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Finance for Development: what's at stake?

Background

Government leaders, ministers and representatives are gathering in Addis Ababa, Ethiopia from 13-16 July for the third UN Financing for Development Conference.

Addis hasn't had the attention it deserves. The UN's financing for development process should establish the systems and mechanisms through which the global community will finance poverty eradication and sustainable development – whether through aid, tax, debt relief, private investments or other innovative means. Addis is particularly important because it will set out how the global community will raise the money needed to finance the Sustainable Development Goals – a set of universal global goals for eradicating poverty and protecting the planet which are due to be agreed in New York in September.

The potential for Addis is huge. It could help release billions of dollars to build a fairer, more prosperous and safer world for us all. It will also set the bar for success at the Sustainable Development Goals Summit and the Climate Change Conference in Paris at the end of 2015.

The need could hardly be greater. One billion people – approximately one in seven of us - live in extreme poverty.ⁱ Extreme inequality is spiralling out of control, both within countries and especially between developed and developing countries. Over the 15 years prior to 2010 (for which we have latest figures), the average GDP per capita for those living in rich countries has stood between \$US 30-35, 000 per year, while for those who live in India, South Asia and Sub-Saharan Africa, it has stagnated at a constant US\$ 2,000 GDP per capita, per year. It is around US\$5000 for China.ⁱⁱ Meanwhile climate change is already hitting the world's poorest regions hard.

The big challenge for Addis is to rebalance the skewed international finance rules that are costing the developing world billions of dollars every year – money that could be invested in overcoming poverty and inequality. The rules governing tax, private investments, aid and climate change are stacked in favor of rich governments and vested interests; they have helped create a situation where developing countries lose more money every year than they gain. Since 2008, it has been estimated that for every US\$1 dollar developing countries gain (through foreign direct investment, remittances, aid etc.), they lose around US\$2 dollars (especially in illicit financial flows and debt repayments)ⁱⁱⁱ.

Unfortunately with countries on all sides negotiating for their own short term political and commercial interests, Addis is unlikely to deliver the necessary changes. Indeed, the conference risks doing more for the global business community's bottom line than it does for the world's poorest people.

Up until now, negotiations on the Addis 'outcome document' have been marred by a series of disputes between the developed and the developing world. At the heart of the North-

South clash is each side's interpretation of rich countries' international commitments to poorer countries. Rich countries are keen to play down their past commitments on aid while demanding that emerging economies such as India bear a greater share of the cost of international development.

Developing countries want rich countries to deliver on past aid promises. They are demanding action to clamp down on the corporate tax dodgers who are cheating poor nations out of billions of dollars in revenue every year - a call which is being vigorously resisted by rich countries. Meanwhile all countries are set to give the green light for an expanded role for private finance in development without the checks and balances which are needed to ensure private initiatives deliver for poor people.

At the time of writing, negotiations on the final text for the Addis outcome document are stuck in deadlock over the key issue of tax. The most recent proposed text is entitled the 'Addis Action Agenda' instead of the Addis Accord (so as to remove all hints of legal force of the document). This text has been rejected so "nothing is agreed until it is all agreed" and negotiations are likely to continue right up the wire in Addis.

Outside the formal negotiations governments and international institutions are expected to announce funding commitments towards a variety of development initiatives. These initiatives may make a positive contribution in some areas, but are no substitute for the fundamental changes to the global financial architecture this Summit so desperately needs to deliver.

Governments have a mountain to climb if they are to agree anything in Addis – let alone anything worthwhile. However with no final text agreed there is still hope that something worthwhile can be plucked from Addis. This will require bold and courageous international leadership - sorely lacking from the developed world whose leaders are staying away from the talks. Maybe it is time for governments from some of the world's emerging economies such as South Africa, India or Brazil to step forward to broker new rules and standards on development finance to which all can subscribe?

Big issues in Addis

Tax

Reforming the international tax system and clamping down on corporate tax dodgers could release billions of dollars that could be invested in tackling poverty and inequality and in delivering the Sustainable Development Goals.

Estimates of how much tax revenue developing countries lose because of corporate tax avoidance schemes are hard to come by because of a lack of available data and opaque corporate reporting. A recent report from UNCTAD found that developing countries lose around US\$100bn in tax revenues each year as a result of corporate tax avoidance schemes that route investments through tax havens.^{iv} This US\$100bn does not include the full set of tax avoidance schemes used by multinational companies nor does it include the estimated US\$138bn per year that developing countries lose because they give away generous tax incentives to multinational companies^v.

Corporate tax avoidance is not just a problem for developing countries. Publics and politicians across the globe have woken up to the scale of corporate tax abuse in recent years following a number of well reported cases involving global brands such as Apple and Starbucks.

The G20 has recognized that the international corporate tax system is out dated and requires reform. The reform process is being led by the Organisation for Economic Cooperation and Development (OECD) through the Base Erosion and Profit Shifting (BEPS) Action Plan and is due for completion at the end of 2015.

The BEPS project will do little to help developing countries. The BEPS negotiations are dominated by rich countries and corporations and the majority of developing countries - two-thirds of the world's governments - have no formal role in the negotiating process. As a result, many of the tax loopholes that matter most to developing nations are not on the agenda. For example, BEPS gives scant attention to the agribusiness, telecommunications and extractives sectors that are central to developing economies. Neither will it ensure that multinational companies pay taxes where they do business (which would benefit developing nations) rather than where they base their headquarters (which largely benefits the developed world).

The G77 group of developing countries, backed by Oxfam and others, have been calling for the establishment of an UN inter-governmental tax body as an outcome of Addis. This body would include all countries as equal members and have the mandate and resources to reform international corporate taxation to prevent tax evasion and avoidance and harmful tax competition, and to ensure tax cooperation between governments. To deliver this the G77 is calling for the current UN Committee of Experts on Cooperation in Tax Matters to be upgraded to an UN Commission with political representation, and increased financial support. This has been blocked by the US, with support from the EU, Australia and Canada. The most they have been willing to offer is three additional meeting days for the UN Tax Committee, with no guarantees that they will pick up the tab. With the G77 standing firm on their demand there is, at the time of writing, a stalemate.

This stalemate will have to be broken for an agreement on the broader agenda to be reached in Addis. There are three ways this could play out. First, before delegates reach Addis, the rich countries blocking calls for an intergovernmental tax body could agree to a strengthened role for the UN in setting global norms on international tax cooperation – the effectiveness of this approach depends on exactly what is agreed. Second, ahead of Addis, the G77 countries may capitulate in the interests of getting an agreement in Addis and securing concessions elsewhere. Or third, the battle for the intergovernmental tax body will be taken to Addis for political level negotiations.

What is certain is that developing countries will not raise the resources they need to overcome poverty and deliver the SDGs unless they have an equal say in reforms of the international tax system so that it meets their needs too. The status quo cannot continue.

Private Finance

Rich countries are keen to see an expanded role for private finance in Addis and the G77 group of developing countries seem willing to play along.

For rich countries, private finance offers a convenient way of plugging the huge funding gaps linked to the Sustainable Development Goals and a way of side stepping their decade's old promise to increase public funding for official development aid. For many countries, rich and poor alike, there is also an, often unsubstantiated belief, that the private sector is simply more effective than public bodies. Across the board insufficient attention has been paid to the checks and balances needed to ensure private finance delivers for poor people.

There is also pressure from the business community. In a submission led by the International Chamber of Commerce (ICC) responding to the draft negotiating text for the Addis Summit, the ICC pushed for the insertion of new language to promote 'blended finance' (public and private) and a bigger role for private finance, including 'using limited public finance to mobilize private'.

There is no doubt that private finance is needed and that it can play a critical role in some areas that require large-scale infrastructure projects, such as roads, railways, clean power and telecommunications. However, too often, private finance is mobilised in murky, unaccountable ways, leading to hidden public and user debt burdens and environmental, social and human rights abuses. There is rapidly growing evidence showing how long-term contractual arrangements in which the private sector is tasked with the delivery of a public service or an asset are a very expensive and risky method of financing. If they fail, public-private partnerships (PPPs) can end up 'privatizing benefits while socializing losses', when

the public sector has to rescue or bail-out a failing private service provider. Oxfam research into 'mega-PPPs' in agriculture similarly found them likely to skew the benefits of investments towards the privileged and powerful, while leaving the risks to fall to the poorest and most vulnerable^{vi}.

Despite this, there has been a rapid expansion of aid being used in partnership with private sector investment without the required level of debate on the strong accountability mechanisms needed to ensure that the aid is stimulating the private sector's contributions to sustainable development. By the end of 2015, the amount of aid flowing to the private sector is expected to exceed US\$100bn - equivalent to almost two thirds of overseas development aid^{vii}.

More fundamentally private investors are simply not interested in investing in areas unlikely to yield a profit. For example, private health and education services benefit the richest first and foremost, leaving people in poverty behind. When healthcare is sold through the private sector for instance, quality care and medicines are often available only to those who can afford them, while poor people may be forced to rely on low-quality medicines or unqualified care. Good quality public health and education services that are free at the point-of-use and available to all can be powerful equalizers, enhancing the economic prospects of the majority while protecting those who are most vulnerable from impoverishment.

At the same time, prioritizing the private sector can see public services eroded as financial and human resources are diverted from the public to the private system. Oxfam found that a new PPP hospital in Lesotho cost 51 per cent of the total health budget for the entire country leaving many rural areas dangerously under-resourced^{viii}.

Against this backdrop considerable care and caution is needed around the use of private finance for development that has so far been absent in negotiations on the draft text. Governments - north and south – need to be awake to the potential hazards as well as the possible opportunities for private finance. They must ensure the Addis Declaration puts the proper checks and balances in place so that no more public funds are squandered on public private initiatives which will do little for the world's poor or make their lives even harder.

Overseas Development Aid

Overseas Development Aid (ODA) will continue to be a significant and influential source of development finance for the foreseeable future. Partly because it will take time to mobilize alternative forms of finance such as tax revenues. Aid is still larger than any other external resource flow in 43 countries - most of them in sub-Saharan Africa - which is home to over 220 million people living on less than US\$1.25 a day^{ix}, and where over 20 per cent of the population is going hungry.

Whilst there is always room for improvement, good quality aid not only saves lives but is indispensable in unlocking poor countries and poor people's ability to work their own way out of poverty. For example, in Mozambique, aid spending on healthcare has helped to reduce the number of children dying before their fifth birthday by 20 percent over the last decade^x. In the aftermath of cyclones and floods in 2000 which killed 800 people, displaced half a million more and left more than a million people without an income, international aid has helped Mozambique put in place a nationwide master-plan which will save lives and protect livelihoods in the future^{xi}.

In the negotiations for Addis, rich countries have been trying to weaken the draft text around their decades' old aid promise to spend 0.7 per cent of their gross national income on ODA. Only the EU has collectively re-committed to this target with a concrete timetable by 2030 (15 years later than their last deadline). There has been no universal re-commitment to this target or the introduction of concrete timelines to reach these commitments.

This is a significant blow. The average aid spend of countries in the Organisation for Economic Cooperation and Development (OECD) currently stands at just 0.29 per cent of gross national income with only five countries - Denmark, Luxembourg, Norway, Sweden

and the UK meeting the 0.7 per cent target. This year some donors have reduced their aid contributions further with the biggest declines in aid seen from Australia, Canada, France, Japan, Poland, Portugal and Spain. Yet, if all OECD donors delivered on this commitment this would raise an additional US\$250bn a year, bringing their total aid contribution to just short of US\$400bn per year^{xii}.

While side-stepping their own aid commitments rich countries are calling on emerging economies to contribute more in international aid. It's unlikely these countries, which have large populations of people living in poverty, will be able to make up the difference between what they promised and what they pay. While the levels of south-south aid has increased over the past 15 years - with this accounting for US\$16.1bn–US\$19bn of aid in 2011^{xiii} – this is still only equivalent to one-eighth of total aid from OECD donors.

It's not just about the quantity of aid, quality matters too. To increase the effectiveness of all forms of public (and private) finance, action is needed in Addis to accelerate progress toward meeting existing development effectiveness standards. These standards include commitments on transparency and accountability for all development actors. Of paramount importance is that developing country governments have ownership over (and are accountable for) their development agendas.

Unfortunately the current Addis text is weak on commitments aimed at enhancing the quality of aid and development cooperation. On ODA specifically, there are no binding commitments in the draft text that would commit countries to focus more of their ODA in the world's poorest countries. Donor countries spent just 0.09 per cent of their collective gross national income on aid to Least Developed Countries - the majority of which are in sub-Saharan Africa. The draft text only 'encourages' ODA providers to consider setting a target to provide at least 0.20 per cent of their national income to Least Developed Countries, rather than setting a commitment to achieve that target.

Climate Finance

Rich countries are keen to keep any new commitments on climate finance off the agenda in Addis and developing countries have not stood in their way.

For many developing countries, climate change already presents huge additional costs that were not taken into account when aid targets were set. For example, Oxfam estimates that sub-Saharan African countries are already spending around US\$5bn of their own resources on climate change adaptation - for many countries this is far more than the amount they have received in international climate finance^{xiv}. Ethiopia spends approximately twice on the amount on adaptation from its own budget each year than it received in international climate finance assistance during the 'Fast Start Finance' period - the three years between 2010 and 2012 during which rich countries committed US\$30 billion to help poor countries adapt to a changing climate and curb their emissions^{xv}.

While it's welcome that the draft Addis text restates existing commitments on climate finance made within the UN Climate body, setting a good precedent for the climate negotiations later this year, there are still no guarantees that existing aid will be used to meet these commitments. Currently 17 per cent of overseas development aid is used for climate finance with increasing amounts of aid diverted to meet climate needs. The Addis text should include guarantees that as climate finance rises; overall aid should also increase, at least at the same rate. That would be a first step towards ending the diversion of aid to climate finance, and making the provision of climate finance additional to existing aid promises. Agreement at the Addis Conference on this point would be an important trust-building measure ahead of the climate negotiations later this year at the UNFCCC meeting in Paris.

New Development Initiatives

Throughout the Addis Conference, governments and international agencies, such as the World Bank, will be announcing a series of new development initiatives. Key initiatives include the World Bank Global Infrastructure Facility that has been designed to help address

the infrastructure financing gap and build a global pipeline of infrastructure investments. A new Global Financing Facility for Every Women, Every Child is also set to be announced which will accelerate efforts to end preventable new-born, child, adolescent and maternal deaths and improve the health and quality of life of women, adolescents and children. It is also expected that a group of governments including the US, UK, Germany and the Netherlands will announce the Addis Tax initiative, which aims to strengthen the capacity of developing countries' tax authorities. The full list of initiatives likely to be launched in Addis are listed here: <http://www.un.org/esa/ffd/ffd3/commitments.html>

These initiatives are welcome if they provide new and additional resources, guarantee sustainable and equitable development and contribute to ending poverty. Any initiative where the balance of the benefit falls in favour of rich governments and commercial interests is not a welcome contribution. Moreover, these initiatives can never be a substitute for the fundamental changes to the financial architecture needed in Addis.

An Alternative Vision for Addis

There is a huge amount of work to do if the Finance for Development Meeting is going to put the commitments in place, which are needed to end extreme poverty and reduce inequality. Government representatives must find the vision and leadership to deliver action on tax, aid and standards for private finance in Addis. If they achieve this they will help lift millions out of poverty and create the political momentum needed for success at the UN Sustainable Development Goals Summit in September and the UN Climate Change Conference at the end of the year.

Oxfam is calling for the following steps to be taken to ensure that financing for development is fair for all:

- All countries must work together to clamp down on the multinational companies that are cheating governments out of billions of dollars in tax revenues every year. Governments must agree to create an intergovernmental body for cooperation in tax matters that includes all countries, developed and developing, on an equal footing in decision making; and broaden the scope of future tax negotiations to address tax dodging in developing countries.
- Rich countries must re-commit to delivering 0.7 per cent of their national income in aid with 50 per cent of this aid targeted at the world's poorest countries within the next five years. They must also ensure climate finance contributions are additional to overseas development aid.
- Governments must stop the headlong rush towards the privatization of development. Private finance is needed but only if it delivers sustainable development and poverty reduction. Overseas aid money should not be wasted on private projects that result in dubious outcomes for the poorest and most vulnerable people. And private finance must not be promoted as a substitute for overseas aid spending.

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ⁱ EURODAD <http://www.eurodad.org/files/pdf/55379eda24d40.pdf>

ⁱⁱ PPP 2005, World Bank WDI: <http://data.worldbank.org/indicator/PA.NUS.PPP.05>

ⁱⁱⁱ EURODAD: <http://www.eurodad.org/Entries/view/1546318/2014/12/17/2-lost-for-every-1-dollar-gained-the-single-fact-that-shows-how-the-global-financial-system-fails-developing-countries>

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