

## Financing for Sustainable Development in the Future

2014



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Introduction

In 2015, a new set of global goals will be adopted that aims to combine goals from both a development agenda (post-Millennium Development Goals) and a sustainability agenda (Sustainable Development Goals). The new global agenda on sustainable and inclusive development<sup>1</sup> will need to be supported by a comprehensive strategy to mobilise the necessary means for its implementation, including both financial and non-financial means. With regard to financial resources, it will require far more official grants and highly concessional loans than global levels of Official Development Assistance (ODA) currently provide, even though most of its financing will come from domestic resources.

The UN Secretary General and institutions such as the World Bank and the EU, among others, have called for the post-2015 agenda to include the goal of ending extreme poverty in the world by 2030. In its report, the High Level Panel of Eminent Persons on the Post-2015 Development Agenda (HLP) emphasised that no target should be considered achieved until it has been met for every income and social group. This means that no-one should be left behind.<sup>2</sup>

At the same time the Dutch and German governments contributed to the debate on funding by starting an international discussion on the future definition of ODA. The points raised by these governments include:

- The current ODA definition does not measure results
- It takes no account of financial innovation and private actors
- It does not accommodate new donors
- It includes countries that are no longer poor
- Recipient countries are diverse and ODA does not appropriately reflect this
- Some expenditures are included that do not represent flows to developing countries.

This position paper presents VENRO and PARTOS’ position on how to enhance the current ODA reference framework in order to monitor progress and effectively advocate the new global sustainable development agenda.

The following examines the opportunities provided by the positions constituting the current debate on reforming the development finance system and the risks they involve. This paper then summarises a number of proposals from German and



A young girl participates in a tree planting campaign at one of Haiti's last pine forests

Dutch civil society organisations aimed at developing a new monitoring reference system for post-2015 Financing for Sustainable Development (FfSD).

The scope of a new Financing for Development Reporting System: ODA, Official Climate Finance Cooperation and private financing as separate categories within a new framework

The UN Agenda on Financing for Development consists of six working areas that take into account the different financing needs and diverse functions of specific resource flows for development. These are: a) domestic resource mobilisation; b) Foreign Direct Investment (FDI) and other private flows; c) trade; d) ODA; e) debt relief; and f) the development coherence of the international financial and economic system. Furthermore, climate change is addressed as an emerging issue.

<sup>1</sup> Sustainable development should be understood throughout this paper as referring to sustainable and inclusive development.  
<sup>2</sup> UN High Level Panel Report on the Post-2015 Development Agenda: ‘A new global partnership: eradicate poverty and transform economies through sustainable development’, p. 9.





A farmer on his way to paddy fields in Central Java, Indonesia

Three areas should be assessed separately within a new reporting system for sustainable development financing according to the specific role these resources play in development. These areas are:

- **Measuring Official Development Assistance**  
ODA is a unique source of financing since it can directly target policy sectors that are crucial for poverty eradication, governance, the implementation of human rights, democratic ownership, and specific Global Public Goods (GPGs) such as health. Its definition should be sharpened in order to count effective flows in line with the Busan agreements, rather than opened up as a means of integrating flows with questionable impacts on development (see Section 2).
- **Measuring Official Climate Finance and other Global Public Goods**  
Climate change is a growing challenge for development and an additional burden for developing countries that requires additional financing beyond ODA. It is essential to ensure that countries are able to mitigate climate change and adapt to the changes it will cause. Furthermore, GPGs such as forests, biodiversity and oceans need to be protected, and this is in the interest of the entire world. At the same time, poor countries are the least able to protect themselves from the consequences of polluted GPGs. As climate adaption and mitigation is a GPG, related measures should be financed and reported separately, according to the polluter pays principle (see Section 3).

- **Measuring Foreign Direct Investment and private flows**  
Whereas ODA and Official Climate Finance require a public budget from donor countries, FDI and private flows have no such requirement. They are profit-driven in nature and their impact on social development is often questionable. Therefore, these financial flows should be reported separately in order to avoid blurring the lines between public responsibilities and private engagement (see Section 4).

Furthermore, it is not only essential that financial flows from donor countries are recorded, but that other development-related donor actions are also recorded to ensure policy coherence for development.

- **Measuring policy coherence for development**  
Whilst financing for development is important, other forms of donor action in development-related policy sectors also affect developing countries and hamper their prospects. The UN agenda on Financing for Development is already involved with some of these structural issues (trade, the international financial and economic system). These issues are important elements of any new reporting system aimed at assessing the net impact of policies and overall donor action. This is particularly the case with regard to sustainable development and when a system is to be used as a Policy Coherence for Development index. A useful addition to this system would be the introduction of a ‘price tag’ on policy incoherence (see Section 5).

## 1. The context and principles behind a new reporting system for the financing of sustainable development

### Setting the context: Financing needs in developing countries are enormous

The question of how to set up a new reporting system for sustainable development financing should not be viewed and discussed in isolation from the debate about specific financing needs for sustainable development and the appropriate resources to meet these needs.

Estimating the exact financing needs for sustainable development is a difficult task. Funding requirements clearly depend on the goals established under a new global sustainable development agenda and the timeframes in which they are to be achieved, as well as on how much financing can be mobilised from domestic savings, from for-profit cross-border flows, and from grants and official lending.

The UN System Task Team on the Post-2015 UN Development Agenda’s Working Group on Financing for Sustainable Development has calculated rough investment needs in different scenarios. It stated that “investment requirements for the energy transition respecting agreed climate targets are huge, of the order of trillions US\$ per year. [...] Investment requirements for MDGs and other related goals (e.g. universal access to electricity) are one order of magnitude lower than those related to climate change mitigation. [...] The order of magnitude of estimated investment requirements for the management of global commons (biodiversity, oceans, and forests) is several tens to hundreds of billion dollars per year.”<sup>3</sup>

Even though only rough estimates can be given, there is no doubt that finding sufficient financing for an ambitious sustainable development agenda will require huge efforts by all political actors, especially if this agenda aims to eradicate poverty by 2030, secure sustainability and realise basic human rights for all as well as implement democratic governance. The UN Working Group emphasises: “Financing needs for sustainable development are enormous. Different

estimates of financing needs all confirm that there are large requirements across all critical sectors.”<sup>4</sup>

### Recommendations

- Countries, private actors and NGOs need to clearly express their willingness to take action and fight global poverty.
- The new reporting for sustainable development system should be linked to the needs debate in sustainable development.

### Both public and private financing are needed

In order to meet these requirements, both private and public financing from domestic and international sources will have to be increased. It is important to note that public and private flows “serve development goals better if they are seen as complements rather than substitutes, as each type of financing has unique objectives.”<sup>5</sup> However, aid still has a unique role to play in this setting (see below).

Over the past few years, financing for development instruments have become more diverse. FDI in developing countries has increased massively,<sup>6</sup> and this has altered the picture of the financial resources reaching poor countries. “Today, traditional ODA accounts for approximately 20% of net external flows of developing countries whereas it represented around 50% in the 1960s. Total ODA from member countries of the Development Assistance Committee (DAC) currently stands at about USD 130bn per year, far behind remittances, over USD 345bn, and foreign direct investment, around USD 414bn.”<sup>7</sup> It has been argued that it may be easier to further boost private financing than increase ODA as a means of fostering sustainable development. This argument, however, neglects the different objectives of these various sources of financing and does not differentiate

<sup>3</sup> UN System Task Team on the Post-2015 UN Development Agenda Working Group on “Financing for sustainable development”, Executive Summary, p. 4.

<sup>4</sup> Ibid. p. 1.

<sup>5</sup> Ibid.

<sup>6</sup> According to Development Initiatives, the volume of international resources received by developing countries has more than doubled since 2000, reaching an estimated US\$ 2.1 trillion in 2011. Development Initiatives: Investments to end poverty. Real money, real choices, real lives. September 2013, p. 3. Available at: [http://devinit.org/wp-content/uploads/2013/09/Investments\\_to\\_End\\_Poverty\\_full\\_report.pdf](http://devinit.org/wp-content/uploads/2013/09/Investments_to_End_Poverty_full_report.pdf)

<sup>7</sup> Tomasi, Serge: Proposal for a new journey. October 2013, p. 1.



between countries and sectors (see below). Although its significance for donor governments seems to be declining, ODA remains an important tool for financing development.

This is especially true for the least developed countries. An analysis by Development Initiative revealed that “82% of the world’s extreme poor live in countries where government spending is less than US\$1,000 per person per year (measured in purchasing power parity (PPP) terms), compared with PPP\$15,025 across DAC countries. (...) More than 100 million people in extreme poverty live in countries where government spending is less than PPP\$200 per person per year (55 cents a day), and in those countries more than half the population lives below the \$1.25 a day poverty line.”<sup>8</sup> These severe spending constraints will continue, and aid plays a vital role in these countries. In particular, it provides 60% of external financing for low income countries in Sub-Saharan Africa.

### Recommendations

- Both, private and public financing need to be increased to finance sustainable development. These sources should be seen as complementary to ODA, rather than substitutes in the fight against poverty and for sustainable development.
- More evaluation of the different development impacts and purposes of private and public finance are needed.

A woman hoes a field near Timbuktu, Mali



### Effectiveness and counting net flows as core principles of a new framework

Different financial instruments have different impacts on the fight against poverty and the realisation of human rights. Therefore, any new FfSD reporting system needs to take into account total financial flows, and the composition of development financing. For example, this should include counting financial flows that really have an impact on poverty eradication and sustainable development.

Development effectiveness should be the aim of all financial flows. Major donor countries as well as a number of civil society organisations (CSOs) and organisations representing private sector interests have committed themselves to promoting development effectiveness by complying with the international standards set out in the Busan Partnership. Although the Busan Partnership is neither universally accepted nor endorsed by all donor governments or CSOs, it serves as a useful basis on which to build a new FfSD reporting system.

This is particularly the case with issues such as transparency, predictability/volatility of flows and tied/untied aid, and deciding whether the different instruments of public and private financing for developing countries actually support national priorities and democratic ownership. In practice, this means highlighting as effective those financial flows that are in line with the Busan agreements.

Furthermore, it is not only essential to count inflows but also outflows from developing countries in order to produce an overview of net flows between donor and developing countries. This is already the case regarding ODA when loans are repaid by developing countries and, consequently, deducted from ODA. However, there is still room for improvement in the current ODA system (see Section 2). This should also be the guiding principle behind the measurement of other financial flows such as official climate financing (see Section 3) and private flows (see Section 4).

### Recommendations

- A new FfSD reporting system should be based on the Busan Partnership agreements and integrate criteria such as transparency, predictability/volatility of flows and tied/untied aid. It also needs to enable decisions to be made on whether the different instruments of public and private finance for developing countries support national priorities and democratic ownership.
- A new FfSD reporting system should also count and map financial outflows, for example tax evasion or illicit financial flows (see Section 4).

## 2. Retain ODA as an important part of a new system and reaffirm the 0.7% target

### Reform ODA and reaffirm the 0.7% target

European NGOs have long campaigned for a realistic and explicit definition of ODA. All parties accept that ODA should be retained as a measurement of public financial contributions to development. Therefore, a new reporting system should include ODA as a standalone category because of its importance as a large source of external public flows and the unique role it plays in the development process. The current discussion is an opportunity to clearly define ODA and exclude controversial factors that are not directly aimed at promoting development.

ODA should be clearly focused on eradicating financial poverty; the fulfilment of human rights, and implementing democratic ownership. It is a crucial source of public financing especially for Low Income Countries (LICs) and a key factor in the creation of an environment that enables social development.

While other resource flows, such as domestic resources, outweigh ODA by volume, aid continues to play a crucial role in contexts where government spending is low. This can also be seen in Middle Income Countries (MICs) where aid may play a catalytic role in leveraging larger resources for poverty reduction. In LICs, ODA is a critical source of funding and amounts to 10% of their GDP.<sup>9</sup> Besides its necessity, ODA is also a normative obligation and a powerful expression of global solidarity. ODA is a long-term source and should be a transparent and accountable form of finance.

1.2 billion people still live below the extreme poverty line of US\$1.25 per day; many more live just above this line. In the coming years, developing countries will face a financing gap of US\$150 billion (€112 billion) annually, which will be needed if they are to tackle the challenge of poverty.<sup>10</sup> Poverty is caused and exacerbated by a variety of factors, including a lack of human rights and social equity; inequality, the current political framework, climate change, economic growth, conflict and insecurity.<sup>11</sup>

In this context, ODA can make an essential contribution to development. First, ODA financing and technical assistance can help create a domestic and internation-

al enabling environment for development, includes peace, security, and the rule of law, but that also effectively and adequately finances governments. ODA can help allocate domestic resources and this increases accountability and effectiveness. It can strengthen the capacity of the domestic financial sector to facilitate long-term financing, and provide appropriate access to financial services for the poor and for small and medium enterprises.<sup>12</sup>

Second, ODA may play an even more important role in countries such as LICs that are less attractive to private investors. Within these countries, ODA can contribute to shared domestic growth and prosperity by building social systems, especially social protection floors that are particularly needed by the poorest. It can do so by providing predictable financing, whereas private flows are often highly volatile. Donors need to deliver on their commitments, particularly to the most vulnerable countries such as the Least Developed Countries (LDCs) and countries in conflict or emerging from conflict.

Third, ODA is indispensable in sectors that are at the core of poverty eradication and which should not be under the control of private companies, such as small-scale farming, education, health and the realisation of human rights, including gender equality. Spending on health has increased substantially in developing countries since 2000 due to increased external assistance in this sector. Although the MDGs focusing on health are unlikely to be met in many countries, ODA has contributed to improving the health situation in these countries. The role ODA plays in social sectors cannot be substituted by the private sector, as the private sector is profit-oriented and investments in these areas do not always deliver financial returns. Furthermore, a massive increase in private financing for public purposes is unlikely to happen; thus international public financing will remain a critical resource for development. ODA is key to the role of government, due to its implications for the realisation of human rights and democratic governance. While the private sector can play an important role in upholding rights and the adherence to transparent governance principles, by definition its role is limited to enterprise.

<sup>8</sup> Development Initiatives: Investments to end poverty. Real money, real choices, real lives. September 2013, p.4

<sup>9</sup> OECD DAC insights/Blog by Lorna Gold, Head Trócaire/member of CIDSE.

<sup>10</sup> AidWatch Report/Greenhill R and Ali A, 2013, ODI.

<sup>11</sup> Development Initiatives: Investments to end poverty. Real money, real choices, real lives. September 2013, p.16.

<sup>12</sup> Brot für die Welt Text/Notes on a Multistakeholder Consultation Organized by the Permanent Mission of Chile to the United Nations.



The UN Working Group on Financing for Sustainable Development reviewed estimates of the level of global investment that would be required to reach the MDGs and ‘global commons’, which they defined as infrastructure, agriculture, land management and rural development; energy, climate change mitigation and adaptation, forests, biodiversity and oceans. They concluded that additional investments are necessary to meet the MDGs. In terms of quantity, the UN Working Group estimated the magnitude of investments needed for the global commons as even higher than the investment required to realise the MDGs. To meet the MDGs, additional investments in the range of US\$20 billion to US\$200 billion would be needed. The necessary proportion of ODA has only been calculated for LDCs, but their additional needs of US\$62 billion annually indicate that the figures are likely to be high. In 2013, the ODA expenditures of all DAC countries amounted to US\$135 billion or an ODA quota of 0.3%. The 0.7% target thus seems to be a minimum demand. The international commitment by developed countries to spend 0.7% of donor Gross National Income (GNI) on development should thus not be abandoned until development objectives have been met. Reaffirming this internationally agreed benchmark is essential and should be accompanied by new incentives and pressure for donor action. Donors should respond by achieving this benchmark as soon as possible, by setting clear timetables that entail milestones, and defining the instruments they plan to use to do so.

Public support for ODA in Europe is strong (61% of Europeans think that ODA should be increased). And the 0.7% target is among the few goals of development policy that has credibility beyond the narrow development community. Any move away from the 0.7% target may seriously harm public support for development cooperation in the short-term; in the long-term, it could direct public attention away from poverty reduction-focused policies.

ODA is increasingly being used to leverage private finance, and finance GPGs. Although there are strong connections and overlaps between financing for poverty reduction, human rights, democratic governance and GPGs, it is critical to ensure that ODA does not become side-lined in poverty reduction. Although more private resources are needed, this should not be blended with ODA. Instead, other political incentives have to be found, and this could also include a different system of measurement.<sup>13</sup>

### Recommendations

- Any new reporting system should highlight a new definition of ODA as a standalone category.
- The commitment to spend 0.7% of donor GNI on ODA should be reaffirmed and accompanied by sufficient accountability mechanisms and a clear timetable.

### Removing ODA's inappropriate (inflating) elements

In terms of quality, not all that is currently counted as ODA really contributes to development. A reform of the definition of ODA is thus in line with the Busan Partnership agreements that focus on development effectiveness. This would mean removing ODA's inflated components and providing a better definition of concessionality, as well as emphasising that financial resources should be controlled and administered by governments in developing countries.

Debt cancellation,<sup>14</sup> imputed student-costs, in-donor refugee-costs as well as interest payments on loans and other items that do not have development and poverty reduction as their main objective should be excluded<sup>15</sup> from ODA reporting. When loans are repaid, their face value is subtracted from donor ODA and this is indicated as a ‘net’ flow. However, recipient countries pay interest on these loans and this is not deducted from total net ODA figures. If interest repayments were to be subtracted, the net ODA flows would be significantly smaller. In 2012, interest payments amounted to €174 million in Germany alone.<sup>16</sup>

Refugee costs are the costs that donors spend on the support of refugees during the first year of their stay in a donor country. Imputed student costs reflect the calculated (imputed) costs of foreign students in donor countries. Funding refugees and students is important but it should not be counted as development assistance as it does not benefit developing countries directly. Debt cancellation is equally important but does not result in any cash flow or investment in poverty reduction; it is then inconsistent with the current OECD/DAC definition of ODA as a ‘flow’. Furthermore, debt cancellation is often motivated by an attempt by donors to clean up their balance sheets: doing so enables them to remove debts from their books that are unlikely to be repaid. Accordingly, debt cancellation often has more to do with geopolitical or economic rationales than the promotion of development.

<sup>13</sup> Ibid.

<sup>14</sup> All European Governments formally agreed at the United Nations 2002 Monterrey Financing for Development Summit that debt cancellation – though vitally important for development – should be additional to Official Development Assistance (AidWatch report 2006, p. 8).

<sup>15</sup> Germany, one of the EU's largest donors and host to the 2007 G8 Summit, increased its aid by more than 40% in 2005 and has an actual aid level of only 0.20% of GNI (AidWatch Report, 2006, p. 6).

<sup>16</sup> AidWatch report 2013, p. 22. Available at: <http://www.concordeurope.org/275-2013-aidwatch-report/>

### Recommendations

- A new FfSD reporting system should put poverty eradication, the fulfilment of human rights and democratic ownership at its normative centre.
- A new definition of ODA should exclude interest payments on loans, refugee costs in donor countries, imputed student costs and debt cancellation.

### The role of Official Development Assistance in LDCs and MICs

Choosing which countries are eligible to receive ODA is a highly contested issue. It is common sense that ODA should target the extreme poor, but the scenarios in which poor people find themselves differ greatly. Some estimates show that 72% of people living in extreme poverty are located in MICs,<sup>17</sup> while others predict that by 2025 the majority of the poorest people will be living in “fragile, mainly low-income and African states”.<sup>18</sup> The current OECD/DAC recipient list has often been criticised for not including some of the countries that are most in need.<sup>19</sup> Furthermore, the list of the top ten recipient countries of gross ODA in 2011 includes six MICs, such as the emerging donor China, but only four LDCs.<sup>20</sup> At the same time, some LICs with a high percentage of their population living on less than US\$1.25 a day, receive comparatively little ODA under the current allocation model, and count as so-called “aid orphans”.<sup>21</sup>

There are many people living in extreme poverty in MICs (including in some emerging donors) and LICs. ODA is crucial to lifting people out of extreme poverty, both in MICs and LICs, but it has to be targeted to have the maximum impact in different contexts. Extreme poverty is not the same in MICs and LICs. It also varies between countries and regions, and between rural and urban areas. For instance, the ‘depth of poverty’ (the number of people living below the US\$1.25

threshold) varies enormously between different regions. The depth of poverty is highest in Sub-Saharan Africa, the region in the world that has witnessed the lowest progress in reducing extreme poverty over the last few years. In India, however, a lower MIC, some districts remain far below the extreme poverty threshold whereas others have vastly cut extreme poverty rates.<sup>22</sup> The regions in which people are furthest away from leaving extreme poverty have to be targeted the most.

Furthermore, ODA has to fulfil different roles.<sup>23</sup> In LICs, where domestic resources are lowest, ODA should provide a basic minimum where domestic governments are unable to do so. This could mean financing public services, such as strong and cost-free education and health systems. In MICs, ODA has to play a ‘catalytic’ role, leverage larger resources, and support countries in overcoming capacity constraints and NGOs in their watchdog role of ensuring government accountability to the poor and marginalised. By providing support for better tax systems and addressing barriers to participation in society, as well as in health and education systems, ODA can play a game-changing role in both MICs and LICs.<sup>24</sup> In both settings, ODA should serve as an ‘international backstop’ in the fight against extreme poverty.

### Recommendations

- Although MICs should still be eligible for ODA, it should focus on regions with extreme levels of poverty.
- ODA should serve as an ‘international backstop’ to fight extreme poverty in both LICs and MICs.

### An improved definition of concessionality is needed to qualify for ODA

ODA comprises of unrequited grants of funds or technical assistance provided in kind or in the form of ‘concessional’ loans. The current OECD/DAC definition of concessionality, which

<sup>17</sup> Loewe, Markus/Nicole Rippin, Globale Armutsstrukturen im Wandel, 2012, German Development Institute. Available at: <http://www.die-gdi.de/analysen-und-stellungnahmen/article/globale-armutsstrukturen-im-wandel/>

<sup>18</sup> Kharas, Homi/Andrew Rogerson, Horizon 2025, Creative destruction in the aid industry, 2012, Available at: <http://www.odl.org.uk/sites/odi.org.uk/files/odi-assets/publications-opinion-files/7723.pdf>

<sup>19</sup> European Parliament. Modernising ODA in the framework of the post-MDG agenda, 2014, pp. 56-57, Available at: <http://www.europarl.europa.eu/document/activities/cont/201401/20140114ATT77478/20140114ATT77478EN.pdf>

<sup>20</sup> OECD/DAC aid statistics. See: Ibid, p. 33.

<sup>21</sup> KfW, Entwicklungspolitik Kompakt, 2014, p. 21Available at: [https://www.kfw-entwicklungsbank.de/PDF/Download-Center/PDF-Dokumente-Development-Research/2014-01-14\\_EK\\_aid-orphans.pdf](https://www.kfw-entwicklungsbank.de/PDF/Download-Center/PDF-Dokumente-Development-Research/2014-01-14_EK_aid-orphans.pdf)

<sup>22</sup> Development Initiatives: Investments to end poverty. Real money, real choices, real lives. September 2013, p. 21ff. Available at: [http://devinit.org/wp-content/uploads/2013/09/Investments\\_to\\_End\\_Poverty\\_full\\_report.pdf](http://devinit.org/wp-content/uploads/2013/09/Investments_to_End_Poverty_full_report.pdf)

<sup>23</sup> Ibid.

<sup>24</sup> CONCORD AidWatch input to OECD's Development Assistance Committee (DAC) senior level meeting between 3 and 4 March 2014, pp. 4-5. Available at: <http://www.concordeurope.org/301-concord-aidwatch-input-oecd-s-development-assistance-committee-dac-senior-level-meeting-on-3-4-march>.

dates from the 1970s, defines loans with a grant element of 25%, calculated at a discounted rate of 10%, as “concessional in character”.<sup>25</sup> The rationale underlying this definition is that concessional loans include effort on the part of donors as they provide recipients with cheaper money than they would be able to access on capital markets. This is either done by reducing interest rates, allowing longer repayment periods or providing a grace period before loan repayments begin. In most cases, concessionality involves all three elements. However, the current definition of ‘concessional in character’ has been criticised as not fit for purpose, most prominently by Richard Manning, the former OECD/DAC chair.<sup>26</sup> The current discounted rate is well below the market rate at which donors borrow. Hence, the current definition enables donors to provide loans at interest rates above their borrowing cost, and as long as the interest rates on these loans remain below 10%, they still count as concessional. However, these loans do not incur any development effort. Donors such as Germany, France and the European Investment Bank (EIB) have been criticised for taking advantage of this instrument to easily increase their reported ODA. A new FfSD framework hence has to reform the definition of concessionality so that it reflects the rationale of providing accessible and cheaper loans to poorer countries, while remaining fit for purpose even if market conditions change. The ‘discounted rate’ should be replaced with a more appropriate benchmark and be aligned with the interest rates at which donors borrow their funds on capital markets. Furthermore, the new system should deduct interest repayments from net ODA and only count the grant element of subsidised loans (calculated at an appropriate rate) as ODA. This needs to replace the current practice of counting the full face value of the loan. A debt sustainability criterion should also be added to the new system in order to tailor concessionality requirements to the debt situation of borrowing countries. This means introducing higher concessionality for LICs at risk of debt distress.<sup>27</sup>

### Recommendations

- A new FfSD framework must include a reformed definition of concessionality that reflects the rationale of providing accessible and cheaper loans to poorer countries.
- ODA reporting should be done in net terms in order to account for actual flows. Only the grant equivalent of loans should be counted as ODA.
- ODA loans also need a debt sustainability criterion.

### Official Development Assistance and blending with private funds

Blending is an instrument that enables donors to supplement grants or ODA loans with commercial loans and thus leverage larger resources for development. Blending is most commonly used by development finance institutions. Some blending practices have been criticised as lacking transparency, monitoring and accountability, and for supporting sectors and countries where private financing is available. Furthermore, some blending practices have been used to assist companies from donor countries. The new FfSD framework should encourage blending mechanisms that leverage large private resources with the aim of ending poverty. However, whilst establishing strict conditions for using these instruments, blending mechanisms should retain a focus on development and poverty reduction. For example, development outcomes should be the primary criterion for project selection and evaluation. Blended projects, public or private, have to be aligned with the development priorities of national and local governments. Furthermore, blending practices have to ensure that public financing granted for blended funds creates net additional flows and does not come at the expense of ODA subtracted from public financial means that are needed elsewhere, such as from public services and goods. Additionally, transparency, accountability and strict monitoring of blending practices is essential, and this has to be done with a view to avoiding unsustainable debt levels for recipients. Finally, blended funds should only count as ODA within the ODA measurement system if they are provided in the form of grants.<sup>28</sup>

### Recommendations

- Development outcomes should be the primary criterion for project selection and the evaluation of blended projects. ODA blended projects should be accompanied by strong standards to ensure they have an impact on development.
- Only the grant element of blended funds should be counted as ODA within the new FfSD framework.
- Public and private finance provision to developing countries should be in line with commitments made at Busan and support national priorities.

<sup>25</sup> OECD/DAC, Is it ODA?, 2008, p. 1, Available at: <http://www.oecd.org/investment/stats/34086975.pdf>

<sup>26</sup> Financial Times 9 April 2013, <http://www.ft.com/cms/s/0/b3d73884-a056-11e2-88b6-00144feabdc0.html#axzz2sEvVKNQc> (accessed 2 Feb. 2014). For the discussion see: <http://www.cgdev.org/blog/are-oecd-countries-getting-away-murder-aid-figures/>

<sup>27</sup> CONCORD AidWatch input to OECD’s Development Assistance Committee (DAC) senior level meeting between 3 and 4 March 2014, pp. 4-5. Available at: <http://www.concordeurope.org/301-concord-aidwatch-input-oecd-s-development-assistance-committee-dac-senior-level-meeting-on-3-4-march>.

<sup>28</sup> This paragraph is based on the CONCORD AidWatch input to OECD’s Development Assistance Committee (DAC) senior level meeting between 3 and 4 March 2014.

## 3. Count public climate finance and certain other Global Public Goods separately

### New and additional financing

Under Article 4 of the UN Framework Convention on Climate Change (UNFCCC), developed countries committed themselves to provide new and additional financial support to developing countries and assist them to reduce emissions and adapt to a changing climate. This vague commitment has never been further defined, making assessments of the degree to which developed countries have made progress virtually impossible. The Copenhagen promise to increase climate finance to US\$100 billion annually by 2020 could be seen as a first step towards quantifying the Article 4 commitment. However, clarity is missing on a number of questions, such as how finance should be counted by the various forms, channels and instruments. Climate finance has its roots in the UNFCCC Article 4 commitment. This is not only separate from the general ODA commitment, but also includes private as well as official flows, and domestic as well as international flows. It also calls for climate finance to be new and additional. There is thus reason to argue that reporting, monitoring and assessment of cli-

mate finance should take place separately from non-climate ODA financing, even though implementation on the ground should usually be well integrated into a country’s development priorities.

The new global goals are expected to encompass a wide range of topics that are important for global sustainable development and include many more topics than those ‘usually’ on the agenda of international cooperation commitments. Many of these topics can be referred to as GPGs, a concept relating to problems and solutions affecting people across national borders and characterised by the fact that “some of these challenges are likely to spread their costs and benefits across several generations”.<sup>29</sup> Although it is a widely used concept, there is no agreed definition of what a GPG includes or excludes. The UN Working Group on Financing for Sustainable Development refers to ‘global commons’. Global commons are distinguished from climate adaptation/mitigation and the implementation of MDGs (with several parallels and overlaps). As cited in Section 1 of this paper, the “investment requirements for the management of global commons (...) is several tens to hundreds of billion dollars per year.”<sup>30</sup> A new and comprehensive reporting system for sustainable development will have to count the financial flows for GPG or global commons. While it is unclear which (and whether any) of these points will be integrated into the new agenda and who will bear the costs, it should be clear that these points cannot be financed at the expenses of the development of the poorest countries. Financing for GPGs needs to be new and additional and should be provided according to the polluter pays principle. This would be in line with civil society demands concerning



Offshore wind farm, Germany

### Recommendations

- Deliver and report on public climate finance and financing for GPGs in a manner that is both new and additional to ODA.
- Adapt concrete roadmaps with intermediate targets on how to deliver adequate resources in each country and call on actors to act according to the polluter pays principle.

<sup>29</sup> See: Global Public Goods, German Development Institute, 2013. Available at: [http://www.die-gdi.de/uploads/media/DP\\_2.2013.pdf](http://www.die-gdi.de/uploads/media/DP_2.2013.pdf)

<sup>30</sup> UN System Task Team on the Post-2015 UN Development Agenda Working Group on “Financing for sustainable development”, Executive Summary, p. 4.





Massive ice formations at Jökulsárlón glacial lagoon, Iceland

climate finance and would have to be further developed in accordance with the UN debate on FfSD.

Reform the existing system

Climate finance reporting remains deeply unsatisfactory. At present, donor countries report to the OECD/DAC and classify the flows according to two ‘Rio Markers’ for adaptation and mitigation. The Rio Marker 2 is assigned to projects that have adaptation/mitigation as their main objective; the Rio Marker 1 is assigned to projects that have some climate relevance among other objectives; whereas the “Rio Marker” 0 is assigned to projects that have no climate relevance at all. This system is riddled with haziness especially in the large grey area of Rio Marker 1, where the climate relevance of a project can be high or low, thereby creating the risk of over-coding. Developed countries also report on climate finance in their regular reports to the UNFCCC, through the system of national communications and the recently adopted provisions for the biennial (update) reports. These reports face the problem that the volumes provided are aggregated according to sectors and countries, making it impossible to track and verify the financing.

Rather than developing yet another system of climate finance reporting, the existing systems should be reformed and brought together into a comprehensive and coherent reporting system that enables financial flows to be tracked and verified. This would require the following aspects: project-level report-

ing (such as for reporting to the OECD/DAC), including information on the level of the climate-relevance of a financed project (expressed as a percentage), the sector a project addresses (adaptation, mitigation or REDD+<sup>31</sup> ) and the financing instrument (loans, grants or other types). Project-level reporting is a prerequisite for the proper functioning of the UNFCCC’s monitoring, reporting and verification system. Project-level reporting helps build mutual trust between developed countries (that provide financing), and developing countries (that use financing), and it also enhances ambition.<sup>32</sup> While climate finance should be provided in addition to finance provided by countries to meet their 0.7% ODA target, similar statistical reporting issues would also apply to all topics reported in the new system. This would include questions related to the counting of loans that inflate countries’ ODA levels, and climate finance levels in some countries.<sup>33</sup>

Recommendations

- Increase the financial transparency of climate finance by reforming current climate reporting and integrating it as a standalone category within the new reporting system for sustainable development.
- As a minimum, comprehensive climate finance reporting should consist of project-level data provided by a sector project that addresses and provides information on the financing instrument.

<sup>31</sup> REDD+ stands for Reducing Emissions from Deforestation and Forest Degradation.

<sup>32</sup> Experience with the (lack of) reporting of fast start climate finance between 2010 and 2012 led to cases where donor countries listed certain projects in their (voluntary) reports that recipient countries knew existed but had no idea that they were part of the fast start commitment – nor that they were climate-related.

<sup>33</sup> Most countries currently report on climate finance levels based on actual budget allocations. Exceptions include France, the US and Canada that not only include loans at face value but also financing in the form of export credit insurance and other official flows.

4. Measuring private flows: Placing the impact on poverty eradication at the heart of reporting

The development relevance of FDI

Export credits (mostly provided by banks, often with official guarantees) and FDI can potentially have an impact on development and poverty eradication, but there is no a priori way of distinguishing which of these flows contributes to development. According to the UN System Task Team’s Working Group on Financing for Sustainable Development, “global financial assets are estimated at around \$218 trillion.<sup>34</sup> Redirecting a small percentage of this investment toward sustainable development could thus have an enormous impact.”<sup>35</sup> Therefore, institutional investors are a critical source of development financing.

In order to effectively monitor FfSD, private flows should be measured against their contribution to poverty eradication and development. The true value of foreign investment is determined by the types of investments made, the technology and ideas transferred, the goods, services and opportunities offered, and the impact on the local economy. Small and medium enterprises from developing countries may benefit more from FDI that purchases inputs locally and has other linkages to the local economy compared to enclave investments. This is a key issue that should be assessed if private flows are to be properly measured in a new reporting system. An analysis of the current situation shows the importance of such an assessment. For example, development finance institutions have massively increased their private sector portfolios since 2000, but an assessment of investment projects by the World Bank and the EIB in poor countries shows that only a quarter of supported companies came from developing countries.

Recommendations

- Private flows should be measured against their contribution to poverty eradication and development. ODA blended projects should be accompanied by strong standards to ensure they have an impact on development (see Section 2).

Monitor whether private flows are in line with the Busan agreements

In order to monitor whether private flows are in line with the intentions of the Busan agreements, monitoring needs to be undertaken of whether private sector financing is aligned with the development strategies of a particular national government. FDI should support if not strengthen national ownership, rather than undermine it. This requires foreign investment to support the objectives of national industrial or agricultural policy. Ensuring transparency of FDI flows and private actors is vital to this end.

Transparency is also essential to ensure FDI generates income in developing countries; this can be monitored by disclosing taxation information and outflows from developing countries. These are huge. It has been estimated that “of the US\$472 billion in foreign direct investment into developing countries, US\$420 billion flowed out as repatriated profits.”<sup>36</sup>



A fuel-efficient stove made in the Rwanda camp for internally displaced people in North Darfur, Sudan

<sup>34</sup> IMF, World Economic Outlook 2012.

<sup>35</sup> UN System Task Team on the Post-2015 UN Development Agenda Working Group on “Financing for sustainable development”, Executive Summary, p. 1.

<sup>36</sup> Development Initiatives: Investments to end poverty. Real money, real choices, real lives, September 2013, p. 4.





Thanks to a microfinance loan this woman was able to establish a small sewing workshop at home, Gaza

Developing countries’ efforts to finance their own development are often undermined by illicit outward flows of finance by resident foreign firms, as well as by their own people, largely through tax havens. All these negative contributions and outflows would also need to be reflected in a revised reference system by offsetting outflows against inflows.

Company accounts must be fully transparent and measurements need to be put in place through a new FfSD framework. This would help ensure fair tax contributions from transnational companies. Tax authorities, including those in developing countries, need to have the information to track and tackle offenders. Therefore, donor contributions to tackling illicit flows and strengthening tax authorities in developing countries to expand their tax collection capacities should also be taken into account (see Section 5).

Essentially, a new FfSD framework should take private flows into account separately, thereby considering

policy coherence and transparency, without replacing or mixing ODA with private funds. Extended transparency is crucial in order to ensure a credible measurement of private sector contributions. As a recent report by the European Parliament states: “The effective incorporation and monitoring of private resources into the post-2015 agenda will require substantial improvements in the available information about investment and other private resources.”<sup>37</sup>

Recommendations

- Ensure private finance to developing countries supports national priorities.
- Report private finance transparently in the new reporting system as a clearly separate category.

<sup>37</sup> European Parliament, Directorate-General for External Policies 2014: Financing for Development post-2015: Improving the contribution of the private sector. Jesse Griffiths. Available at: <http://www.eurodad.org/files/pdf/5346a6b10e9a4.pdf>

5. Measuring policy coherence for development

Ensuring policy coherence for development

National policies beyond ODA have an impact on development in the countries they aim to assist. This makes policy coherence an important aspect of development cooperation. In order to take policy coherence for development into account, a revised reporting system has to measure positive as well as negative contributions to sustainable development. This goes beyond the traditional measurement of financial flows. It means assessing donor action in policy sectors outside of traditional development cooperation if it is relevant to development. A realistic assessment of the overall coherence of the impact of donor policies on recipient countries is needed to form a comprehensive picture of a donor’s contribution to sustainable development.

Such a monitoring system should include, for example, the impact of policies affecting developing countries’ exports; the impact of the intellectual property regime on access to emerging technologies, such as new medicines; and tax evasion resulting from donor countries’ foreign policy. Furthermore, an analysis needs to be conducted as to whether a ‘price tag’ can be developed for incoherent policies.

A number of initiatives already exist with which to build a policy coherence framework for development. For example, the European Union has developed a PCD Agenda, which comprises 12 areas including migration, decent work, trade, and agriculture and fishery; and it reports regularly on policies in these areas. The weakness here is that it is not really based on an independent assessment; at the same time, it excludes important areas such as tax evasion and capital flight.

Another important initiative is the Commitment to Development Index (CDI), published by the Center for Global Development. The CDI measures rich countries’ contributions to development in seven areas: ODA, trade, investments, security, environment, technology and migration. Although the CDI has a number of weaknesses, for example, it does not cover all of the relevant aspects of development, the concept is a move in the right direction as it acts as an index or scorecard for the assessment and comparison of various countries’ commitments to global responsibilities. The post-2015 discussion provides the opportunity to introduce such

an index, which would have to be established under the leadership of the United Nations.

Recommendations

- A new FfSD reporting system should go beyond the traditional measurement of financial flows and assess donor policies in sectors outside of traditional development cooperation. Only an assessment of the ‘sustainability-friendliness’ of donor policies can provide a comprehensive picture of a donor’s contribution to sustainable development.
- A clear definition of sustainably is needed that integrates the principles of the Busan partnership agreements.



Local volunteers plant trees in a school yard in Goma, Democratic Republic of the Congo





The directors of a local farmers' cooperative standing above a water pumping station near Timbuktu, Mali

## 6. Processes and structures

The United Nations' agenda for Financing for Development (FfD) was developed in the early 2000s. It addresses both ODA and other important issues such as global trade, debt relief, domestic resource mobilisation and the mobilisation of private international capital flows, including FDI. As part of the on-going post-2015 process, the UN is searching for a means to finance the new sustainable development framework. This broad development process requires substantial and sufficient funding; far more means than development assistance can deliver, and far more funds than current global ODA is able to provide. At the same time, several stakeholders including governments, CSOs, and the private sector have a role to play in the agenda, and the responsibility of contributing towards it. Provide an inclusive and transparent reform process. In short the new framework should:

- Promote discussion in representative and legitimate institutions.
- Achieve an accountable and transparent reference framework.
- Include new partners.
- Overcome the complexity and diversity of the current structure.

One challenge to effective development cooperation is the duplicative nature of the current aid-effectiveness process at the level of the OECD and the UN. The OECD-based

process grew out of the DAC. The members of this forum have adopted a number of aid harmonisation policies (such as untying aid to LDCs) and promote result-oriented actions, inter alia, through committee monitoring and peer review mechanisms.

An example of the OECD and the UN working together is the Global Partnership for Effective Development Cooperation, which was created as a platform for dialogue in Busan in 2011. OECD/DAC and UNDP serve as its secretariat and the Global Partnership is managed between meetings by a multi-stakeholder steering committee, currently chaired by ministers from Indonesia, Nigeria and the UK. The Netherlands has shown an interest in becoming one of the co-chairs in the near future. The Global Partnership collaborates with the UN Development Cooperation Forum, the Development Working Group of the G20 and the UN-led process for creating a post-2015 global development agenda.

In 2005, the Development Cooperation Forum (DCF) was created at the level of the United Nations to review and strengthen the implementation of commitments made in the Millennium Declaration. The DCF is based on universal participation; as such, it includes non-state stakeholders, but it explicitly remains a discussion forum. Nevertheless, it could build political momentum around aid-effectiveness proposals, such as strengthening mutual accountability. It has the potential to become the key universal platform for global dialogue on development cooperation trends, co-

herence and effectiveness. The growing number of southern donors and increasingly diverse actors in development cooperation could benefit from such an inclusive global platform to discuss experiences. However, the DCF needs to be strengthened in order to become more effective and fulfil its goals.

The United Nations and other international and national institutions should therefore support the efforts of the DCF to monitor the new FfD framework, such as regarding data collection and processing. Ideally, the OECD-led monitoring-process should be included in the UN pro-cess, as it would benefit from the legitimacy provided by the United Nations and this would also improve its efficiency.

Another advantage of a UN-led process would be the inclusion of new actors in the field of development finance. The existing OECD framework currently ignores the financial and political leverage that new actors, such as the BRICS, have on the global field.

A critical priority for a post-2015 framework should be increasing policy coherence across the various fora for development cooperation. The post-2015 agenda should also set rules for guiding financial investment, taxation, debt and financial systems, and all parts of aid flows. Renewed political commitment is essential for the implementation of agreed goals and targets. This has been absent in recent years.

Other stakeholders such as CSOs and the private sector also need to be included in the post-2015 framework. Participation and ownership of these processes by all of the actors involved is central to the effectiveness of development.

### Recommendations

- The new FfSD reporting system should establish transparent reporting mechanisms that hold governments to account, include new partners and ensure the effective participation of developing countries in the design and implementation of the system.
- The new FfSD reporting system should support and strengthen the efforts of the DCF to monitor the new FfD framework.



Clean drinking water runs from a communal water tap in Ndombil, Senegal





## VENRO

VENRO is the German umbrella organisation for non-governmental organisations (NGOs) focusing on development policy. It consists of around 120 organisations from private and church-related development cooperation, humanitarian aid, and development policy education, public relations and advocacy.

VENRO represents the interests of NGOs focusing on development and humanitarian issues at the political level, raises public awareness of development policy and develops standards for quality and transparency.

[www.venro.org](http://www.venro.org)



## PARTOS

Partos is the Dutch association for NGOs working in International Development. The association represents 120 Dutch development organisations that work in the field of poverty reduction, humanitarian aid, human rights and sustainable development. They are active in development- and middle income countries, often working with local partner organisations. Most of the organisations are also active in the Netherlands and within the EU, where they focus on knowledge development and policy advice.

[www.partos.nl](http://www.partos.nl)



## ‘Your voice against poverty – development needs participation’

The VENRO project ‘Your voice against poverty’ encourages debate about sustainable development. The aim of the project is to develop a sustainable understanding of development together with other social actors and anchor this understanding within politics and society. The project organises nationwide campaigns that are particularly intended to motivate young people to actively support the implementation of development goals. Further important aspects of the VENRO project include providing information and promoting dialogue.

‘Your voice against poverty’ is the German platform of the international alliance ‘Global Call to Action Against Poverty’ (GCAP). This alliance consists of charities and other non-profit organisations, but also celebrities and millions of people in more than 100 countries who are campaigning for an end to poverty.

[www.deine-stimme-gegen-armut.de](http://www.deine-stimme-gegen-armut.de)

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