

Oil to Cash: Fighting the Resource Curse through Cash Transfers

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This brief is a summary of the book *Oil to Cash: Fighting the Resource Curse through Cash Transfers* (Washington, DC: Center for Global Development, 2015).

Summary

As poor countries continue to discover massive deposits of natural resources—oil in Nigeria, gas in Timor-Leste, copper in Mongolia, and more—they face the daunting prospect of translating windfall income into broad economic gain and political progress. In the worst cases, corruption and mismanagement waste revenues, and citizens hardly see any benefit. Even if income is spent well, public spending drawn primarily from resource revenues has the deleterious effect of eliminating the need to tax citizens and thus severs the crucial link of accountability between a government and its people.

We propose a new policy solution, “Oil-to-Cash,” which would provide every citizen the right to a dividend of their nation’s resource wealth through a regular, universal, and rules-based cash payment. Oil-to-Cash would benefit both citizens and governments by transferring cash directly into the hands of the people while creating incentives to restore the social contract built on taxation and accountability.

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Why Oil-to-Cash?

Pitfalls of Natural Resource Windfalls

Responding to new windfall gains is a challenge for a huge number of developing countries. Even with recent price downturns, some 50 out of Africa’s 55 countries are either producing or exploring for oil. Yet too often, the potential of oil, gas, minerals, timber, diamonds, and other resources has been lost. Instead of delivering a better life for citizens, national prosperity, or a robust polity, these discoveries have time and again largely benefited a small elite. Oil and other sources of unearned income are thought to fuel corruption, political

repression, export overconcentration, and even conflict.¹

This paradox is evident over time and across regions, yet many new producers have failed to take more than token steps to address the risks. The policy community has many useful ideas to fight the resource curse, such as ring-fencing revenues and boosting transparency. These measures are huge steps forward for any country, but they

1. Among a rich literature, please see: Ross, Michael. *The Oil Curse: How Petroleum Wealth Shapes the Development of States*. Princeton, NJ: Princeton University Press, 2012; Gelb, Alan. *Oil Windfalls: Blessing or Curse?* Oxford, UK: Oxford University Press, 1988, published for the World Bank; Karl, Terry L. *The Paradox of Plenty: Oil Booms and Petro-States*. Oakland, CA: University of California Press, 1997.

The Three Steps of Oil-to-Cash

1. Create a separate fund to receive windfall revenues.
2. Formulate clear rules for paying universal, regular, and transparent dividends directly to citizens.
3. Use the dividend mechanism to build a broad tax system.

are only partial measures that bolster the *supply* of information while not yet producing sufficient *demand* for better governance. They do not address the underlying problem that citizens don't feel the income is theirs, the government doesn't care what citizens want, and there is little bridge between the two. In other words, windfall income exacerbates the lack of a social contract. This is the fundamental link that Oil-to-Cash seeks to rebuild.

Potential of Cash Transfers

Oil-to-Cash rests in part on the notion that distributing revenues directly to citizens will advance development more effectively and more equitably than through government coffers. Is this

assumption true? After all, governments have years of experience managing budgets for health, education, and other public services. Why might transferring cash directly to citizens provide any greater benefit?

Countries across Africa, Latin America, and Asia have been experimenting with cash transfers for years, most famously in Mexico and Brazil. The ample and growing literature around these programs is especially encouraging, providing

evidence for positive effects of cash transfers, such as mitigating chronic poverty, narrowing income inequality, boosting nutrition, increasing school attendance, enhancing healthcare access, and even encouraging local business investment.² Oil-to-Cash builds on these results by providing a steady cash transfer to all citizens linked to their country's natural resource income.

Supporting a Social Contract

Oil-to-Cash, at its heart, is about strengthening the incentives for good governance. The lack of accountability between a government and its people in resource-rich countries stems, in part, from the absence of a social contract. The bargain that usually ties those in power to the citizenry has been severed: citizens don't pay taxes and the government doesn't provide quality public services. As a result, people don't expect much from their government, and public officials aren't responsive to citizens' interests. Because Oil-to-Cash includes a tax to be paid by citizens on their resource dividends, it offers an opportunity to build the social contract by creating tax-paying citizen shareholders.

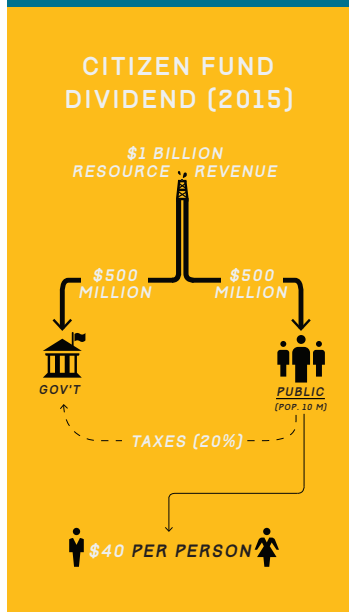
What Is Oil-to-Cash?

Countries can sidestep the challenges associated with an oil bonanza by converting the revenue into regular income for their citizens through cash transfers. This is the Oil-to-Cash approach, and it is applicable to any windfall income. Thus, the proposal applies to gas-to-cash (Timor-Leste, Mozambique), gold-to-cash (Zambia, Mongolia), ore-to-cash (Liberia, Guinea), and even strategic-location-to-cash (Djibouti, Panama). Although the specifics will differ from country to country, the basic approach is grounded in three essential steps:

1. Create a Separate Fund to Receive Windfall Revenues

Governments receiving oil or mineral revenues would first funnel income, including signing bonuses, royalties, and other taxes, into a transparent and ring-fenced special fund. This

Figure 1: Sample Card



2. Among a vast literature, a good summary is: Department for International Development (DFID-UK). "Cash Transfer Literature Review." London: DFID-UK, 2011.

initial receiving fund can serve multiple functions: promoting transparency, serving as a mechanism for spending triage, and bringing stability to often volatile revenue streams. It could also have predetermined allocation rules, such as a division of income split between the public budget and the dividend payments.

2. Formulate Clear Rules for Paying Universal, Regular, and Transparent Dividends Directly to Citizens

Dividends should be:

- **Equal and universal.** Transfers should be based on the principle—enshrined in most constitutions—that natural resources belong to citizens, not just the government or political elites. As such, payments should ideally be made in equal amounts to all citizens, regardless of the specific location of the natural resources, thus supporting national unity and helping to create a broad constituency.
- **Paid on a regular schedule.** Because transfers are a right of citizenry, not a gift from politicians, the frequency of payments should occur on a predictable schedule rather than at the discretion of officials. Beneficiaries are able to plan their spending when they know in advance when they will be paid.
- **Calculated on clear and transparent rules.** Similarly, the amount of each dividend should be based on easy-to-understand and well-publicized criteria. (Alaska's Permanent Fund dividend, for example, is based on 50 percent of the five-year average income from the state sovereign wealth fund, divided by all state residents.) This approach enables beneficiaries to understand how commodity income affects them, and they can confirm they are receiving the correct amount.

3. Use the Dividend ID and Delivery Mechanism to Build a Broad Tax Collection System

Part of the distributed dividends should be taxed back to finance public services, potentially starting as a withheld portion but eventually transitioning to directly paid taxes. This may initially seem

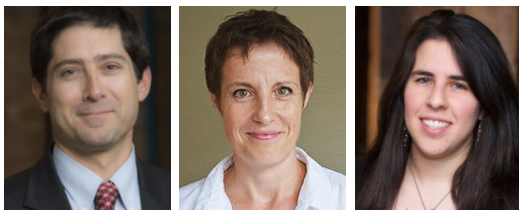
inefficient: why distribute money, only to then take some of it back? But taxes create an essential bond between people and the state. Bargaining around taxes generates positive engagement between and among governments, citizens, and firms, and creates an incentive for citizens to hold governments accountable in managing and spending their money.

How Can Oil-to-Cash Work?

Implementing Oil-to-Cash will vary from country to country. Fortunately, recent technological advances make the key components increasingly feasible and affordable. The four components for any such program to work include:

- **A public information campaign.** Building public understanding and support for the program may take time, but it can be aided by clear multimedia campaigns. Policymakers and civil society groups can use community meetings, radio, and even SMS messages and social media. Billboards, posters, and handheld cards could explain the concept with simple math (see Figure 1).
- **Reliable identification.** Biometric ID systems, which use unique physical characteristics such as fingerprints or irises, can help reduce the risk of fraud. Many countries are already building these systems, with more than one billion people in developing countries already having their biometric data recorded.³
- **Electronic money transfer.** The current revolution in electronic and mobile payments offers a safer and more efficient method to distribute cash transfers. By connecting every biometric ID to a mobile bank account, funds can be easily transferred, fraud can be minimized, and the results can be audited.
- **A tax system.** The same ID + e-banking formula to distribute dividends can form the backbone of a national tax collection system. Payments merely flow in the opposite direction.

3. Gelb, Alan, and Julia Clark. "Identification for Development: The Biometrics Revolution." Working Paper 315. Washington, DC: Center for Global Development, 2013.

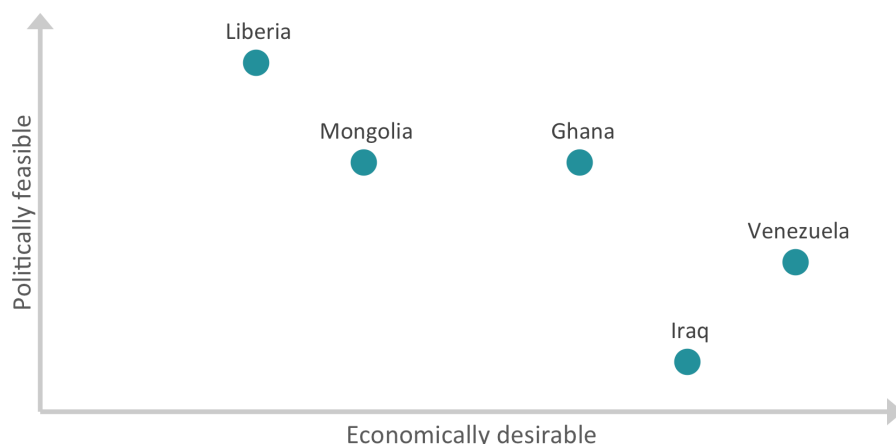


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Figure 2: Best Potential Cases for Oil-to-Cash



Source: Authors' estimates.

Where Is Oil-to-Cash Most Likely?

Which countries are best positioned to actually try Oil-to-Cash? Of course, Oil-to-Cash is a proposal that will become substantially messier when it is applied in the real world. The idea doesn't apply everywhere and, where it is attempted, it will have to adapt significantly to local political and economic conditions. Nevertheless, there are economic and political factors that make some countries more promising candidates. Oil-to-Cash is likely more economically desirable in countries with high resource income per capita, poor business climates, and the worst corruption. This scheme may be most politically feasible where there are new resource discoveries, a new political order, a competitive democracy, or a country whose current leaders are focused on a long-term legacy. A few examples of these best cases are noted in Figure 2.

Conclusion: Time to Try It

Barring a major disruption in the global economy, a growing number of countries face the prospect of becoming dependent on natural resource revenues. Thus, managing resource windfalls will remain a pressing issue for governments and citizens across Asia, Africa, and Latin America. Some variant of universal dividends or a resource revenue-linked national cash transfer program will be implemented somewhere in the near future. It will be an experiment, and many things will go wrong. But other countries will learn from their successes and mistakes, just as we are all now learning from policy experiments in Nigeria, Alaska, Mongolia, Ghana, India, and elsewhere. Creating citizen shareholders and putting the wealth of nations into the hands of the true owners—the people—is a powerful idea that deserves attention. Now is the time to put it to the test.



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