) in the fiscal process are evident. However, these initiatives face a significant challenge: they are not formally documented or systematically incorporated into the fiscal framework. Notable developments in this regard include: (i) the recent organization of a public-private dialogue; (ii) the establishment of a formal partnership between the tax administration (AGID) and the Chamber of Commerce, as well as other unions; and (iii) the creation of a joint committee consisting of customs officials and operators to enhance dialogue and strengthen relationships.



**7. While the LOFE provides for public participation through the Budget Orientation Debate, such debate has never been organized.** This debate is a crucial aspect of the budgetary process in many African countries. It serves as a platform for discussing the broad fiscal policies, priorities, and strategies that will guide the government's budget for the upcoming fiscal year. This debate typically occurs before the budget proposal is submitted to the legislative body for approval. During the session, government officials, including the finance minister, present the economic outlook, financial challenges, and proposed priorities for the next budget cycle. Discussions would touch on key sectors such as education, healthcare, infrastructure, social programs, and economic development. The goal is to provide an overview of the government's overall financial strategy and the expected allocation of resources to various sectors. Members of the legislative body, often including representatives from different political parties, can scrutinize the government's proposed plans, question the priorities, and offer their insights and suggestions. This debate encourages transparency, accountability, and public engagement in the budgetary process. Ultimately, the insights gathered during the Budgetary Orientation Debate inform the final budget proposal that is

presented to the legislative body for approval. This process ensures that the government's budget aligns with the country's economic conditions, development goals, and the needs of the population.

**8. The authorities' capacity to prepare the budget proposal needs to be strengthened.**

Currently, the country lacks the production of macroeconomic projections for the budget year and the subsequent two fiscal years and macro-fiscal sensitivity analyses, despite being mandated in the preparation of an economic programming document as per Article 48 of the LOFE. This situation arises from the absence of a comprehensive macro-fiscal model in Comoros, despite training provided by the World Bank. Consequently, the budget proposal submitted to the National Assembly lacks the necessary annexes mandated by the provisions of the LOFE. According to the World Bank's 2022 Public Expenditure Review (PER), there is a need for enhancement in the government's budget law documentation<sup>8</sup>. Efforts need to be directed towards strengthening the skills and capabilities of staff to develop budget proposals across various administrative units.

**9. Weaknesses persist in budget monitoring and reporting, highlighting the urgent need to enhance the capacities of stakeholders, particularly in debt and payment arrears management.**

Concerning budget monitoring, the Ministry of Finance produces quarterly budget execution reports and annual reports, which are currently accessible within the Ministry. Documents related to debt stock and payment arrears are necessary attachments to the budget proposal as stipulated by the provisions of the LOFE. However, in practice, similar to other relevant documents that should be appended to the budget proposal, these documents are not generated due to capacity constraints and a lack of coordination among stakeholders involved in debt contract negotiations. The World Bank evaluates the country's debt management as inadequate, highlighting significant delays in information availability within the Debt Unit of the Ministry of Finance. The Public Debt Reports Heatmap evaluates dissemination practices of public debt in IDA countries, addressing: (i) dissemination of debt statistics; (ii) publication of key debt management reports; and (iii) other debt data including contingent liabilities. This assessment utilizes information from national authorities' websites and expects governments to regularly release debt statistics online to maintain transparency standards for citizens and investors. The results are represented in a heatmap, showcasing strengths and weaknesses by country and indicator, ranked from low (red) to high (green) based on set criteria. Figure 3 illustrates that Comoros should improve its management in terms of debt data accessibility, instrument coverage, sectoral coverage, information on recent contractual loans, periodicity, time range, debt management strategy, annual borrowing plan, and other debt statistics/contingent liabilities. Indeed, the debt management of the country does not exercise central oversight over borrowings contracted by the government, owing to insufficient capacities and lack of coordination among parties involved in debt negotiations. Furthermore, the debt database remains outdated, a consequence of recurring external arrears and frequent renegotiations of debt contracts.

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<sup>8</sup> Indeed, the only document provided with the budget proposal include an explanatory memorandum, a budget presentation note, an annex tables on revenue and expenditure forecasts, macroeconomic assumptions include estimates of economic growth, inflation, and the projected budget deficit i.e., primary balance and the overall balance based on authorization. Meanwhile, details on financing are not provided.

**Figure 3. Union of the Comoros: Debt Reporting Heat Map: 2021**

Source: World Bank.

The World Bank's Public Debt Reporting Heatmap is limited due to assessment criteria being subject to interpretation, leading to potential subjectivity and inconsistency in evaluations across different countries.

## D. Recommendations

**10. The Ministry of Finance, specifically the GDB, is faced with the imperative to undertake a comprehensive range of reforms in both the short and long term.** These reforms are crucial for sustainable fiscal practices. The findings of the PER highlight the pressing need to swiftly implement a series of measures to address immediate challenges. Additionally, they emphasize the importance of formulating and implementing long-term strategies to enhance fiscal transparency and improve the efficiency of budget allocation and execution. Figure 4 provides a roadmap to navigate immediate challenges and forge a sustainable fiscal future. By undertaking these essential short-term and long-term reforms, the ministry can build a robust and responsive financial system that aligns with national priorities and fosters inclusive and sustainable development.

**11. In the near term, the presentation of the budget proposal and the enacted budget law should be revised to incorporate basic information which they do not currently contain.** This includes providing clarity on expenditures and revenues at level two of the GFS classification; information regarding deficit financing; the debt stock for the current fiscal year; and information about special accounts. The inclusion of these additional basic budget elements would already constitute an important first step in enhancing Comoros' PFM process.

**12. Measures should be taken to improve the tracking of and reporting on budget execution.** To strengthen the TOFE production process, a committee clearly tasked with tracking budget execution and producing a timely report on it needs to be appointed and empowered to carry out these responsibilities. This would ensure that the committee is legally empowered to collect relevant information from various agencies within a specified timeframe. As is common practice in other countries, such a committee should be housed at the Treasury where much of the information on revenues and expenditures is collected. The shortcomings in TOFE production are



primarily attributable to significant challenges in the Treasury function, particularly stemming from the absence of the General Directorate of the Treasury and weaknesses in the accounting system, which substantially affect the production of financial information.

**13. To enhance transparency, the authorities should gradually start publishing the various documents supporting the budget process.** The publication of certain documents, such as the annual executive budget proposal, enacted budget law, in-year execution report, annual budget execution report, and the Supreme Audit Institution (SAI) report on the annual financial report are already required by the LOFE<sup>9</sup>, although none are currently published. As shown in Table 2, one of the crucial aspects of fiscal transparency involves the prompt online publication of documents related to the fiscal process. To achieve this objective, efficient coordination between the GDB and the department responsible for managing the Ministry's website is necessary. Several countries in Africa have established dedicated open budget platforms for sharing such data, leading to substantial improvements in their transparency scores<sup>10</sup>. Such an approach could be explored by Comoros, especially considering that many development partners can provide support for such initiatives.

**14. Over the longer term, budget documents, particularly in the budget proposal, would need to incorporate other essential elements.** These include the quantification of tax expenditures, documents outlining medium-term fiscal forecasts, and comprehensive presentations on the implications of new policy initiatives and significant public investments on revenues and expenditures. Additionally, the budget documentation should include more well-founded and detailed macroeconomic assumptions, underscoring the need to develop macro forecasting capacity. Comoros should establish or procure an integrated macroeconomic forecasting model for formulating a medium-term fiscal framework and a medium-term expenditure framework. These tools constitute the basis for the elaboration of multi-year budget and economic programming document which is discussed during the Budget Orientation Debate according the LOFE (see below)<sup>11</sup>. Furthermore, special reports on State-Owned Enterprises (SOEs) and extra-budgetary entities must also be integrated to enhance transparency and oversight.

**15. Moreover, to advance public participation in PFM in Comoros, effective collaboration and prioritized actions among key stakeholders are essential.** Among these stakeholders, the Ministry of Finance bears a significant responsibility. To foster greater public engagement, the Ministry's recommendations encompass piloting mechanisms that involve the public in budget formulation and implementation processes<sup>12</sup>. Furthermore, the Ministry should take proactive steps to connect with vulnerable and underrepresented communities by partnering with civil society organizations that represent them. By encouraging active participation and inclusivity, Comoros can strengthen public participation in this fiscal process. Comoros's Union Assembly also holds

<sup>9</sup> According to the provision of Article 45 of the LOFE.

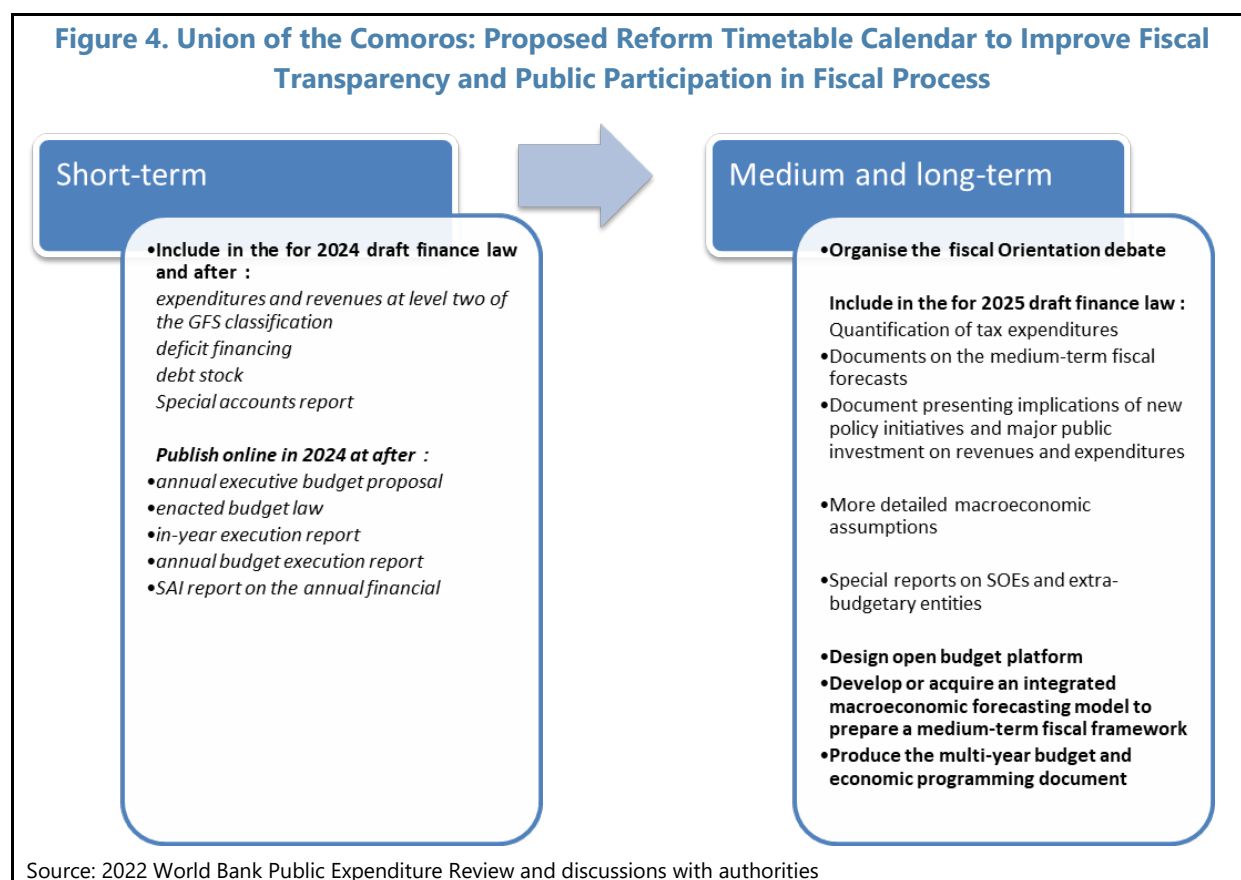
<sup>10</sup> <http://datastandardshelp.imf.org/knowledgebase/articles/792072-opendata-platform-odp>

<sup>11</sup> (1) see the provision of the 2nd paragraph of Article 48 of the LOFE.

<sup>12</sup> Chamber of Trade, Union organizations, NGO/CSO specialized in economics matters.

significant responsibility in fostering public participation. To achieve this, the Assembly should allow members of the public and civil society organizations to testify during its hearings on the budget proposal before its approval. That reform could be implemented easily by organizing the Budget Orientation Debate.

**16. Furthermore, the Accounts Section of the Supreme Court in Comoros should prioritize actions to improve public participation.** It can achieve this by establishing formal mechanisms for the public to contribute to the development of its audit program and participate in relevant audit investigations. By involving citizens in the audit process, transparency and accountability can be enhanced.



**17. Several partners, including the IMF, are providing support to the GDB to implement budget program reform and fiscal transparency, but funding gaps remain for some PFM reforms.** Comoros has benefitted from the Fund's capacity building support in PFM reforms, focusing on the production of the TOFE and the draft SOE law to improve the government's oversight of SOEs and reduce fiscal risks<sup>13</sup>. In collaboration with several government entities,

<sup>13</sup> IMF Afritac South carried out a technical assistance mission aimed at outlining specific actions related to the implementation of the amended version of the LOFE. This mission pinpointed 61 actions grouped under 19 axes. Only a few of these actions have garnered funding, underscoring the pressing need for further technical and financial

UNICEF's notable partnership with the General Directorate of Budget was prominent, particularly in crafting the 2023 citizen budget. Working closely with partners, including the Ministry of Finance and the Assembly, UNICEF played an essential role in ensuring the participation of the Civil Society Organization, Citizen Initiative on Budget Transparency, during the 2023 budget review conferences' fiscal process. Other partners have contributed to the production of the Citizen Budget and budget program reform. However, despite all these efforts, further activities crucial to the comprehensive overhaul of the PFM system. These activities may include capacity-building efforts, technical assistance, and the adaptation of the information system<sup>14</sup>. Despite the efforts made by existing partners, the GDB requires further financial backing to address the complexities and challenges associated with public finance reform effectively. Sustained financial support from others developing partners is essential to facilitate the successful implementation of comprehensive reforms, which will, in turn, lead to more transparent, efficient, and accountable financial practices within the government. By doing so, the GDB can drive substantial improvements in fiscal management, bolster economic growth, and effectively utilize public resources to address critical social and developmental needs.

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support. Successfully executing these measures is pivotal for enhancing Public Financial Management (PFM) in Comoros, enabling the country to achieve its socio-economic development goals.

<sup>14</sup> Adapting the current SYMBA information system will enable its modification to facilitate the transition to the program budget scheduled for 2028. This will also involve ensuring integration with other information systems such as GISE for salary management purposes.

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