**8. Revenue Management and Distribution**



Once EI revenues have been generated and collected, government must decide on their management and allocation. Options include spending or saving, with decisions required on appropriate channels or mechanisms for each. The volatility of resource revenues presents a special challenge, addressed in many countries through resource funds. Sharing of resource revenues among levels of government and regions is increasing common and requires careful balancing of pros and cons.

The fourth link in the EI Value Chain is concerned with **Revenue Management and Distribution**. A failure to manage and distribute the wealth arising from oil, gas and mining operations can lead to the promotion of social and economic inequalities, the funding of corrupt practices and the generation of intra-state or even-inter-state conflicts. Transparency, which has been identified as a cross-cutting topic, is crucial to achieving success in these areas. This Chapter examines some of the issues that typically arise relating to the management and distribution of revenue generated from EI activities, and the instruments such as fiscal rules or special funds that governments may adopt to tackle them. It is designed to support policy-makers in their decision-making.

Good practice in resource revenue management is increasingly recognized, yet the experience of most resource-rich developing states has not been especially encouraging. This suggests that there are continuing problems in the implementation of resource revenue management good practice.  As always, the lessons from good practice for avoiding common pitfalls have to be understood in a contextual manner. Where they appear relevant, they need to be adapted to fit the particular circumstances of the country concerned. Those circumstances will include: the level of development; nature of the resources and their size; fiscal dependence on resource revenues; institutional capacity, fiscal federalism, budget rigidities, transparency levels and capital scarcity. So, there can be no such thing as combining the best lessons into a ‘standard model’ that a single government can blindly follow.[[\*]](http://eisourcebook.org/reference.php?id=298)

It is worth recalling the kind of starting piont that is likely to be typical for a country that has recently discovered large-scale natural resources in the developing world. At least three important contraints are likely to be present: a scarcity of capital, with an interest rate higher than the global rate, and limited access to international capital markets, possibly as a result of the country's credit rating; an undersupply of public infrastructure, and an investment climate that has depressed private investment. In a number of African countries this starting point is likely to be compounded by their landlocked status. From these inauspicious circumstances, the country has the prospect of making high return investments and putting its economy on a growth path that will involve capital deepening with the rate of return converging to the world rate. At the same time, wages, consumption and income will move on an upwards trajectory. As two leading development economists note, the question for government in such circumstances is then: "what is the optimal consumption profile: i.e. that maximizes the present value of the utility of cosumption given available investment opportunities?"[[\*]](http://eisourcebook.org/reference.php?id=297)

**Why does revenue management always present challenges?** The importance of revenue management cannot be exaggerated: “[s]ince oil revenues are to a large part concentrated in the public sector, the question of how the oil revenue should be spent and distributed across present and future generations becomes key to any economic development.”[\*] The same observation can be applied to mining.

Three areas of sensitivity underline this priority:

* Firstly, the exhaustibility of oil, gas and other mineral resources raises inter-generational issues and also reveals a need for balance between government consumption and saving for the long term. Policy makers need to strike a balance between spending today and saving for tomorrow.
* Secondly, the question of what to do with the large rents generated is complicated by the fact that the revenues are for the most part generated abroad (although linked to the resource in the host country), creating issues about macro-economic absorption capacity and competitiveness.
* Thirdly, a crucial source of complexity in revenue management is the idea that since ownership of the natural resources vests in the people, the revenues should be shared or distributed among the people.

In responding to this context, any design of revenue management rules is complicated by the uncertainty of estimates of oil receipts. Indeed, he overall policy for EI resource development needs to take into account the volatility, uncertainty and cyclical nature of prices as well as imprecise assessments of reserves and the finite character of the resources involved. As a result, policies have to be designed in ways that avoid transmitting this volatility (which is outside the control of policy-makers) into the macro-economy, and also take into account the need to smooth spending flows, promote long-term fiscal sustainability and inter-generational equity, and enforce measures to mitigate Dutch Disease (see the discussion in Chapter 2 and Chapter 5.1 of overall resource policy).

Experience suggests that success is often elusive: "(c)apital flows, fiscal policy, monetary policy, and sectoral allocation each tend to be more procyclical in commodity producing countries than economists' models often assume. If anything, they tend to exacerbate booms and busts instead of moderating them."[[\*]](http://eisourcebook.org/reference.php?id=296)Another study of increased revenues from oi production concuded that "implementation of quantitative fiscal rules have proved very challenging, mainly due to the characteristics of oil revenue and political economy factors... Many countries have had difficulty managing funds with rigid operational rules, as tensions have often surfaced in situations of significant exogenous changes or with shifting policy priorities."[[\*]](http://eisourcebook.org/reference.php?id=299)

In practice, government authorities are often faced with a limited number of options with respect to the allocation of EI sector revenues. These options tend to fall under two general headings: spending (comprising consumption and domestic investment); or saving (through asset accumulation or debt reduction, where interest rates are higher than the social rate of return on domestic investment). For an increasing number of governments the sub-national dimension of revenue management is also becoming a source of complex and sensitive issues, often with a constitutional aspect. In virtually all cases, transparency in relation to revenue management has become linked to the legitimacy of the model they use.