Making Benchmarking Effective: Risks and Opportunities

Benchmarking and diagnostic efforts of the type presented here can have obvious benefits. However, the realization of these benefits depends on deploying the tool in a way that is consistent with local needs and priorities.

Conceptually, effective benchmarking and diagnostics can allow both domestic and external actors to develop a more nuanced view of reform needs and priorities. In particular it can support a move away from a narrow focus on total tax collection in favor of an emphasis on, among other elements, equity, accountability, cooperative models of compliance, increasing transparency and the careful development and management of human resources.

Operationally, effective benchmarking and diagnostics can assist efforts to identify reform needs, while providing useful benchmarks against which to judge reform progress. Internationally comparable information about national tax systems can play a useful role in supporting experience sharing and the identification of potential areas for reform.

However, alongside these benefits there are also significant risks. The primary goal of diagnostic and benchmarking exercises should be to better understand the strengths and limitations of existing systems and practices in order to guide reform efforts. However, benchmarking and diagnostic exercises can easily become excessively focused on ranking tax systems in order to facilitate cross-country comparison and simple quantitative judgments about system effectiveness. These latter possibilities can be a useful additional benefit of benchmarking and diagnostic processes, but an excessive focus on international ranking and comparison can distort and undermine broader effectiveness.

In practice it is frequently donors and external actors who are most heavily focused on international comparison, while local actors are primarily concerned with targeted diagnostic exercises that can inform reform priorities. This can lead to tension and disengagement if local actors feel that a resource intensive benchmarking and diagnostic exercise is oriented too heavily towards donor concerns rather than supporting local priorities. These risks are likely to be amplified if local actors are confronted by multiple and contrasting diagnostic exercises that consume valuable resources while primarily serving external agendas.

Such tensions can have both short-term and long-term consequences.

In the short-term local actors may choose to disengage from, or undermine, a benchmarking and diagnostic exercise that they view as holding little value. Effective implementation demands the compiling of extensive data and information by tax administrations, and the quality of that data is likely to be closely linked to the value that local actors place on the process. As Vazquez-Caro and Bird (2011) have written, “If those who must generate most of the critical data needed for a benchmarking exercise are aware
that they will be judged by it, and they see no direct benefits for themselves from accurate reporting, accurate reporting is unlikely to ensue."

Over the longer-term the imposition by donors of benchmarking and diagnostic exercises that are viewed as unnecessary and unproductive by local actors is likely to undermine the development of the types of strong and open partnerships that are necessary to support reform effectively. Tax administrators in various parts of the world have expressed frustration with such externally mandated processes, which they view as indicative of the absence of genuine partnership.

In the worst case externally driven diagnostics efforts may come to play an excessive, and ultimately counterproductive, role in shaping reform efforts. Where external engagement becomes excessively focused on such cross-country indicators it can lead to reform that is focused on meeting specific short-term targets rather than on achieving longer-term reform and development goals. For example, a focus on individual targets may lead to individual reform objectives being addressed as isolated challenges rather in the context of holistic reform strategies. A focus on specific targets may similarly lead to the privileging of more easily attainable goals over important longer-term investments, or to efforts to achieve particular targets even at the expense of more important, but less easily quantifiable, goals. Finally, a narrow focus on targets disconnected from local realities may lead to a focus on priorities that are inconsistent with local political economy constraints and needs.

These challenges do not lend themselves to simple solutions, but highlight the need for an emphasis on making diagnostic exercises relevant to local needs, rather than becoming excessively focused on the collection of internationally comparable data and the development of narrowly defined reform goals.

Vazquez-Caro and Bird (2011) have argued that benchmarking needs to move away from simple “benchmarking by numbers” in favor of a systemic approach focused on “considering how all aspects of the administrative system function as a whole in the context of the environment within which that system is embedded and operates.” The key insight is that tax system performance depends on how the different elements of the tax system fit together, while reform priorities can only be identified and fully understood in light of a broader understanding of the overall tax system environment.

Seen in this light, a benchmarking exercise focused only on gathering discrete pieces of data is likely to be useful to external actors, but much less useful to domestic actors. The corresponding challenge is to ensure that the data gathering exercise forms part of a locally embedded benchmarking and diagnostic process that is closely linked to the immediate reform challenges confronting different tax administrations.