EUROPEAN COMMISSION

Brussels, 9.7.2012
SWD(2012) 199 final

VOL 1

COMMISSION STAFF WORKING DOCUMENT

EU Accountability Report 2012 on Financing for Development Review of progress of the EU and its Member States

Accompanying the document

COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT, THE COUNCIL, THE EUROPEAN ECONOMIC AND SOCIAL COMMITTEE AND THE COMMITTEE OF THE REGIONS

Improving EU support to developing countries in mobilising Financing for Development.

Recommendations based on the 2012 EU Accountability Report on Financing for Development.

{COM(2012) 366 final}

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LIST OF ACRONYMS	
A2II	Access to Insurance Initiative
ACP	Africa, Caribbean and Pacific
ADA	Austrian Development Agency
ADB	Asian Development Bank
ADF	Asian Development Fund
AfDB	African Development Bank
AFI	Alliance for Financial Inclusion
AfT	Aid for Trade
AMC	Advance Market Commitment
ASEAN	Association of Southeast Asian Nations
AT	Austria
ATAF	Africa Tax Administration Forum
B4D	Business for Development
BE	Belgium
BIO	Belgian Investment Company for Developing Countries
BMI/SBI	Belgian Corporation for International Investment
BMZ	Germany's Federal Ministry for Economic Cooperation and Development
BPC	Building Productive Capacity
CBD	Convention on Biological Diversity
CDE	Centre for the Development of Enterprise
CDM	Clean Development Mechanism
CER	Certified Emission Reduction
CGAP	Consultative Group to Assist the Poor
CIAT	Inter-American Centre of Tax Administrations
COP	Conference of the Parties to the CBD
CPA	Country Programmable Aid
CPSS	Committee on Payment and Settlement Systems
CRS	Creditor Reporting System
CRW	IDA Crisis Window
CSO	Civil Society Organisation
CSR	Corporate Social Responsibility
CZ	Czech Republic
DAC	Development Assistance Committee
DDA	Doha Development Agenda
DE	Germany
DFI	Development Financial Institutions
DFID	Department for International Development - UK
DK	Denmark
DMF	World Bank Debt Management Facilitaty for Low Income Countries
DMFAS	Debt Management and Financial Analysis System from United Nations UNCTAD
DTC	Double Taxation Convention
DTIS	Diagnostic Trade Integration Study
EAC	East African Community
EBRD	European Bank for Reconstruction and Development
ECB	European Central Bank
EDF	European Development Fund

EDFI	European Development Finance Institution
EGI	Ethical Globalisation Initiative
EIB	European Investment Bank
EIF	Enhanced Integrated Framework
EITI	Extractive Industries Transparency Initiative
EPA	Economic Partnership Agreement
ES	Spain
ETS	EU Emission Trading System
EU	European Union
EUR	Euro
FAC	Foreign Affairs Council
FAO	Food and Agriculture Organisation
FAT	Financial Activities Tax
FDI	Foreign Direct Investment
FI	Finland
FIRST	Financial Sector Reform and Strengthening Initiative
FLEGT	Forest Law Enforcement, Governance and Trade
FR	France
FTA	Free Trade Agreement
FTT	Financial Transaction Tax
G20	Group of Twenty (G8 countries plus Argentina, Australia, Brazil, China, EU, India, Indonesia, Mexico, Saudi Arabia, South Africa, South Korea, and Turkey)
G8	Group of Eight (i.e. Canada, France, Germany, Italy, Japan, Russia, United Kingdom and USA, plus EU)
GAVI	Global Alliance for Vaccines and Immunisation
GDP	Gross Domestic Product
GEEREF	Global Energy Efficiency and Renewable Energy Fund
GEF	Global Environment Facility
GIZ	Gesellschaft für Internationale Zusammenarbeit
GNI	Gross National Income
HDI	Human Development Index
HIPC	Highly Indebted Poor Countries
HLF	High Level Forum
HU	Hungary
IBRD	International Bank for Reconstruction and Development
IDB	Inter-American Development Bank
IE	Ireland
IF	EIB Investment Facility
IFAD	International Fund for Agricultural Development
IFCA	Investment Facility for Central Asia
IFFIm	International Financial Facility for Immunisation
IFI	International Financial Institutions
ILO	International Labour Organisation
IMF	International Monetary Fund
IPD	Innovative Partnerships for Development
IPSAS	International Public Sector Accounting Standards
IT	Italy

ITC	International Tax Compact
ITF	EU–Africa Infrastructure Trust Fund
ITRS	International Transactions Reporting System
KfW	Kreditanstalt für Wiederaufbau
LAIF	Latin America Investment Facility
LDC	Least Developed Countries
LT	Lithuania
LIC	Low Income Countries (LDC+OLIC)
LMIC	Lower Middle Income Countries
LU	Luxembourg
LV	Latvia
MDG	Millennium Development Goals
MDRI	Multilateral Debt Relief Initiative
MIGA	Multilateral Investment Guarantee Agency
MoU	Memorandum of Understanding
MS	Member States
MSME	Micro, Small and Medium Enterprises
MT	Malta
MTO	Money Transfer Organisation
NGO	Non Governmental Organisation
NIF	Neighbourhood Investment Facility
NL	Netherlands
NORAD	Norwegian Agency for Development Cooperation
ODA	Official Development Assistance
OECD	Organisation for Economic Cooperation and Development
OECS	Organisation of Eastern Caribbean States
OJ	Official Journal
OLIC	Other Low Income Countries
PCD	Policy Coherence for Development
PEFA	Public Expenditure and Financial Accountability
PEM	Public Expenditure Management
PFM	Public Financial Management
PPP	Private Public Partnerships
PSD	Payment Services Directive
PT	Portugal
REDD and REDD+	Reducing Emissions from Deforestation and Forest Degradation. REDD+ goes beyond deforestation and forest degradation, and includes the role of conservation, sustainable management of forests and enhancement of forest carbon stocks.
REGMIFA	Regional Micro Small and Medium-Sized Enterprises Investment Fund for Sub-Saharan Africa
REPARIS	The Road to Europe: Programme of Accounting Reform and Institutional Strengthening
ROAP	Regional Office for Asia and the Pacific
ROSC	Report on the Observance of Standards and Codes
SE	Sweden
SME	Small and medium-sized enterprises
SWC	System-Wide Coherence Reform

TA	Technical Assistance
TCX	The Currency Exchange
TD	Trade Development
TEEB	The Economics of Ecosystems and Biodiversity Study
TIEA	Tax Information Exchange Agreements
TNA	Trade Needs Assessment
TPR	Trade Policy Regulations
TRA	Trade Related Assistance
TRAdj	Trade Related Adjustment
TRI	Trade Related Infrastructure
UK	United Kingdom
UMIC	Upper Middle Income Countries
UN	United Nations
UNCCD	United Nations Convention to Combat Desertification
UNCTAD	United Nations Conference on Trade and Development
UNEP	United Nations Environment Programme
UNFCCC	United Nations Convention on Climate Change
UNITAID	International Drug Purchasing Facility
US or USA	United States of America
USD	United States Dollar
WB	World Bank
WBIF	Western Balkans Investment Framework
WFP	World Food Programme
WTO	World Trade Organisation

EXECUTIVE SUMMARY

This Staff Working Document is the tenth in a series of annual progress reports drafted since 2003 for the purpose of assessing where the EU and its Member States stand in relation to their common commitments on financing for development, including aid effectiveness, aid for trade, fast-start climate finance and good governance in tax matters.

The EU and its Member States are making substantial efforts to achieve international targets on the **quantity and quality of Official Development Assistance (ODA)**, as enshrined in the Millennium and Paris Declarations. Collectively the EU is not only the world's largest provider of ODA in value, but its ODA/GNI ratio is more than double those of Japan and the USA. The EU has also made a greater contribution to the achievement of the aid effectiveness agenda than any other bilateral donor. The EU is keeping to its commitments on fast-start climate finance, has achieved the goal of providing ODA to LDCs equivalent to 0.15 % of GNI, and has increased EU ODA to Sub-Saharan Africa by around EUR 5.5 billion in real terms over the period 2004-2011.

While the direction of change is positive, the pace of implementation is modest. This report shows in fact that the EU and its Member States missed their collective 2010 ODA/GNI target of 0.56%, and in 2011 the ODA/GNI ratio declined from 0.44% to 0.42%, while aid volumes fell by about EUR 400 million. The EU scaling-up process has been uneven, with asymmetric efforts. Member States that do not contribute fairly to the burden-sharing effort endanger the performance of the EU as a whole and substantially increase the risk of failure for future ODA targets.

The projections confirm that Member States do not plan to make the necessary increases under the current tight budget conditions. At today's pace, the 0.7% target will not be achieved by 2015 as planned. Based on the projections provided by Member States and/or estimates prepared using their 2006-2011 compound annual growth rate, the EU27 ODA is expected to increase to 0.45% by 2015. Considering the expected GNI growth rate till 2015, reaching the 0.7% ODA/GNI target would require the EU and its Member States to dramatically step up efforts and almost double their current ODA in nominal terms. At the current pace, there is a delay equivalent to about 25 years on the path to 0.7%, as ODA is projected to increase at an annual rate of 0.01% of GNI.

Progress on **improving aid effectiveness** has also been modest. As noted by the OECD DAC Secretariat in its analysis of the 2011 Paris Declaration Survey's findings, these were 'sobering' for all donors, including the EU and its Member States. As a whole, the EU met only one of the twelve indicators relating to donor performance (i.e. coordinated technical cooperation). However, OECD DAC also concluded that 'considerable progress has been made towards many of the remaining targets'. Most of the overall progress among bilateral donors worldwide was made possible by the performance of EU Member States, which was generally above the 'all donors' average, showing a significant commitment to achievement of the goals of the Paris Declaration under difficult global conditions.

The Monterrey Consensus and the Doha Declaration recognise the importance of other financial flows besides ODA. If sustainable progress towards the MDGs is to be achieved, the financing discussion should concentrate on **increasing developing countries' overall revenue base for development**. The EU can effectively assist its partners in increasing their domestic resources for development in line with the principles of good governance in tax matters (transparency, exchange of information and fair tax competition). Enhanced international cooperation in tax matters in particular will not only increase domestic revenues in developing countries by reducing tax evasion, it will also help to address money laundering, corruption and the financing of terrorism.

As noted in recent EU policy statements on budget support, and on increasing the impact of EU development policy, fair and transparent **tax systems** are central to fostering citizenship and state-building, leading to enhanced domestic accountability and political participation. Member States are increasingly focusing on the issue of taxation and development. The EU and most Member States undertook new initiatives in 2011 to support tax reforms in developing countries. Many Member States delivered training indirectly by funding specialised programmes managed by international organisations (such as the IMF, OECD, etc.). Other support focused on tax policy reforms and related legislation.

The EU has consistently supported developing countries in **using trade as a tool for development**. Since 2007, the EU and its Member States have been driving the global Aid for Trade efforts, confirming again in 2010 the **EU's position as collectively the largest provider of AfT in the world**. Indeed, the EU and its Member States together accounted for around 32% of total AfT flows in 2010, reaching more than EUR 10.7 billion (EUR 8.2 billion from Member States and EUR 2.5 billion from the EU), an increase of 4.2% in comparison with 2009. The EU and its Member States have exceeded their 2010 EUR 2 billion target for Trade Related Assistance (TRA) since 2008. However, for the first time since 2005 there has been a decrease of TRA, in 2010. Total TRA in 2010 reached EUR 2.6 billion, compared to EUR 2.8 billion in 2009 (or -8% in 2010, as compared to +24% in 2009).

The Commission and the EU Member States are steadfastly committed to providing debt relief and are increasingly prioritising the prevention of unsustainable debt. In 2011, the EU provided debt relief through participation in the World Bank's Debt Relief Trust Fund (DRTF) to fund the participation of the African Development Bank in the HIPC Initiative. By the end of 2011, 32 countries had reached HIPC completion point, with another seven sub-Saharan countries potentially eligible.

The 2011 Commission Staff Working Paper on 'Migration and development' provides further analysis of the achievements since 2005 in the area of **remittances**, and identifies some remaining challenges, including capacity building to support partner countries interested in designing regulatory frameworks and in promoting financial literacy, new technologies and access to credits to stimulate productive investment and job creation. According to the latest estimations of the World Bank, global remittance flows to developing countries increased by 12.1% in 2011, and are expected to grow at a rate of 7-8 % annually to reach EUR 333.5 billion by 2014. At EU level, total EU27 remittance outflows amounted to EUR 31.2 billion in 2010, a 3% increase from the previous year (EUR 30.4 billion in 2009), most of which are sent to developing countries.

At EU level, **remittance services have been made cheaper, more transparent, more competitive and more reliable**. In particular, the transposition of the 2007 Payment Services Directive (PSD) into the national legislation of a majority of EU Member States has contributed to increased transparency in the provision of payment services, including the remittance market. Moreover, several EU Member States (including France, Germany, Italy, the Netherlands and the United Kingdom) have set up their own remittance price comparison websites on costs and quality of services.

In the current context of financial crisis and budgetary austerity, discussions on innovative financing mechanisms have gained a new resonance, both within the EU and at global level. A good illustration of this growing interest in innovative financing mechanisms is the G20's formal agreement for the first time to support innovative financing for development and climate change and to move forward by using a menu of options. Twelve Member States are currently using or are planning to use one or more of the existing innovative financing mechanisms to raise funds for development and/or climate action. Examples of these mechanisms are the International Finance Facility for Immunisation (IFFIm), the Advance Market Commitments (AMC), the air ticket levy, and the EU Emissions Trading System. Following on from a Commission proposal, the EU is currently discussing the possible establishment of a Financial Transaction Tax as a new own resource for the EU budget. While the revenues raised would not be earmarked for development *per se*, they could nonetheless facilitate Member States' efforts to mobilise funding required for meeting aid targets and tackling other global challenges.

Recent EU policy statements have given added emphasis to inclusive and sustainable economic growth as a crucial element contributing to long-term poverty reduction and also leading to wealth and job creation. The EU and its Member States support programmes to achieve these goals by **improving competitiveness of local private sectors**, enhancing the investment climate, promoting MSMEs, facilitating access to finance and encouraging public-private partnerships. Blending mechanisms can leverage additional financial resources for development at a time when the prospects for increased foreign investment look uncertain. The Busan meeting put forward a framework to enable the participation of the private sector in the design and implementation of development policies. Furthermore, Corporate Social Responsibility has been given added prominence in order to improve the quality of growth.

The **need for improved global governance** has been recognised following the Busan Forum during which the EU played a prominent role. This involves broadening cooperation to all development partners. The EU is committed to self-restraint with regard to avoiding further proliferation of global and thematic programmes or vertical funds, and will seek to use and strengthen the existing channels. Completing the reforms of multilateral institutions thus takes on added prominence. These reforms entail increasing developing countries' representation and voice.

The way forward

In the context of various ongoing international processes, discussions on ODA, climate finance, sustainable development, biodiversity and global public goods are closely linked. **There seems to be an emerging international consensus that a joined-up approach** is thus needed to tackle global challenges. The proposals for defining new aggregates that would enhance accountability fall into three broad categories: (a) changing *how* we measure development efforts; (b) changing *what* we measure (including by complementing/replacing ODA with a broader aggregate); or (c) changing *where* we measure ODA/GNI ratios (at the recipient level rather than at the donor's level). These discussions will have an impact on future EU Accountability Reports.

Introduction

This Staff Working Document is the tenth in a series of annual progress reports drafted since 2003 (previously labelled ‘Monterrey report’). Building on previous reports, it assesses where the EU and its Member States stand in relation to their common commitments on financing for development. This report is especially focused on the evolution in key areas since the previous one, and thus only summarises issues discussed at length last year.

The Report fulfils the Council’s invitation to the European Commission to monitor progress and report annually on common EU commitments, initially focusing on ODA commitments made at the 2002 International Conference on Financing for Development in Monterrey. The Council later expanded the original monitoring mandate to cover all areas of financing for development, including aid effectiveness, aid for trade, tax governance and development, and fast-start climate finance.

The report is also intended to serve as input for EU preparations for several international meetings to be held in 2012, for the operationalisation of the Busan High Level Forum IV on aid effectiveness held in late November 2011, and the bi-annual WTO/ OECD monitoring meeting of all donors on aid for trade. It will also contribute to discussions on the post-2015 MDG framework, including the UN MDG Review Summit.

The report is based on input provided by EU Member States and the Commission through (i) the 2012 EU annual questionnaire on Financing for Development, which covers key EU commitments related to the international financing for development agenda, (ii) the bi-annual 2011 trade and development WTO/OECD survey, (iii) the complementary in-country monitoring, through EU Delegations, of aid for trade provided by EU donors and (iv) public sources and OECD online databases on development cooperation (IDS Online).

The Council also called on the Commission to make the annual progress report a model of transparency and accountability, and for the second time the Commission is presenting a single, comprehensive report covering all topical issues of the international financing for development agenda. Furthermore, like last year, all Member States have agreed to the online publication of their replies to the annual questionnaire on financing for development. The Commission complements this exercise through Donor Profiles that give an overview of the overall development strategy of each Member State. These are available on the EuropeAid webpage. **Annex 1** lists the bibliography for all chapters. **Annex 2** presents the methodology applied for analysing ODA and climate finance. **Annex 3** is the Statistical Annex on ODA trends (including individual graphs for all EU Member States showing the gaps from 2010 to reaching 2015 targets for ODA to Africa and ODA to LDCs). **Annex 4** consists of the Aid for Trade Report 2012.

1. REDUCING AID DEPENDENCY AND INCREASING SUSTAINABLE FINANCING FOR DEVELOPMENT

1.1. Improving domestic resource mobilisation

EU Commitments

● *EU policy on tax and development is set out in the 2010 Communication on "Tax and Development - Cooperating with Developing Countries on Promoting Good Governance in Tax Matters"*[1] *and accompanying Staff Working Document. Their main recommendations were endorsed by the Council in its Conclusions of 14 June 2010*[2] *and by the European Parliament resolution of March 2011.*

● *The relevance of this agenda was reinforced through the 2011 Commission Communication on "The future approach to EU Budget support to third countries".*[3] *The "Agenda for Change" Communication provides further emphasis on tax policy and administration by stating that "the EU will continue to promote fair and transparent domestic tax systems in its country programmes, in line with the EU principles of good governance in the tax area, alongside international initiatives and country by country reporting to enhance financial transparency".*[4] *The main recommendations of the Agenda for Change were endorsed by the Council in its Conclusions of 14 May 2012.*[5]

The objective of this chapter is to present EU progress in implementing the Monterrey consensus, and subsequent Doha declaration in the area of tax and development. The recent Busan Partnership for Effective Development Cooperation highlights the relevance of this area by emphasising its role in underpinning sustainable development and combating illicit flows by addressing tax evasion.[6]

As evidenced by the fiscal difficulties experienced worldwide during 2011, domestic resource mobilisation is more crucial than ever for creating a sustainable fiscal space to implement and support development programmes.

1.1.1. Strategic Orientations

Taxes are essential for sustainable development, the legitimacy of the State, economic stability, and the financing of public services and infrastructure. The Commission's Communication on Tax and Development argued that development aid policies should contribute to building **effective, efficient, fair, and sustainable tax systems** in line with the principles of good governance in tax matters (transparency, exchange of information and fair tax competition) and to helping generate sustainable **revenues** in partner countries. The Council Conclusions on Tax and Development of 14 June 2010 stated that the EU would support developing countries in tax policy, tax administration

[1] COM(2010) 163 final, http://ec.europa.eu/development/icenter/repository/COMM_COM_2010_0163_TAX_DEVELOPMENT_EN.PDF
[2] Council Conclusions on Tax and Development – Cooperating with developing countries in promoting good governance in tax matters, 11082/10, 15 June 2010, http://register.consilium.europa.eu/pdf/en/10/st11/st11082.en10.pdf
[3] COM(2011) 638 final, http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2011:0638:FIN:EN:PDF
[4] COM(2011) 637 final, http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2011:0637:FIN:EN:PDF
[5] http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/EN/foraff/130243.pdf
[6] See European Parliament resolution on combating tax fraud and tax evasion. While mainly concerned with Member States, the resolution also mentions third parties. http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+TA+P7-TA-2012-0137+0+DOC+XML+V0//EN&language=EN

and tax reforms, including the fight against tax evasion and other harmful practices.[7] A recent IMF paper[8] reviews issues and good practices concerning revenue mobilisation in developing countries and provides a useful complementary road-map on implementing reforms in this area. Some of its proposals are taken on board below.

Following the Monterrey Conference of 2003, there has been no visibly increased emphasis on tax reform in developing countries, which is in contrast to the significant scale-up of reforms in the mirror area of public expenditure management. The 2011 Agenda for Change Communication[9] calls on the EU and its Member States to accelerate progress in this area through promoting more domestic resource mobilisation in line with the principles of good governance in tax matters, inter alia in the context of budget support operations. Furthermore, as noted in the 2011 Communication on Budget support[10], fair and transparent tax systems are central to fostering citizenship and state-building, lead to enhanced domestic accountability and political participation. Both Communications also reaffirm the principle whereby EU budget support should complement the partner country's own efforts to mobilise domestic revenues. The EU will thus continue to promote domestic resource mobilisation in its country programmes and will pay special attention to reforms in this area when considering eligibility to Budget Support.

Complementing the above-mentioned EU policies, Member States are increasingly focusing on the issue of taxation and development. Recently issued policy statements or analysis include:

- A DFID briefing note issued in 2009, but still reflecting current UK policy, highlights how effective tax systems are central to core priorities including promoting economic growth, tackling climate change and achieving the Millennium Development Goals. It points that the tax system is at the heart of an effective State. Taxes, raised in ways that encourage economic growth and promote political accountability, build the political legitimacy of the State and offer the eventual “exit strategy from aid”. Furthermore, in February 2012, a select committee[11] of the **UK** Parliament reporting on tax and development made the case that in view of substantial funding available to tax agencies, UK aid should focus more on neglected areas such as international and subnational taxation, encouraging broader citizen engagement, and building specialised expertise in tax administrations.[12]
- In 2011, the **French** Ministry of Finance issued a working paper entitled “Orientations for French Cooperation in Tax Matters.”[13] Noting that taxes are the largest source of development finance, the report argues for more attention to be paid to revenue mobilisation through taxes. It concludes that in order to enhance the impact of actions this context justifies strengthening bilateral cooperation in the field of tax mobilisation while ensuring it is well articulated with both France’s bilateral budget support and with all the multilateral programmes.
- The **German** Ministry of Economic Cooperation and Development, in collaboration with the OECD, has funded a report on appropriate modalities for supporting tax systems.[14] The objective of this 2011 study was to assess the role of various aid approaches and to identify practical recommendations for improving development assistance in this area.

[7] More details were provided in the 2011 Accountability Report.
[8] “Revenue Mobilization in Developing Countries”, IMF, March 2011.
http://www.imf.org/external/np/pp/eng/2011/030811.pdf
[9] COM(2011) 637 final, Op. Cit.
[10] COM(2011) 638 final, Op.Cit.
[11] Appointed by the House of Commons.
[12] http://www.publications.parliament.uk/pa/cm201012/cmselect/cmintdev/writev/1821/tax04.htm
[13] http://www.diplomatie.gouv.fr/fr/IMG/pdf/Rapport_cooperation_en_matiere_fiscale.pdf
[14] Draft of September 2011: http://www.taxcompact.net/documents/2011-11-02_Appropriate-Aid-Modalities-for-Supporting-Tax-Systems_DRAFT.pdf

1.1.2. EU assistance to developing countries in tax and customs reform and related capacity building

Supporting domestic resource mobilisation in developing countries remains the most important element of tax reform from a macroeconomic standpoint. For low income countries, it is important not only to increase domestic revenues, but possibly to consider the tax system as a whole: its composition, its impact on economic activity and private investment, its redistributive effects and its impact on state-building.

There is limited systematic and comparable information on tax systems of developing countries. There appears to be support for establishing **a standard diagnostic framework for assessing tax programmes**, styled after the Public Expenditure and Financial Accountability (PEFA) framework that has been widely used for budget assessments. Nevertheless, recent studies provide insights for specific regions:

- A news release by OECD in January 2012 underlines the role of rising tax revenues in Latin America's economic development. It shows that the average tax to GDP ratio in 12 Latin American and Caribbean countries rose almost continuously from 14.9% in 1990 to 19.2% in 2009. This increase reflects strong economic growth, taxation of non-renewable natural resources, and better management of tax administrations. As these countries find themselves in relatively strong economic conditions, they are able to consider reforms that generate long-term, stable resources for governments to finance development.
- A 2012 report by the Asian Development Bank[15] considers the issue of how mobilised revenue can help alleviate inequality. It notes that both government spending and taxation can affect inequality and that more tax revenues can be mobilised by broadening tax bases and improving tax administration.

The need for additional revenue is substantial in many developing countries, but the quality of measures also matters. More fundamentally still, the centrality of taxation in the exercise of State power means that more efficient, fairer, and less corrupt tax systems can spearhead improvement in wider governance relations. Developing countries bear primary responsibility for building and improving efficient and fair tax systems and committing the necessary resources thereto, with EU and Member States supporting these efforts.

It is unclear whether Member States pursue **coordinated and complementary approaches** to avoid aid fragmentation and unmet demand in some countries – especially those with limited donor presence. Nevertheless, a division of labour based on comparative advantage seems to be applied in practice to improve coverage of recipient countries.

In contrast to the previous period, the EU and its Member States do not report initiating any new support to national supreme audit institutions, nor were civil society organisations (CSOs) and parliaments specifically targeted. The relatively low level of engagement with CSOs and national parliaments may lead to low level of stakeholder ownership of tax reform. Indeed, where CSOs are weak, key stakeholders in reforms may lack a voice. Similarly, parliaments lacking an adequate understanding of public financial management issues may not fully appreciate the importance of the laws presented to them in this area, and may not sufficiently scrutinise public financial management and hold governments to account.

[15] Asian Development Bank, Asian Development Outlook 2012 - Confronting rising inequality in Asia, 2012, http://www.adb.org/sites/default/files/pub/2012/ado2012.pdf

Mobilising domestic financial resources for development

The EU and most Member States undertook new initiatives in 2011 to support tax reforms in developing countries. Exceptions include both new Member States and some Eurozone members. The breadth and scope of activities were quite diverse with respect to focal countries and type of assistance. Capacity building activities commonly reported included the development of financial management systems, research programmes, training and study tours. Many Member States deliver training indirectly by funding specialised programmes managed by international organisations (such as the IMF, OECD etc.). Other activities focused on tax policy reforms and related legislation. Most of the assistance was concentrated on ACP countries, ENP countries and candidate countries for EU membership, as well as Latin America, in contrast with what was reported last year. Ministries of finance as well as tax and customs administration constituted the bulk of beneficiaries in recipient countries. While three-quarter of Member States provide no or **limited support for domestic resource mobilisation** in the context of Public Financial Management reforms, they nonetheless recognise its importance and monitor progress. Only Portugal reports a substantial level of support.

The EU and about one-third of Member States **monitor domestic resource mobilisation**. Typically, this is done in the context of budget support operations, notably through a Financial Management criteria. Some Member States such as Austria and Finland rely on specific indicators to monitor domestic resource mobilisation. Similarly, Sweden and Germany refer to indicators embedded in joint assessment frameworks. The latter also conducts annual fiduciary risk assessments in each country receiving budget support; revenue/GDP below 10% is considered as grounds for exclusion from such support. Finally, DFID's monitoring is indirect, through project monitoring of interventions which aim to improve revenue collection in countries.

Limiting the impact of tax expenditures

The general EU position is to discourage tax avoidance. However, a number of developing countries, investors and development partners have put forward arguments either in favour of or against specific regimes. The basic case made in favour of tax expenditures (including exemptions, deductions and credits) is that they promote economic development, for instance by reducing investment costs, help overcome market distortions elsewhere and avoid regressive taxation, such as taxation of humanitarian aid. The case against specific regimes argues that they lead to revenue loss, may reduce transparency and create an uneven playing field, while many of the benefits may be gained through appropriate provisions in the general tax code.

Tax expenditures are substantial in most developing countries and half of EU Member States support initiatives aimed at improving tax collection and reducing exemptions. The EU supports partner countries in this area through various initiatives. The Commission Communication on Tax and Development gives a strong signal towards reducing tax exemptions and provides the basis for technical cooperation with partner countries in the tax area, as well as for the bilateral support provided through the EU Delegations. Most of the aid provided by Member States is through technical assistance. This includes direct support such that provided by Belgium to Burundi, Germany to African and Latin American countries, France's fiscal diagnostic, dissemination of best practice by Latvia, and the UK's support to Kosovo[16]. Romania's support is provided through the sponsoring of study tours for experts from Iraq and Palestine. Another approach is to fund regional centres, especially those associated with the OECD and the IMF. Member States providing such support include Germany, Spain, Hungary and the UK. Finland's involvement in this area was through participation in joint public expenditure reviews in Tanzania.

[16]under UNSCR 1244/1999

There is no consensus between Member States on whether or not tax exemptions should continue to be sought on projects financed through external aid. The debate concerns whether tax exemptions reflect a specific case or should be dealt with by encouraging coherence with the general EU stance against it, and if taxes are to be financed who should do so (donor, beneficiary, and/or government). One rationale for continued exemptions as opposed to funding of taxes by donors is to ensure that maximum amount of funding is used to support the specific project, as opposed to providing the government's consolidated budget with resources. Austria for example notes the risk of providing such additional resource to governments with weak governance structure. The UN has also argued that taxation hinders humanitarian assistance and proposes that this type of aid be exempted. In addition to being in-line with the general position on tax exemption, one argument in favour of funding taxes by development partners is pragmatic, in line with growing programmatic lending and to avoid project implementation difficulties due to insufficient counterpart funding and/or delays in granting of tax exemption.

Some donors and international financial institutions, including the World Bank[17] in 2004, have already changed their rules and regulations towards funding all reasonable project costs including taxes. The practice regarding tax exemptions of EU projects is also moving in this direction. However, a common approach has not yet been adopted by Member States. Some are considering eliminating the requirement that their projects be tax exempt without necessarily adopting a formal position on the matter (e.g. Finland, Denmark and UK), while others have either expressed cautious support (e.g. Austria, Cyprus, Czech Republic, Germany) or are in favour of no longer requiring tax exemptions (Estonia, Slovenia, France and Romania are already implementing this measure) and/or start funding taxes. Despite progress, the following considerations still remain: (a) certain types of exemptions may need to remain (humanitarian aid, officially supported credits, and exemptions based on double taxation treaties); (b) donor approaches (EU, OECD and UN) would need to be harmonised; and (c) as pointed out by Hungary, specifics would need to be worked-out.

1.1.3. Promoting good governance in the tax area

The EU and most Member States have provided support in the past for addressing tax evasion and harmful tax competition, and promote the principles of good governance in tax matters in their cooperation policy.

The EU **promotes the principles of good governance in tax matters** with partner countries by:

- Including specific references to the principles of good governance and to the need for strengthening tax systems in economic cooperation, partnership and other agreements with third countries.

– Making the best use of its relevant dialogue and assessment tools for the monitoring of domestic revenue efforts and good governance commitments. Mainstreaming DRM issues into EU budget support programmes.

– Providing capacity building in tax matters to developing countries committed to the principles of good governance in the tax area.

The Commission and nine Member States reported new activities in 2011. Member States completing new Tax Information Exchange Agreements (TIEA) were Belgium, Czech Republic and

[17] See http://www1.worldbank.org/operations/eligibility/index.html

Slovak Republic. Technical assistance and training seminars were also funded by Germany (supporting the East Africa Community and Central American countries) Spain, France (Chad), Slovak Republic (Georgia and Serbia) and UK (Kenya and Ghana). The German Federal Ministry for Economic Cooperation and Development (BMZ) also continued its support of the International Tax Compact[18] (ITC) – an informal international action and dialogue platform grouping bilateral and multilateral donors to strengthen international cooperation with developing and transition countries to fight tax evasion and avoidance.

Adoption and implementation of the OECD Guidelines on Transfer Pricing

Transfer pricing rules determine how international transactions within a multinational company must be priced to ensure each country receives its fair share of tax. The OECD Transfer Pricing Guidelines, approved by the OECD Council in their original version in 1995 (last updated in 2010), provide guidance on its application. At the OECD's first Global Forum on Transfer Pricing on 28 March 2012, tax officials from 90 countries agreed on the need to simplify transfer pricing rules, strengthen the guidelines on intangible issues and improve the efficiency of dispute resolution. In the coming year, the Global Forum will carry out a transfer pricing risk assessment, developing a detailed "how-to" manual[19] which will establish good practices for governments when they assess transfer pricing risk at the beginning of an audit.

In the past years, about half of the Member States had already provided assistance with implementing OECD guidelines on transfer pricing. Eight Member States, as well as the EU, supported new initiatives in this area during 2011. The Commission, Netherlands and Belgium participated in the OECD task force subgroup on Transfer Pricing. Belgium, Spain, France, Slovenia and UK organised training seminars – some in collaboration with OECD. The EU and some Member States, at times in collaboration with OECD, supported developing countries in drafting transfer pricing regulations: EU pilot initiative in Ghana and Vietnam; Germany's support to Ghana; Estonia's support to Moldova; and UK's assistance to Kenya and Ghana.

In 2011, the EU funded a study[20] on transfer pricing oriented towards strengthening this area in developing countries. The study recommends suitable approaches for supporting developing countries in the adoption and implementation of transfer pricing rules in line with international standards in order to increase tax revenue. The study outlines the current transfer pricing situation in Ghana, Honduras, Kenya and Vietnam, and makes recommendations for donor support to developing countries. As a follow up to the study, the Commission envisages providing support to capacity building in transfer pricing to a number of developing countries.

To increase donor coordination in the field of transfer pricing which results in better targeted and more coordinated assistance to the partner countries an OECD**/EU/WB initiative on transfer pricing** was initiated**.**

[18] http://taxcompact.net/index.html
[19] In parallel with this UN is working on a manual that provides practical guidance on dealing with transfer pricing issues and applying the arm's length principle to developing countries.
See: http://www.un.org/esa/ffd/tax/documents/bgrd_tp.htm
[20] EuropeAid, Implementing the Tax and Development policy agenda – Transfer pricing and developing countries, http://ec.europa.eu/taxation_customs/resources/documents/common/publications/studies/transfer_pricing_dev_countries.pdf

Revenue Transparency[21]

The OECD's 2011 publication on tax transparency[22] documents **substantial progress in areas such as multilateral conventions, and Tax Information Exchange Agreements as well as double taxation conventions**. The number of agreements that meet the international standard has increased by more than 700 since the G20 put a spotlight on the issue. These agreements are starting to yield real results as mechanisms for the enforcement of tax laws. During 2011, members of the Global Forum on Transparency and Exchange of Information for Tax Purposes have issued reports (peer reviews) on the 14 EU Member States.[23] These reviews provide information on agreements with developing countries.

EU Member States also participate in other initiatives that contribute to transparency and combating corruption. In particular, 23 EU Member States report their support and/or adherence to the United Nations Convention against corruption[24] and 20 Member States participated in the implementation of the OECD convention on combatting bribery of foreign officials.[25] A further 9 Member States participated in the Stolen Asset Recovery initiative[26] launched in 2007 by the World Bank and UN.

In addition, in October 2011 the Commission adopted a legislative proposal[27] for a new set of disclosure requirements for extractive companies that are based in EU countries. Under the new rules, companies in the EU would have to publish all payments to the governments in countries they operate in. This proposal is currently being discussed in the Council and the European Parliament. The increase in transparency will contribute to fighting corruption, increase resource-rich countries' accountability and improve domestic revenue mobilisation.

Box 1.1.3 The Extractive Industry Transparency Initiative (EITI)

Some 3.5 billion people live in countries rich in oil, gas and minerals. Through good governance the exploitation of these resources can generate large domestic revenues to foster inclusive growth, discourage conflict and reduce poverty.

The EITI is a voluntary process aimed at strengthening governance by improving transparency and accountability in the extractive industries sector. With 35 implementing countries now, the initiative is becoming a global standard for corporate governance and transparency. The EITI requests that companies publish payments to governments, and that the latter, in turn, disclose revenues received from companies. This enhances domestic accountability and strengthens the demand for good governance so as to reduce corruption related to extractive activities. EITI implementation slowed down in 2011. Nevertheless, 13 countries have now achieved EITI-compliant status (compared to 11 last year) and 20 countries are new candidates.

The EU is an increasingly active participant in, and supporter of, this initiative. Its position is reflected in the recent European strategy on the sustainable supply of raw materials, and in the follow-up to the commitments on enhanced support made in the 2010 Tax and Development Communication. The Commission is a member of the Steering Working Group of EITI and a member/observer of the EITI Board. It provided further support to EITI during 2011 through (a) co-financing of two conferences (i.e., 5th Global Conference and National Coordinators Conference); (b) bilateral support via Delegations; and (c) contribution to World Bank EITI Trust Fund.

[21] The Kimberley process was covered in some detail in the 2011 Accountability Report. One notable recent event is that in November 2011, the EU played a key role in reaching a consensus on trading Marange diamonds from Zimbabwe.
[22] OECD, Tax transparency 2011 – Report on progress, http://www.oecd.org/dataoecd/52/35/48981620.pdf
[23] OECD, Op. cit. see P. 14
[24] http://www.unodc.org/unodc/en/treaties/CAC/
[25] http://www.oecd.org/dataoecd/4/18/38028044.pdf
[26] See website for further information. http://www1.worldbank.org/finance/star_site/
[27] COM(2011) 683 final of 25.10.2011 http://europa.eu/rapid/pressReleasesAction.do?reference=MEMO/11/734&format=HTML&aged=0&language=EN&guiLanguage=en

Several Member States listed activities in support of EITI:

- Belgium and UK provided funding to the multilateral Trust Fund administered by the World Bank. In addition to funding the Trust fund, Germany, Denmark and Netherlands also supported the EITI secretariat by funding its activities. Denmark also funded the 2011 EITI Global Conference. Netherlands was an EITI board member in 2011, hosting the 17th board meeting June 2011, and has seconded a staff member to EITI secretariat for the period 2012 – 2015.
- Germany is supporting the EITI implementation through various bilateral as well as regional TC-projects, e.g. in DR Congo.
- The Italian Government continues to support EITI by: (a) favouring its outreach proposing a suitable scoring system so as to provide an incentive for good performance by implementing Countries; (c) supporting the New EITI rules without expanding the scope of the Initiative; (d) improved monitoring. A private Italian enterprise engaged in the oil and gas, power generation, petrochemicals, oilfield services and engineering industries is implementing pilot projects and initiatives in Congo, Gabon, Nigeria, Kazhakstan and Timor Leste.

Support to international and regional initiatives, and organisations

The EU and many Member States indicated that they continued relying on intermediaries when supporting developing countries' tax reform agendas. This is being done through international initiatives such as the Africa Tax Administration Forum (ATAF), the OECD, the International Tax Compact (ITC) and International Tax Dialogue[28] (ITD), "Centro Inter-Americano de Administraciones" (CIAT) and three IMF facilities (i.e. Regional Technical Centres, the Trust Fund on Tax Policy and Administration, and the Topical Trust Fund on Managing Natural resource Wealth).

The IMF remains the prime partner,receiving by far the most financial support. ITC was the next largest recipient, albeit at a much smaller scale. While there are a number of institutions receiving support, there is insufficient information to assess whether this leads to inefficiency and unnecessary segmentation in delivery of tax reforms.

Emerging themes

While the impact of the new approach to EU budget support will only be evident in the future, it is likely that EU and Member States will incorporate tax administration and fair tax collection as part of their budget support eligibility criteria.

[28] The International Tax Dialogue (ITD) is a collaborative arrangement involving the European Commission, IDB, IMF, OECD, UK (DFID) and World Bank Group to encourage and facilitate discussion of tax matters among national tax officials, international organisations, and a range of other key stakeholders. The ITD Secretariat is currently hosted by the OECD. http://www.itdweb.org/Pages/Home.aspx

1.2. Maintaining sustainable debt levels

EU Commitments
● *Council Conclusions of 11 Nov 2008*[29]*, § 44: 'The EU will take action to help restore and preserve debt sustainability in low-income countries (...), to prevent unsustainable lending behaviour by lenders which have not contributed to alleviating the burden of poor countries, and to deter aggressive litigation by distressed-debt funds. The EU also agrees not to sell claims on HIPCs to creditors unwilling to provide debt relief.'*
● *Council Conclusions of 18 May 2009*[30]*: (§12): 'the EU will continue supporting the existing debt relief initiatives, in particular the Heavily Indebted Poor Countries (HIPC) Initiative and Multilateral Debt Relief Initiative (MDRI) and values the Evian approach as an appropriate flexible tool to ensure debt sustainability'.*
● *In line with the Doha Declaration, the EU has also confirmed in the Council Conclusions of 18 May 2009 (§12), that it 'supports discussions, if relevant, on enhanced forms of sovereign debt restructuring mechanisms, based on existing frameworks and principles, including the Paris Club, with a broad creditors' and debtors participation and ensuring comparable burden-sharing among creditors with a central role for the Bretton Woods Institutions in the debate.*

In 2011, the European Commission and the EU Member States have maintained their engagement in providing debt relief and are increasingly prioritising actions on the prevention of unsustainable debt, including by:

- reducing debt levels through debt relief, using existing mechanisms (HIPC, Paris Club, etc.);
- strengthening public debt management capacity to avoid unsustainable debt levels;
- supporting greater transparancy in the new forms of financing;
- fighting against aggressive litigation by vulture funds.

In addition, most EU Member States have highlighted **three current challenges** to continue ensuring debt sustainability:

- In light of the increased weight of bilateral non-Paris Club creditors, there is a need for more transparency and closer collaboration between these creditors and **the Paris Club** in order to guarantee that debt relief operations deliver sufficient relief and preserve a fair burden sharing.
- Debt relief under the HIPC Initiative and MDRI has also created new borrowing space. Domestic debt is likely to grow in importance as domestic savings increase and governments seek to develop domestic debt markets. Low Income Countries (LICs) are likely to face **new risks as the range of creditors and debt instruments continues to expand**.[31]

[29] Council Conclusion on *Guidelines for EU participation in the International Conference on Financing for Development (Doha, 29 November - 2 December 2008),* 15480/08,
[30] Council Conclusions on *Supporting developing countries in coping with the crisis,* 10018/09
[31] Revisiting the Debt Sustainability Framework for Low-Income Countries (2012), WB and IMF http://www.imf.org/external/np/pp/eng/2012/011212.pdf

- Moreover, due in part to the current economic context, many countries remain **vulnerable to shocks**, particularly exporters, facing risk of unsustainable debt in the future.

1.2.1. Honouring EU commitments on debt relief

For the past decade, debt relief has been a key tool for achieving debt sustainability. It has been implemented through the HIPC/MDRI initiative, complemented with bilateral and other types of debt forgiveness.

The Commission and EU Member States have continued to deliver on their commitments on debt relief. In 2011, the EU provided debt relief through participation to the World Bank's Debt Relief Trust Fund (DRTF) to support the participation of the African Development Bank in the HIPC Initiative. HIPC Interim debt relief in the form of coverage of debt service payments or arrears clearance was also provided to the following countries: Comoros, DRC, Ivory Coast, Guinea and Togo. Full relief further to reaching HIPC completion point was provided to Liberia in early 2011.

As of end-2011, 32 countries had reached HIPC completion point, with another 7 sub-Saharan countries potentially eligible.[32]

Debt relief has markedly improved the debt position of the 32 post-completion point Highly Indebted Poor Countries, bringing their debt indicators to sustainable levels. Debt cancelation has brought, and still brings, strong positive effects for debt-distressed countries, allowing more fiscal space for poverty related expenditures.

To date, debt reduction packages under the HIPC Initiative have been approved for 36 countries, 30 of them in Africa, providing EUR 54.6 billion (USD 76 billion) in debt-service relief over time. T**he debt stocks of the 36 post-decision-point HIPCs have been reduced by over 90 %**.[33]

It is to be mentioned that the IMF and IDA Boards had informal discussion on the future of the HIPC Initiative during 2011. So far, this question remains an open issue and the focus is rather on ensuring a close monitoring of vulnerabilities of Low Income Countries than only focusing on HIPC.[34]

1.2.2. Public Debt Management: a critical component of debt sustainability

In 2002, the Monterrey Consensus called for a speedy, effective and full implementation of the enhanced Heavily Indebted Poor Countries initiative and for increased international cooperation for

[32] HIPC Fall Meeting 2011: Chad, Côte d'Ivoire, Comoros and Guinea have past the Decision Point and half of them expected to reach completion point in 2012, while Eritrea, Sudan and Somalia are potentially eligible.

[33] HIPC Initiative country documents and IDA/IMF staff estimates, Fall 2011

[34] The former option would neither be consistent with the original intent of the Initiative nor justified by the current debt sustainability outlook in LICs. It would also be beset with moral hazard. At the same time, fixing a timeline for the closure of the Initiative might not allow the debt situation of some potentially eligible countries to be addressed. While this option would respond to concerns raised about the longevity of the HIPC Initiative, it would eventually require either the setting up of a new debt-relief framework or dealing with each country on a case-by-case basis, which would be politically challenging, time consuming, and ultimately costly." In "Status of Implementation and Proposals for the Future of the HIPC Initiative", IDA and IMF, 8 November 2011

sustainable debt financing.[35] **The G8/Africa Joint Declaration** of the Deauville G8 summit of May 2011 reiterated the call to preserve debt sustainability in Africa.[36]

Debt relief alone is not sufficient to guarantee debt sustainability. As illustrated in the latest World Bank report on HIPC Status[37], strengthening debt management capacity and institutions in HIPC countries is also a priority. According to this study, seven post-Completion Point HIPCs remain at high risk of debt distress after HIPC and MDRI relief, and 10 at moderate risk.

While good debt management has proven to be a valuable asset in mitigating the effects of external shocks, poor public debt management contributes to the negative impact of these shocks and seriously undermines a country's ability to achieve sustainable growth. Governments, both creditor and borrower, need to closely monitor debt management.

"Debt management systems in most African countries have advanced, albeit only marginally" according to the mutual review of development effectiveness in Africa.[38] **To reduce their debt vulnerabilities sustainably, countries need to pursue cautious borrowing policies and strengthen their public debt management capacity.**

Beyond HIPC and MDRI, EU Member States have maintained a strong support to enhance debt management capacities of developing countries. The main international initiatives to support better debt management and to which the EU contributes include the Debt Management Facility and the Debt Management and Financial Analysis Software.[39] (see box 1.2.2) The European Commission has committed new contribution of EUR 3 million to the World Bank's Debt Management Facility (DMF Trust Fund) and EUR 3 million to UNCTAD's Debt Management and Financial Analysis Software (DMFAS); both signed in December 2011.

Box 1.2.2: The Debt Management Value Chain

● The World Bank Debt Management Facility's covers "upstream" activities:
- Diagnosing the performance of debt management in a country (DEMPA)
- Assistance in formulating reform plans to correct the weaknesses identified by the DEMPA (Reform Plan)
- Preparing a reform plan to address the weaknesses identified (Reform Plan)
- Preparing a medium term debt strategy (MTDS)

● The Debt Management and Financial Analysis Software from UNCTAD comparative advantage is in the 'downstream' activities needed for implementing the DMF Reform Plan and strategy, through:
- Supporting countries in implementing debt management reform plans
- Providing debt management systems (the DMFAS system)
- Training the debt management staff in debt reporting, operations, statistics and analysis
- Advising on debt office reorganisation, integration and staffing
- Providing sustainable support (Helpdesk) for these areas

[35] http://www.un.org/esa/ffd/monterrey/MonterreyConsensus.pdf
[36] http://www.g8-g20.com/g8-g20/g8/english/live/news/shared-values-shared-responsibilities-g8-africa.1320.html
[37] WB 2011 HIPC status report. http://siteresources.worldbank.org/INTDEBTDEPT/ProgressReports/23063134/HIPC_MDRI_StatusOfImplementation2011.pdf
[38] Mutual Review of Development Effectiveness 2011. http://www.oecd.org/document/0/0,3746,en_39862406_39906520_49370432_1_1_1_1,00.html
[39] DMFAS Programme, Strategic Plan 2011 – 2014, http://r0.unctad.org/dmfas/docs/Strategic_Plan_2011-2014.pdf

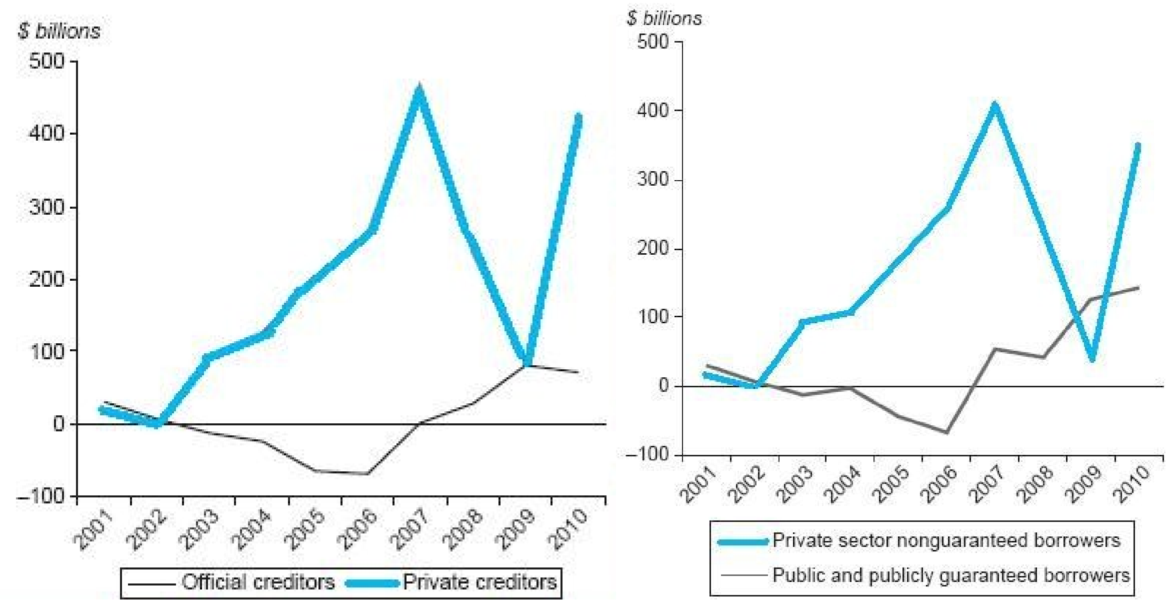
1.2.3. Diversified sources of lending and debt vulnerabilities

In a number of LICs, finding sources to finance priority infrastructure investments has led to an increase of reliance on non-concessional external borrowing, requiring a close monitoring on the evolution of debt vulnerabilities in those countries.[40] In addition, keeping debt at sustainable levels will continue to be a necessity in the context of EU blending operations in developing countries. Debt sustainability is assessed by the European Commission in all of the activities in the framework of innovative financing (see chapter 3.1 on Innovative Financing).

Over recent years, a number of new public and private creditors have increased their lending to Africa's Low-Income Countries, creating concerns of swelling debt burdens. Intra-developing country lending, or so-called South-South flows, have been a driving force behind the rise in lending by bilateral creditors and new commitments. Between 2007 and 2010, bilateral creditors signed new loan agreements totaling around EUR 102 billion (USD 135 billion), of which China accounted for close to one third.

Figure 1.2.3

Net Debt Flows by Creditor Type, 2001-2010 **Net Debt Flows by Borrower Type, 2001-2010**



Source: World Bank Debtor Reporting System in World Bank Global Finance 2012: External Debt of Developing Countries

In an effort to cast more light on the recent activities of new donors, the OECD, in collaboration with the World Bank, the United Nations Development Programme (UNDP), and the United Nations Department of Economic and Social Affairs (UNDESA), conducted a survey of nine

[40] IDA-IMF (2011) HIPC and MDRI – Status of Implementation and proposals for the future of the HIPC Initiative, p17. This highlights the need to broaden the use of the Debt Sustainability Framework (DSF)for Low Income Countries as an appropriate first step towards tracking debt sustainability on a continuous basis (see: http://siteresources.worldbank.org/INTDEBTDEPT/ProgressReports/23063134/HIPC_MDRI_StatusOfImplementation2011.pdf)

developing countries that are considered as important new lenders (Brazil, Chile, China, India, Malaysia, Russia, South Africa, Thailand, and Venezuela). So far only Chile, Malaysia, and Thailand responded to the survey.[41]

A recent analysis by the Africa Economic Outlook[42] shows a relatively limited impact of financing from the non-Paris Club creditors, though the lack of transparency does not allow to fully measure the situation. **The lack of transparency in loan contracting processes from non-Paris Club continues to constitute a risk**, especially for the most fragile nations. Raising transparency standards for financial transactions between African countries and their new partners would help developing economies to borrow more sustainably. This would strengthen the credibility of the "emerging" partners as part of the international financial governance structure.[43] The G8 Action Plan for Good Financial Governance in Africa emphasises the importance of the joint World Bank-IMF Debt Sustainability Framework as the framework of choice for the “new” donors and lenders.

The growing importance of private creditors within the new lenders also increased the need for closer coordination amongst different types of lenders. In 2010, lending by private creditors to developing countries significantly increased from EUR 61.9 billion (USD 86 billion) in 2009 to EUR 320.1 billion (USD 424 billion) in 2010.[44]

The EU as a whole believes that creditor coordination is key to reaching the objective of restoring and preserving debt sustainability in LICs. In that connection, EU Member States call for enhanced dialogue and outreach to non-Paris Club offical bilateral creditors.

1.2.4. The status of Vulture Fund Litigation

The problem posed by vulture funds is also a major concern**. Vulture fund *modus operandi*** is simple: commercial creditors purchase distressed debt on the secondary market, significantly below its face value, and seek to recover the full amount, including through litigation.

Litigation is possible because most debt relief initiatives, such as the HIPC initiative, do not alter the legal rights and obligations between HIPCs and their external creditors. Accordingly, creditors are legally entitled to use available legal mechanisms to enforce their credit claims against HIPCs, unless the HIPC debtors and their creditors reach bilateral legal agreements which would put their debt into the authority of HIPC initiative.

Figure 1.2.4 Where Vulture Funds Strike[45]

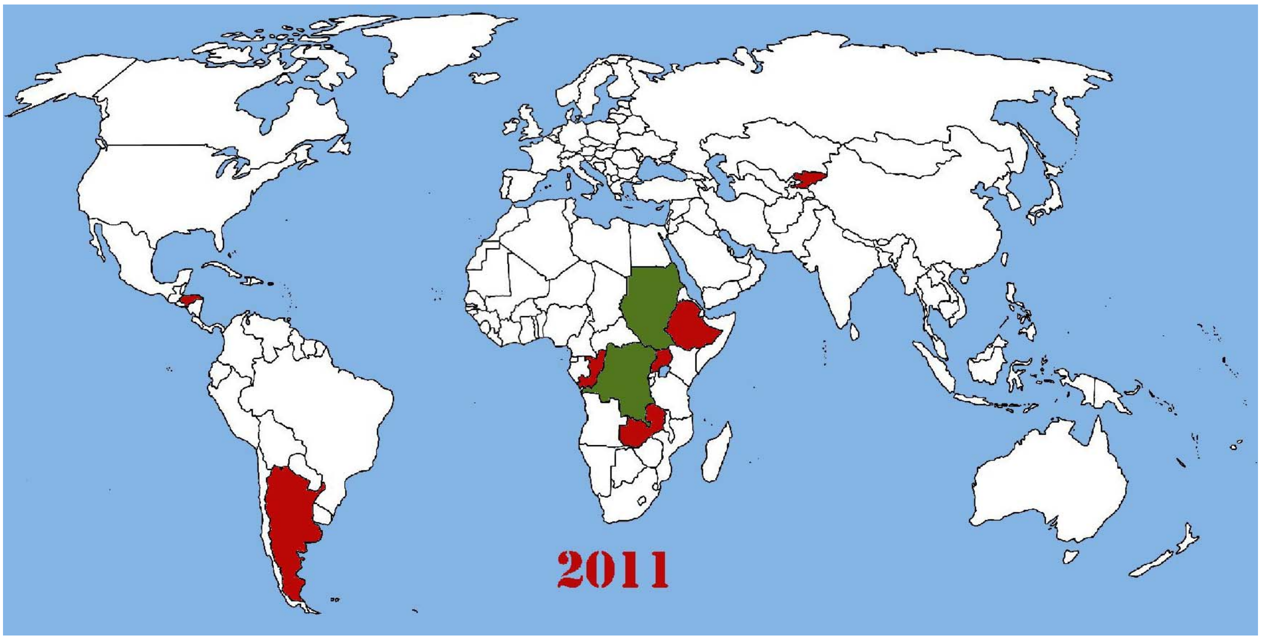
[41] OECD: “Prudent versus Imprudent Lending to Africa: From debt relief to emerging lenders”, http://www.oecd-ilibrary.org/development/prudent-versus-imprudent-lending-to-africa_242613675043

[42] “Transparency needed to end debt sustainability fears”, 2 march 2012 http://www.africaneconomicoutlook.org/en/in-depth/africa-and-its-emerging-partners/industrialisation-debt-and-governance-more-fear-than-harm/transparency-needed-to-end-debt-sustainability-fears/

[43] http://www.g8.utoronto.ca/finance/g8finance-africa.pdf

[44] Global Development Finance 2012: External Debt of Developing Countries. World Bank 2012. page 17. http://data.worldbank.org/sites/default/files/gdf_2012.pdf

[45] African Legal Support Facility, Tunisia, 26 January 2012, http://www.aflsf.org/attachments/article/57/02.%20Amir%20SHAIKH%20(ALSF)-%20Vulture%20Fund%20Overview.pdf



The IMF reports that in some cases, the claims by vulture funds constitute as much as 12-13 % of a country's gross domestic product; 11 HIPCs have been targeted so far in forty-six lawsuits and the plaintiffs are concentrated in three countries, ie. USA (8), British Virgin Islands (7), and the United Kingdom (4).[46] The lawsuits are mostly concentrated in a few courts (New York (15), London and Jersey (7), Paris (7)).[47]

Box 1.2.4: Vulture Funds in Figures[48]

- Vulture funds have **average recovery rates of about 3 to 20 times their investment**, equivalent to returns of (net legal fees) 300-2000 %.
- **The vulture funds exert pressure on the sovereign debtor by attempting to obtain attachment of the government's assets abroad**: in a recent case against Zambia, a vulture fund, having bought a debt for EUR 2.16 million (USD 3 million), sued Zambia for EUR 39.55 million (USD 55 million) and was awarded EUR 11.14 million (USD 15.5 million) at High Court of England and Wales.
- Litigation is typically protracted with many lawsuits taking 3 to 10 years to "settle." Legal documents indicate six years as a **conservative medium estimate for recovery, which suggests that annualised returns average 50 to 333 %**
- Some of these claims were bought at roughly 10 % of face value, implying **very high gross recovery rates**. Subtracting legal costs, often recouped from the sovereign debtor, these recovery rates are probably the highest in the distressed debt market.

[46] Presentation by IMF, *Litigating Creditors in the Context of the HIPC Initiative: An Overview – G-7 Debt Experts Meeting,* presented December 12, 2007, Paris, France

[47] http://www.aflsf.org/attachments/article/60/Annex%201_Memorandum%20for%20the%20establishment%20of%20ALSF.pdf

[48] African Development Bank 2011, http://www.aflsf.org/attachments/article/60/Annex%201_Memorandum%20for%20the%20establishment%20of%20ALSF.pdf

– The World Bank estimates that more than one-third of the countries which have qualified for its debt relief have been targeted with lawsuits by at least 38 litigating creditors with judgments totalling USD 1 billion in 26 of these cases. Out of this amount 72% of the judgments have been against Regional Member Countries.[49]

In 2010, the Paris Club confirmed its deep concern over vulture fund litigation. Taking stock of the harmful consequences of litigation for HIPC countries, and consistent with the principle of comparability of treatment, the Paris Club had resolved[50] in May 2007 to avoid the sale of their claims on HIPCs to other creditors who do not intend to provide debt relief under the HIPC initiative. The Paris Club had also urged other creditors to follow suit.

In that connection, five EU Member States have implemented specific interventions in order to prevent the actions of distressed-debt funds:

– On April 6, 2008, **Belgium** has passed a bill to prevent the seizure or transfer of public funds for international cooperation, in particular related to the methods of the Vulture Funds. Belgium also aims to assist African countries in their legal protection against vulture funds through financial support to the African Legal Support Facility.

– **Spain** regularly supports, on a case by case basis, the initiatives and discussions that take place in the Paris Club in order to prevent aggressive litigation against HIPCs. Spain is committed not to sell or securitize debt owed by HIPC countries. Spain also supports the Debt Reduction Facility by the World Bank, that addresses the issue of litigating creditors.

– **France** is strongly supporting the Debt Reduction Facility by the World Bank.

– **Italy** is commited with any intervention to prevent aggressive litigation against HIPCs within the Paris Club and through the World Bank.

– In 2011, the **UK** made the Debt Relief (Developing Countries) Act 2010 permanent. This legislation limits the amount of money that commercial creditors can recover from developing countries progressing through the HIPC Initiative, removing the incentive to pursue them in courts.

[49] cf list of RMC http://www.afdb.org/en/about-us/members/
[50] http://www.clubdeparis.org/sections/communication/archives-2007/communique-presse-du/downloadFile/PDF/PR_Paris_Club_Lit___HIPCmay2007.PDF?nocache=1180459594.89

2. INTERNATIONAL PRIVATE FLOWS FOR DEVELOPMENT

2.1. Supporting trade as an engine for development

EU Commitments

In 2007, the EU Aid for Trade Strategy51 aimed at increasing financial resources for Aid for Trade and improving its impact on poverty reduction. In particular, the EU committed to:

– Increasing EU Aid for Trade within the gradual increase of overall EU aid;

– Enhancing the Pro-poor Focus and Quality of EU AfT;

– Increasing EU-wide and Member State donors' capacity in line with globally agreed aid effectiveness principles;

– Building upon, fostering and supporting ACP regional integration processes with an ACP specific angle of EU AfT.

– Collectively spend EUR 2 billion annually on Trade-Related Assistance by 2010 (EUR 1 billion from MSs and the Commission respectively). In the range of 50% of the increase to be available to ACP countries.

2.1.1. Towards a more focused EU policy framework on Trade and Development

The EU's new trade, growth and development policy outlines how the EU's trade and investment policies should be used to foster inclusive growth and sustainable development in developing countries. In particular, **the EU has agreed on the need for more differentiation among developing countries** in order to better reflect their differences in needs, potentials and objectives, and to better target Aid for Trade initiatives at LDCs and other countries most in need. At the same time, LDCs need to more systematically and effectively include trade in their development strategies.

Many developing countries have deepened their integration into the world economy and have become increasingly important players in multilateral and international trade. The rise of **emerging economies** such as Brazil, Russia, India, China and South Africa (BRICS), both as economic and political players, is striking in that regard and it serves as a positive illustration that increased participation in world trade can be an engine for economic growth and poverty reduction in developing countries. While these changes have helped lifting hundreds of millions out of poverty, **not all developing countries have enjoyed the same improvements.** This is particularly true for LDCs, especially in sub-Saharan Africa, which have been further marginalised and whose economy remains vulnerable to economic shocks, notably because of their dependence on a few export products, particularly primary commodities. This points to the fact that while trade is a necessary condition for development, it is not sufficient and domestic reforms are essential to harness the benefits of trade for growth and poverty reduction.

[51] Council Conclusions on "The EU Strategy on Aid for Trade: Enhancing EU support for trade-related needs in developing countries", 14470/07, 29 October 2007.

In times of budgetary constraints and when aid budgets are being closely scrutinised, **the need to improve accountability and to show results becomes even more stringent**. This is especially true in the case of Aid for Trade, which has become an increasingly important priority in development cooperation. The topic was discussed at highest level in 2011, in the framework of the Third Global Review of Aid for Trade[52]. The OECD, with financial support from the European Commission, is preparing a study to analyse and assess good practices in developing country-owned results measurement frameworks for trade-related aid activities, with a view to providing the development and trade community with recommendations on how to measure Aid for Trade results.[53] The European Commission is also providing funding to the International Trade Centre (ITC) for the launch of a re-developed Market Access Map, which will provide global trade related information in particular to low income countries.

2.1.2. Taking stock of the way the EU has delivered on its Trade and Development commitments since 2002

In its 2002 Communication on "Trade and Development"[54], the Commission had pledged to grant developing countries greater access to the EU market. In the 2007 Joint Aid for Trade Strategy[55], the EU and its Member States committed to provide developing countries with more Aid for Trade. The **EU has delivered well on both accounts**, leading the way at global level and making the EU the most open market to developing countries in the world.[56] This has mainly been achieved through the EU's Generalised System of Preferences. In particular, the 'Everything but Arms' scheme provides LDCs with duty-free quota-free market access to the EU for all their products except arms. As for the GSP+, it is the flagship EU trade policy instrument supporting sustainable development and good governance in developing countries.

In addition, **the EU has facilitated the use of existing preferential schemes** through new and simpler GSP rules of origin[57], and made it easier for developing countries to get practical information on access to the EU market through the establishment of the online Export Helpdesk.[58] **The EU has also boosted its bilateral trade relations with developing countries**. Since 2002, the EU and ACP countries have been negotiating Economic Partnership Agreements. In addition, a series of Free Trade Agreement negotiations have been launched, and in several cases already concluded, with more advanced developing countries and regions.

The EU's trade policy has also supported the promotion of regional integration of developing countries' markets, although results have often fallen short of expectations. A key difficulty is the limited capacity of regional organisations to formulate project proposals that are viable and supported by their members.

In line with the EU PCD commitments, the EU has strived to improve the coherence and complementarity between the EU's trade and development policies. Several key areas of progress were identified in the "EU 2011 Report on Policy Coherence for Development"[59], including trade negotiations, market access, the decent work agenda, corporate social responsibility, and intellectual

[52] OECD/WTO (2011), "Aid for Trade at a Glance 2011: Showing Results"

[53] OECD (2011), *Strengthening Accountability in Aid for Trade*, The Development Dimension, OECD Publishing.

[54] COM(2002) 513 final
[55] COM(2007) 163 final
[56] http://trade.ec.europa.eu/doclib/docs/2012/january/tradoc_148990.pdf
[57] Council Regulation (EC) No 1063/2010, 18.11.2010
[58] www.exporthelp.europa.eu
[59] SEC(2011) 1627 final

property rights. These orientations were fully taken into consideration in the 2012 Communication on "Trade, Growth and Development", adopted by the Commission on 27 January 2012[60]. The Communication sets new orientations for the next decade on ways to improve the contribution of the EU's trade and investment policies to development. This was followed, on 16 March 2012, by the adoption of Council Conclusions[61] on this topic. The latter set out how Aid for Trade from the EU and its Member States can be better targeted, notably through:

– continued global leadership of the EU and its Member States to respond to the Aid for Trade demands;

– better targeted, result-oriented and coordinated Aid for Trade as part of the aid and development effectiveness agenda, as agreed in Busan;

– encouraging developing countries to integrate trade as a strong component in their development strategies;

– enhancing the complementarity and coherence between trade and development instruments;

– greater focus on LDCs and developing countries most in need;

– better coordination of EU and Member States' AfT and alignment with strategies of partner countries;

– support aimed at helping developing countries' small-scale operators to capture the benefits of trade;

– work with new and traditional partners to increase the effectiveness of the Enhanced Integrated Framework and other internationally recognised frameworks, and focus on impact and results.

2.1.3. Progress on Aid for Trade[62]

Since 2007, the EU and its Member States have been driving the global Aid for Trade efforts, confirming again in 2010 the **EU's position as collectively the largest provider of AfT in the world**. Indeed, the EU and Member States accounted for around 32% of total AfT flows in 2010, reaching more than EUR 10.7 billion (EUR 8.2 billion from EU Member States and EUR 2.5 billion from the EU), an increase of 4.2% in comparison with last year.

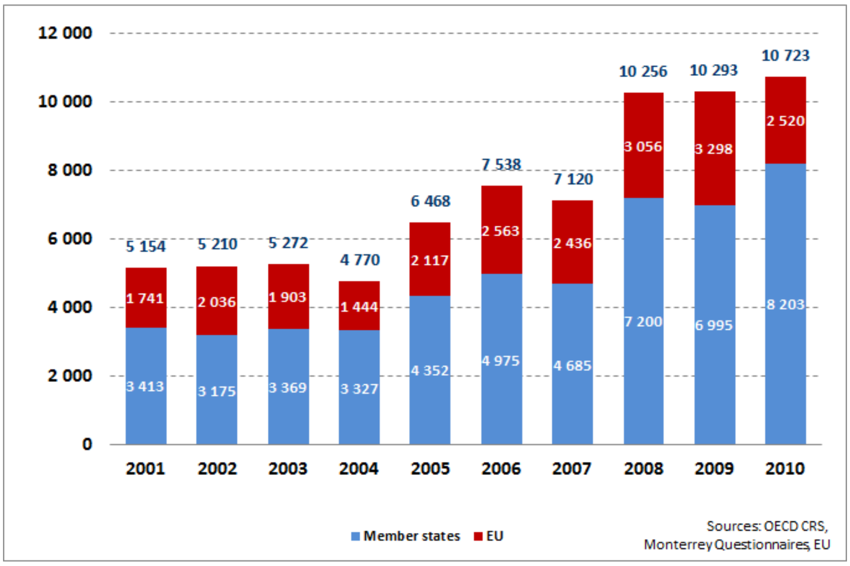
As highlighted in last year's report, the EU and its Member States had already met their 2010 EUR 2 billion target for Trade Related Assistance (TRA) since 2008, however, for the first time since 2005, there was a decrease of TRA between 2009 and 2010**Total TRA in 2010 reached EUR 2.6 billion, compared to EUR 2.8 billion in 2009** (or -8% in 2010, to be compared to +24% in 2009).

Figure 2.1.3. Aid for Trade (EU and Member states, in EUR million)

[60] Communication on "Trade, Growth and Development: Tailoring Trade and Investment for those Countries most in Need", COM(2012)22 final of 27 January 2012, and accompanying Staff Working Document on "Trade as a Driver of Development" - http://ec.europa.eu/trade/wider-agenda/development

[61] http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/EN/foraff/129019.pdf

[62] For more detailed analysis, see the "Aid for Trade monitoring report 2012" which is included in annex 4.



A central observation is the growing complementarity between the EU and its Member States, in terms of geographical distribution, sector presence, instruments used and size of projects.

– **In terms of geographical distribution**: Africa continues to receive the largest share of AfT flows (38% of the total), both from the EU and from the Member States, with a total of EUR 3.9 billion in 2010. It is followed by Asia (20%), Europe (13%) and America (9%). The second primary destination of EU AfT flows is Europe, while it is Asia for Member States. The share of AfT to LDCs declined to 16% of total AfT in 2010 (EUR 1.7 billion against EUR 8.7 billion to non-LDCs), compared to 22% in 2009. This is partially due to cyclical and EU programming factors.

– **In terms of sectoral presence:** while the EU AfT projects are essentially focused on three main sectors, namely agriculture (35%), transport and storage (29%) and energy (13%), Member States are more focused on energy (33%), with agriculture and transport representing smaller shares of the total (17% and 12%). Moreover, Member States are also present in banking and financial services, while the EU is not.

– **In terms of instruments used:** while grants still represent 100% of AfT programmes of the EU institutions, Member States finance 43% of their AfT programmes through loans, and 13% through equity investments. As a result of this, the share of grants has decreased in the overall AfT flows of the EU and Member States, while it has substantially increased for loans. This could also explain the decrease of the share of AfT flows to LDCs, which are the primary beneficiaries of grants.

– **In terms of size of projects:** the average size of EU projects is ten times the average size of Member States projects (EUR 11.2 million in the case of EU and EUR 1.1 million for Member States).

The analysis of replies from the EU Delegations and Member States Representations in developing countries to this year's AfT questionnaires shows a moderate improvement in terms of the partner-donor policy dialogue; the availability of updated trade needs assessments; joint operations and harmonisation; the inclusion of strategic regional economic integration priorities into the national development plan or trade strategy; and in highlighting the prominent hurdles for assessing AfT programmes and projects.

2.2. Remittances as an instrument of development

EU Commitments
• Since 2009, the EU and its Member States are committed "*to promote transparent, cheaper, faster and more secure flows of remittances to migrants' countries of origin, and to ensure that relevant legislation does not contain provisions hampering the effective use of legal remittance channels"*[63].

2.2.1. Towards a renewed EU overarching framework for the cooperation with third countries in the area of migration and mobility

On 29 May 2012, the Council adopted Conclusions[64] on "The global approach to migration and mobility", following the Commission Communication on this subject issued in November 2011.[65] The objective was to strengthen the overarching framework for the cooperation with third countries in the area of migration and mobility, which was defined for the first time in 2005. One of the operational priorities is precisely to maximise the development impact of migration and mobility, including by facilitating remittances and reducing transaction costs. In particular, the Council reaffirmed *"the need to ensure faster, easier and cheaper remittance transfers and enhance the impact on development of social and financial remittances while ensuring coherence with other development priorities".*

The 2011 Commission Staff Working Paper on "Migration and development"[66] accompanying the afore-mentioned Communication provides further analysis of the achievements since 2005 in the area of remittances, and identifies some remaining challenges, including on capacity building to support partner countries interested in designing regulatory frameworks and into promoting financial literacy, new technologies and access to credits to stimulate productive investment and job creation.

In 2011, the European Commission launched a study to assess the state of implementation of existing EU commitments with regard to remittances. The study will be published in the second half of 2012.

While migration and mobility can, if properly managed, contribute to the reduction of poverty in developing countries, proper attention is now also being paid to minimising the negative side-effects of the EU migration policy.[67] In particular, in line with the Policy Coherence for Development commitments, the EU and its Member States must pay due attention to the possible downsides of migration, notably its social costs and the risks of households becoming dependent on income from remittances.

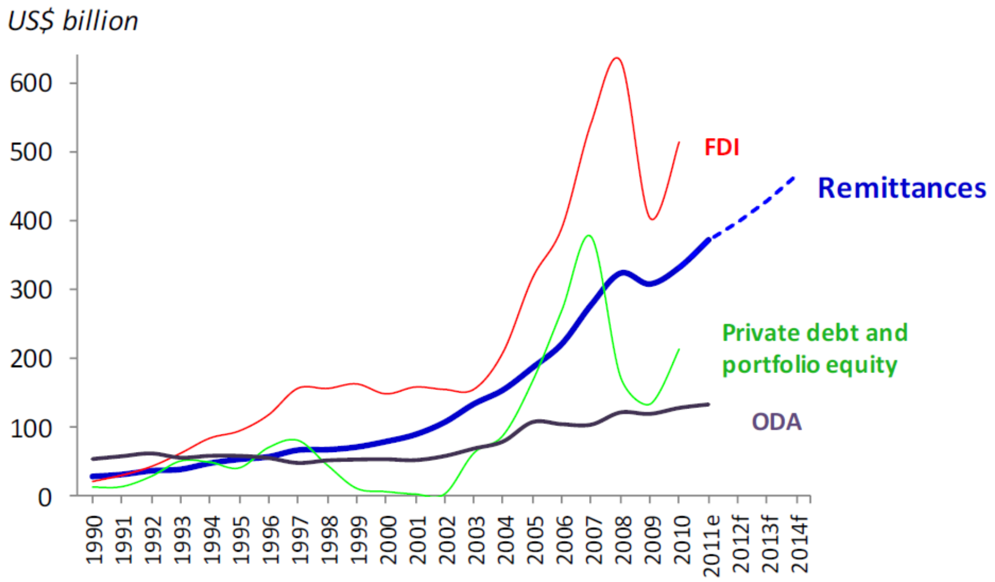
[63] Council Conclusions on Migration for Development, 15806/09, 30 November 2009
[64] Council Conclusions on the global approach to migration and mobility, 9417/12
[65] COM(2011) 743
[66] SEC(2011) 1353 final
[67] SEC(2011) 1627 final

2.2.2. *Progress on remittance outflows*

According to the latest estimations of the World Bank[68], recorded[69] **global remittances** flows to developing countries are estimated at EUR 267.5 billion (USD 372 billion) in 2011, **an increase of 12.1% over 2010**, and are expected to grow at a rate of 7-8 % annually to reach EUR 333.5 billion (USD 467 billion) by 2014.

As shown in the graph below, global remittance flows have been growing steadily during the crisis in comparison to other private resource flows. However remittances from the EU have kept momentum since 2008[70].

Figure 2.2.2



Source: World Bank, 2012[71]

At EU level, total EU27 remittance outflows amounted to EUR 31.2 billion in 2010, **a 3% increase from last year** (EUR 30.4 billion in 2009), most of which are sent to developing countries.

According to Eurostat[72], the outflow of workers' remittances was highest in 2010 in **Spain** (EUR 7.2 billion or **23% of total EU27 remittances**), Italy (6.6 billion or 21%), Germany (3.0 billion or 10%), France (2.9 billion or 9%), the Netherlands (1.5 billion or 5%) and Greece (1.1 billion or 3%). Among these Member States, the share of extra-EU27 remittances in the total ranged between 67% in Germany and 91% in Greece. In 2010, the majority of Member States recorded similar levels of outflows of workers' remittances to 2009.

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[68] World Bank (2012), "Migration and Development Brief n°18", World Bank, Migration and Remittances unit, http://siteresources.worldbank.org/INTPROSPECTS/Resources/334934-1110315015165/MigrationandDevelopmentBrief18.pdf

[69] Only remittances flowing through financial channels are recorded. Actual remittances, including remittances flowing through non-financial channels, are guessed to outperform considerably those figures.

[70] Eurostat Statistic Focus 4/2012.

[71] World Bank, "Migration and Development Brief n°18", Idem.

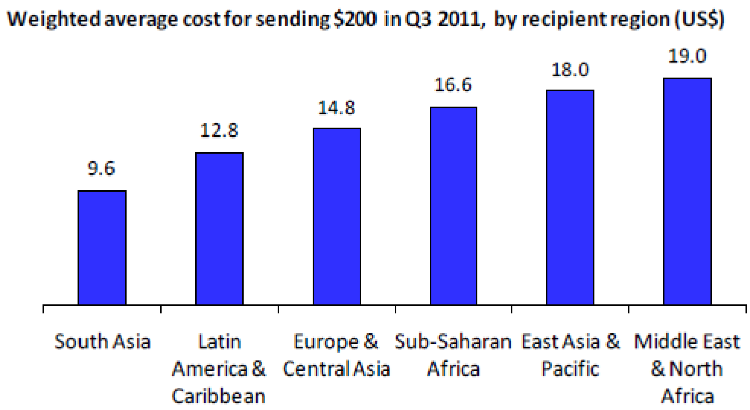
[72] Eurostat News release, 12 December 2011, STAT/11/183, http://europa.eu/rapid/pressReleasesAction.do?reference=STAT/11/183&format=HTML&aged=0&language=EN&guiLanguage=en

2.2.3. *Reducing transfer costs of remittances*

At the Cannes G20 Summit in November 2011, G20 members agreed to reduce the average cost of transferring remittances from 10% to 5% of the amount transferred by 2014.[73]

Although remittance costs have fallen steadily in recent years, they remain high, especially in Africa.

Figure 2.2.3



Source: World Bank, 2011[74]

As seen in figure 2.2.3 above, remittance costs on average continue to remain high, impacting many poor migrants and their families. Efforts to reduce remittance costs include increasing market competition in many remittance corridors and wider application of cheaper and more convenient remittance technology. Also there is a great need to improve data on remittances and migration at the national and bilateral corridor levels, for more accurate monitoring of progress towards the agreed objective. It is estimated that reducing these costs to an average of 5 % (compared to the current average, which is roughly twice that) would save EUR 10.8 billion (USD 15 billion).[75]

At EU level, remittance services are being made cheaper, more transparent, more competitive and more reliable.

In particular, the transposition of the 2007 Payment Services Directive (PSD) into the national legislation of a majority of EU Member States has contributed to increased transparency in the provision of payment services, including the remittance market. Moreover, several EU Member States (including France, Germany, Italy, the Netherlands and the United Kingdom) have set up their own remittance price comparison websites on costs and quality of services. The above mentioned (par. 2.2.1.) study launched by the European Commission will include elements to assess the feasibility of a common EU portal on Remittances.

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[73] G20 Cannes Summit final declaration, http://www.g20-g8.com/g8-g20/g20/english/for-the-press/news-releases/cannes-summit-final-declaration.1557.html

[74] http://siteresources.worldbank.org/INTPROSPECTS/Resources/334934-1110315015165/MigrationandDevelopmentBrief17.pdf

[75] "Innovation With Impact: Financing 21st Century Development", Report by Bill Gates to G20 leaders, Cannes Summit, November 2011.

2.2.4. *Donor initiatives*

Several EU Member States such as Austria, France, Germany, and the Netherlands have either launched or supported the launch of **studies and workshops aimed at improving the knowledge about the main remittance channels and payment systems.** For instance, France has funded a study on "Reducing the costs of migrants' remittance and optimising their impact on development remittance channels from France to Maghreb and the 'franc' area", the results of which were presented in February 2012.[76] The recommendations of the study, carried out by the credit institution "Epargne sans Frontières" (Savings without Borders) and co-financed by AfDB and the French Development Agency, centred on cutting the cost of migrant money transfers and boosting their effect on the development of African countries.

A number of EU Member States (including Denmark, France, Germany, the Netherlands, and Poland) have also taken **specific actions in 2011 aiming at increasing remittances' channelling to productive and social investments**. For example, Germany is in the process of setting up a social lending and knowledge brokerage project aiming at offering migrants a systematic way of collecting and spending remittances as well as sharing knowledge on small enterprise development or social investment in their countries of origin.

[76] Reducing the costs of migrants' remittance and optimising their impact on development remittance channels from France to Maghreb and the 'franc' area , http://www.afdb.org/fileadmin/uploads/afdb/Documents/Publications/2011_12%20Remittances_executive_summary_en.pdf

3. LEVERAGING INTERNATIONAL DEVELOPMENT FINANCE: BEYOND OFFICIAL, BEYOND DEVELOPMENT AND BEYOND ASSISTANCE

3.1. Innovative Financing – Sources and Mechanisms

EU Commitments

● *Council Conclusions of 14 June 2010*[77] *(§31): Innovative financing sources and mechanisms complement other resources. The EU seriously considers proposals for innovative financing mechanisms with significant revenue generation potential, with a view to ensuring predictable financing for sustainable development, especially towards the poorest and most vulnerable countries. The EU calls on all parties to significantly step up efforts in this regard, welcomes the ongoing work by the Leading Group on innovative Financing for Development, and takes note of the ongoing work of the Task Force on International Financial Transactions for Development and of the Task Force on Innovative financing for Education.*

● *Council Conclusions of 14 November 2011*[78] *(§3.5): Engage the private sector in aid and development effectiveness in order to advance innovation, create income and jobs, mobilise domestic resources and further develop innovative financial mechanisms. (§52): The EU calls (…) on development partners to further develop and increase the use of innovative financial instruments and blending of grants and loans that enhance the catalytic role of aid in promoting private sector engagement and private sector development.*

● *Busan partnership for effective development cooperation, December 2011*[79] *(§32. C): Further develop innovative financial mechanisms to mobilise private finance for shared development goals.*

In the current context of financial crisis and budgetary austerity, discussions on innovative financing mechanisms have gained a new resonance, both within the EU and at global level. A good illustration of this growing interest in innovative financing mechanisms is the G20's formal agreement for the first time to support innovative financing for development and climate change and to move forward by using a menu of options.[80]

According to the Leading Group on Innovative Financing for Development[81], which is the main recognised international forum for discussions on this matter, about twenty countries in the world have already set up one or more innovative financing mechanisms so far. Thanks to these mechanisms, close to EUR 4.3 billion (USD 6 billion) have been raised since 2006.[82]

[77] Council Conclusions on the Millennium Development Goals for the United Nations High-Level Plenary meeting in New York and beyond - Supporting the achievement of the Millennium Development Goals by 2015, 11080/10, 14 June 2010.

[78] Council Conclusions on the EU Common Position for the Fourth High Level Forum on Aid Effectiveness, 16773/11, 14 November 2011.

[79] http://www.aideffectiveness.org/busanhlf4/images/stories/hlf4/OUTCOME_DOCUMENT_-_FINAL_EN.pdf

[80] G20 Cannes Summit final declaration, 4 November 2011, http://www.g20-g8.com/g8-g20/g20/english/for-the-press/news-releases/cannes-summit-final-declaration.1557.html

[81] Thirteen EU Member States plus the European Commission are now members of the Leading Group, which was recently chaired by Spain.

[82] Leading Group, "Peer review of existing innovative financings for development", http://www.leadinggroup.org/IMG/pdf/Mapping_FIDENG-3.pdf

At the **10th Plenary Session of the Leading Group**, which took place in Madrid **in February 2012,** the emphasis was put on the important advocacy role of the Leading Group in multilateral fora. Following the successful experience in 2010 at the UNHLPM on MDGs, the Leading Group organised another high-level side event in the context of the Rio+20 Conference, in partnership with the United Nations, in order to raise awareness on the potential of innovative financing mechanisms to **mobilise resources for sustainable development**.

3.1.1. Distinction between innovative financing sources and mechanisms

There is no universally accepted definition of Innovative Financing Mechanisms[83] (IFM). While the term initially referred to new **sources** of development financing that could complement traditional ODA[84] in a stable and predictable way[85], it has progressively been expanded to include new and innovative financial **mechanisms** aiming at enhancing the effectiveness and efficiency of financial flows.

The main characteristic of these mechanisms is that they differ from traditional approaches to mobilising and/or delivering development finance. They are usually complementary to traditional ODA and tend to address a specific negative externality.

IFM are thus mechanisms that (i) support fund-raising by tapping new sources and engaging investors beyond the financial dimension of transactions, as partners and stakeholders in development; and/or (ii) deliver financial solutions to development problems on the ground. They can therefore be considered "innovative" either because of the nature of sources, the way they are collected and used, or their modes of governance.

Broadly speaking, **IFM can be divided into innovations in fund-raising and innovative financial solutions for development:**

(1) Mechanisms that generate additional financing for development by tapping into new and **innovative finance (or funding) sources** (non-traditional or non-conventional ODA resources, emerging donors and the private sector). For example, global solidarity levies (such as the airline ticket tax or the Adaptation Fund) or national lotteries.

(2) Mechanisms that offer **innovative financial instruments/solutions** in the way revenues are collected and pooled, traditional development finance is used and aid is delivered. For example, public-private partnerships such as the International Finance Facility for

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[83] According to the Leading Group on Innovative Financing for Development, Innovative Financing Mechanisms are "*mechanisms for raising funds for development [which] are complementary to official development assistance. They are also predictable and stable. They are closely linked to the idea of global public goods and aimed at correcting the negative effects of globalisation*."

[84] The question of whether or not innovative financing can be counted as ODA in the understanding of the OECD/DAC remains in the remit of each donor country. A thorough discussion on the perimeter of ODA is currently ongoing in view of better identifying and measuring the various financial flows, in the broad sense, benefitting developing countries ("ODA+"). Initiated within the OECD/DAC, this discussion could inspire a general debate on the modernisation and the diversification of the measuring instruments of the financing effort for development.

[85] See Declaration of Doha UN Conference on Financing for Development: §51 - "…*these funds should supplement and not be a substitute for traditional sources of finance, and should be disbursed in accordance with the priorities of developing countries and not unduly burden them*."

Immunisation (IFFIm), or copayment schemes such as the Advance Market Commitment (AMC) mechanism.

According to a World Bank working paper[86], four types of innovative mechanisms can be distinguished:

– *Private mechanisms:* they involve private-to-private flows in the market and in civil society.

– *Solidarity mechanisms*: they include public-to-public or sovereign-to-sovereign transfers and form the backbone of multilateral and bilateral ODA and other official flows (OOF).

– *Public-private partnership mechanisms*: they use public funds to leverage or mobilise private finance in support of public service delivery and other public functions, such as risk management.

– *Catalytic mechanisms*: they involve public support for creating and developing private markets (inter alia by reducing risks of private entry).

3.1.2. State of play and revenues raised by existing innovative mechanisms

Twelve Member States are currently using or are planning to use one or more of the existing innovative financing mechanisms to raise funds for development[87].

For example:

- *International Finance Facility for Immunisation (IFFIm)*: Six Member States (France, Italy, Netherlands, Spain, Sweden and the UK) indicated that they are contributing to the IFFIm under the GAVI Alliance. It is estimated that a total of EUR 2.4 billion (USD 3,4 billion) were levied through this mechanism for GAVI between 2006 and 2011[88].
- *EU Emission Trading System[89] (ETS)*: Four Member States (Czech Republic, France, Germany and Hungary) indicated that they are using or considering using the auctioning of allowances under the ETS with a view to financing climate action in developing countries. In that context, Germany also explicitly targets climate adaptation activities that have biodiversity co-benefits.
- *Air ticket levy*: France is the only EU Member State to have introduced an air ticket levy to finance UNITAID, IFFIm and the Global Fund. France estimates that EUR 175.8 million will have been raised through this mechanism in 2011. Cyprus**,** Luxembourg, Spain and the UK are also supporting UNITAID[90], albeit with direct contributions from their general budgets[91].
- *Advance Market Commitments (AMC)*: Two Member States (Italy, UK) participate in the AMC for the development and production of affordable vaccines (France indicated its support for this mechanism without contributing to it at this stage). In 2011, Italy and the UK have contributed to this mechanism by more than EUR 79 million (compared to 55 million in 2010).

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[86] World Bank (2009), "Innovating Development Finance: From Financing Sources to Financial Solutions", CFP Working Paper Series No. 1

[87] For a short review of existing innovative financing mechanisms, refer to last year's Accountability Report.

[88] Leading Group, "Peer review of existing innovative financings for development", Op. Cit.

[89] Since January 2012, the emissions from all domestic and international flights that arrive at or depart from an EU airport are covered by the EU Emissions Trading System.

[90] "Mapping of IFM", Leading Group, "Peer review of existing innovative financings for development", Op. Cit.

[91] Budgetary contributions are based on what an air ticket levy would bring in.

- *Debt2Health*: Germany is the only Member State participating in this initiative, which it is using for the Global Fund to fight Aids, Tuberculosis and Malaria. In 2011, Germany contributed with EUR 3.3 million under this debt swap mechanism.
- *National Lotteries*: Belgium is the only Member State having declared the use of receipts from its national lottery to finance development cooperation. Part of the receipts (EUR 18.3 million) are earmarked for financing food security projects through the Belgian Fund for Food Security.

3.1.3. Major EU initiatives

At EU level, two recent initiatives are worth underlining.

First, **the Commission's "Proposal for a Council Directive on a common system of financial transaction tax and amending Directive 2008/7/EC**"[92], which proposes setting up a harmonised framework for financial transaction tax in the EU. Such a tax, if adopted, would be levied as a rule on all financial transactions relating to financial instruments when at least one party to the transaction is established in a Member State and a financial institution established in a Member State is involved in the transaction. The idea of an EU FTT is strongly debated among Member States with very differing views. Discussions are currently on-going in the Council and the European Parliament in order to look at all the aspects of the proposal and their implications in practice.

The financial transaction tax was proposed as a new own resource for the EU budget, in the context of the preparation of the next multiannual financial framework 2014-2020. The Commission has recently announced that, if adopted as a new own resource of the EU budget, the financial transaction tax could significantly reduce the contributions of Member States to the EU budget, in the magnitude of EUR 54 billion by 2020.[93]

Second, **the extension of the EU Emissions Trading System (EU ETS) to aviation transport,** the scheme for greenhouse gas emission allowance trading within the Community. As foreseen in the Directive 2008/101/EC of the European Parliament and of the Council of 19 November 2008 amending Directive 2003/87/EC, aviation activities are since January 2012 included in the emissions from all domestic and international flights that arrive at or depart from an EU airport.[94]

While these two initiatives do not foresee earmarking of resources for development *per se*, they are nonetheless expected to facilitate Member States' efforts to mobilise funding required for meeting aid targets and tackling other global challenges.

3.1.4. EU Blending Mechanisms

The EU blending mechanisms are an innovative financing mechanism as they leverage additional resources and investments in a context of constrained resources. In particular, involving the private sector as a partner in development to create jobs and income opportunities for the poor, as well as to leverage additional funding through blending for achieving inclusive and sustainable growth, has

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[92] COM(2011) 594 final, 28 September 2011
[93] http://europa.eu/rapid/pressReleasesAction.do?reference=IP/12/300&format=PDF&aged=0&language=EN&guiLanguage=fr
[94] http://europa.eu/rapid/pressReleasesAction.do?reference=CJE/11/139&format=HTML&aged=1&language=EN&guiLanguage=en

been recognised by the 'Agenda for Change', the 'Busan Outcome document on Aid Effectiveness' and has become common practice in development finance.

The EU blending mechanisms combine grants with additional flows (such as loans and risk capital) to gain financial and qualitative leverage, and increase EU development policy impact. The strategic use of a grant element can make projects and initiatives by public or commercial investors financially viable, thereby exerting a leveraged policy impact. The grant element may take various forms such as: direct investment grants; interest rate subsidies; technical assistance, risk capital and risk sharing mechanisms such as guarantees.[95] Beyond unlocking additional project financing, the EU grant element also reduces the price of the project for the beneficiary and contributes to complying with debt sustainability criteria.

Since 2007, the EU has set up a number of **regional blending facilities**: the EU-Africa Infrastructure Trust Fund (ITF) and Investment Facilities for the Neighbourhood (NIF), Latin America (LAIF) and Central Asia. Since 2007, more than EUR 760 million EU grants have been committed to 115 projects. EU grant contributions have leveraged approximately EUR 10 billion of loans by European Finance Institutions, unlocking total project financing volume totalling in at least EUR 26 billion. With three new facilities for Asia, the Caribbean and the Pacific, worldwide coverage is expected in 2012.

3.2. Facilitating Private Investment

EU Commitments

Current EU thinking on engaging with the private sector is set out in the following Council Conclusions:

- *November 2008 Conclusions on a Common EU position for the Doha Financing for Development Conference[96], §10: "The EU is committed to promote policies and instruments supporting private investment and the expansion of partner countries' private sector in support of an inclusive and sustainable economic growth".*
- *December 2011 Conclusions on Reinforcing industrial policy across the EU[97]: The Council welcomed the Communication from the Commission "A Renewed EU Strategy 2011-2014 for Corporate Social Responsibility as well as of the Social Business Initiative.*

3.2.1. Framework for Private sector-led growth

As emphasised in the recent Communication on 'Increasing the impact of EU Development policy: an Agenda for Change'[98], "*inclusive and sustainable economic growth is crucial to long-term*

[96] Council Conclusions on Guidelines for EU participation in the International Conference on Financing for Development (Doha, 29 November – 2 December 2008), 15480/08, 11 November 2008, http://register.consilium.europa.eu/pdf/en/08/st15/st15480.en08.pdf
[97] Council Conclusions on Reinforcing industrial policy across the EU, http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/en/intm/126548.pdf

poverty reduction". In many developing countries, the expansion of the private sector, notably micro-, small- and medium-sized enterprises (MSMEs) is a powerful engine of economic growth and the main source of job creation. Foreign investment also plays an important role, including through the linkages of domestic firms to international markets and through investments in infrastructure and natural resource based activities. One of the main challenges for governments in developing countries is to establish, design and implement institutional, organisational and regulatory frameworks which are conducive to, and often a pre-condition for, private sector development. Governments alone cannot create a private sector with an enterprise culture, but their actions can either hinder or facilitate it. The latter often requires far-reaching economic reforms aimed at improving the investment climate and facilitating access to finance.

A framework for private sector-led growth is incorporated within the 'Agenda for Change'. It advocates for inclusive and sustainable economic growth, resulting in wealth and job creation through inter alia an increased focus on:

- Key drivers for inclusive and sustainable growth, notably a stronger business environment and deeper regional integration. This will be achieved by: (a) supporting the development of competitive local private sectors including by building local institutional and business capacity, and promoting MSMEs; (b) facilitating legislative and regulatory framework reforms and their enforcement; (c) improving access to business and financial services; (d) promoting agricultural, industrial and innovation policies; (e) developing new ways of engaging with the private sector, notably with a view to leveraging private sector activity and resources for delivering public goods; (f) extending the scope and scale of the EU regional blending facilities to further leverage addition financial resources for development; and (g) encouraging regional and continental integration efforts.
- Sectors which build the foundations for growth and help to ensure that it is inclusive and sustainable, notably education, health, employment, and social protection; and on those sectors that have a strong multiplier impact on developing countries' economies and contribute to environmental protection, climate change prevention and adaptation, notably sustainable agriculture and energy. EU support would help insulating developing countries from shocks and thus help provide the foundations for sustainable growth. It should tackle inequalities, in particular to give poor people better access to land, food, water and energy without harming the environment. In both sectors, the EU should support capacity development and technology transfer.

The recent 4th High-Level Forum on Aid Effectiveness in Busan provided further impetus for the above approach. It **highlighted the need for inclusion of new actors on the basis of shared principles and differential commitments, including the private sector**. In particular, it recognised the central role of the private sector in advancing innovation, creating wealth, income and jobs, mobilising domestic resources and in turn contributing to poverty reduction. To this end, the meeting put forward a framework[99] to enable the participation of the private sector in the design and implementation of development policies and strategies to foster sustainable growth and poverty reduction.

The EU promotes foreign and domestic investments, especially for MSMEs, through its support for private sector development in developing countries. The vast majority of EU support is provided through bilateral cooperation programmes, the remainder being through regional programmes

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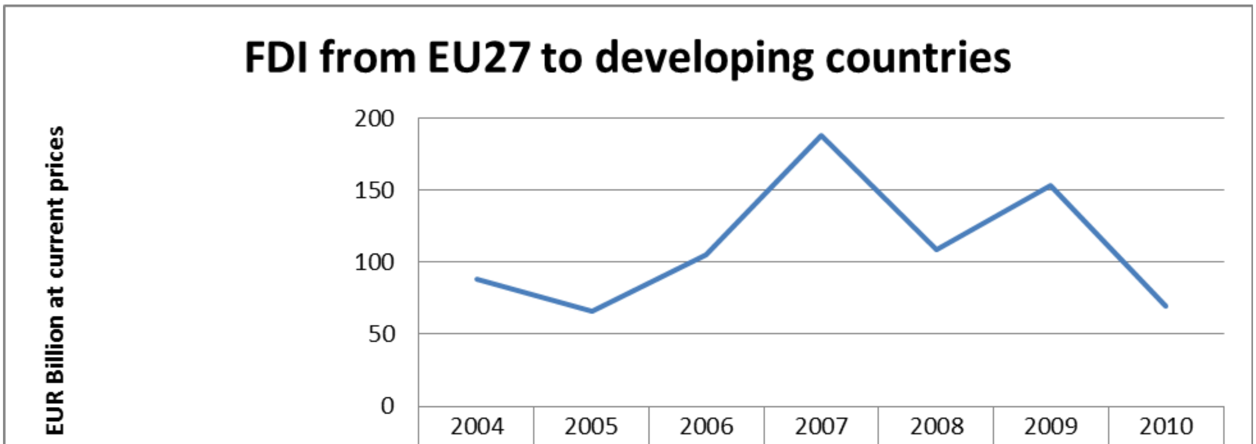
[98] COM(2011) 637 final, http://ec.europa.eu/europeaid/what/development-policies/documents/agenda_for_change_en.pdf
[99] http://www.aideffectiveness.org/busanhlf4/images/stories/hlf4/OUTCOME_DOCUMENT_-_FINAL_EN.pdf

(including all ACP programmes[100]). In addition, the European Investment Bank (EIB) is entrusted with the management of the Investment Facility (IF) provided from the EU Member States' budgets via the European Development Fund (EDF). The IF, alongside the EIB own resources, meets the financing needs of investment projects in the ACP region with a broad range of loans and flexible risk-bearing instruments. In line with the EU Development Policy objectives, the EIB's overriding aim is to support projects that deliver sustainable economic, social and environmental benefits through: supporting responsible private and public investments; fostering regional cooperation and integration; mobilising domestic savings and acting as a catalyst for foreign direct investment; encouraging the broadening, deepening and strengthening of the local financial sector; and relying on/promoting partnerships.

Private flows, notably foreign direct investments, play an important role within the above approach and contribute to provision of needed capital.[101] However, this source of financing from the EU27 has been limited in recent years. According to Eurostat, net FDI from the EU27 to developing countries peaked in 2007 and declined in 2008 before growing in 2009. As shown in Figure 3.2.1[102] below, FDI fell significantly in 2010, reaching a level last observed in 2005. The decline in FDI from the EU, together with resource constraints faced by developing countries, underscores the importance for EU Member States to help mobilise a critical mass of investments in developing countries.

Figure 3.2.1 – Net FDI Flows from EU to Developing Countries (EUR billion, current prices)



	2004	2005	2006	2007	2008	2009	2010
FDI to developing countries	88.5	66.1	105.5	188.5	109	153.1	69.8

Source: Eurostat

3.2.1.1. Business and Investment Climate

Investment climate encompasses economic, institutional, financial and market conditions affecting investment and business operations. It is determined by the legal and regulatory framework, existence of barriers to entry and exit, and conditions in markets for labour, finance, information, infrastructure services, and other productive inputs. It is thus **a cross-cutting issue that affects all aspects of private sector development.** For instance, a typical MSME programme not only

[100] For more details see http://ec.europa.eu/europeaid/what/development-policies/intervention-areas/trade/private_sector_en.htm
[101] Remittances are also relevant; discussed in section 2.2 of the report
[102] The 2010 figure needs to be treated with caution as reporting may not be complete.

addresses access to finance issues but targets improvements in aspects of the investment climate that especially affects the sector.

In developing countries, a conducive investment climate is therefore an important determinant of private sector investment and growth. The EU supports the improvement of the macroeconomic framework and regulatory environment for enterprise development through bilateral cooperation and regional programmes like the Intra-ACP programme "Private Sector Enabling Environment Facility of the Business Environment[103] (PSEEF / BizClim)". Several EU Member States are also active in this area, such as Austria, Netherlands and Germany who work closely with partner countries and donors to improve the business investment climate. Other examples worth mentioning include:

- The **Belgian** Development Cooperation aims at improving the business and investment climate in developing countries by supporting UNDP, the World Bank and Transparency International in their efforts. These are embedded into the bilateral cooperation in countries such as Burundi, Rwanda and DRC.

- The **UK** provides financing for technical assistance and research to improve the investment climate and strengthen growth policies in developing countries. Both are critical for supporting private investment. This assistance helps transform policies, legislation, regulations and government administration to become more efficient and predictable which helps create a more conducive environment for private investment.

3.2.1.2. Financial Services for trade and investment

Financial mechanisms aimed at supporting private sector development usually tackle two inter-related issues of cost and access. The type of funding and the repayment terms are both key determinants on the cost side. Blending of grants with market-based financing is thus a way to reduce costs, especially for investment with long gestation period and with social rates of return well above the financial rate of return. While other measures such as guarantees help address both issues, other mechanisms discussed below help improve access.

The European Commission uses blending mechanisms, in which grants are combined with non-grant financing such as loans and risk capital as a way to leverage additional private and public financing for developmental projects. The strategic use of a grant element and risk-sharing mechanisms may also catalyse public-private partnerships and crowd-in private investment.

The potential range of financial tools used in the EU blending mechanisms includes: technical assistance (TA); investment co-financing; interest rate subsidies; risk-capital operations and risk-sharing mechanisms such as guarantees. To date the EU regional blending facilities have covered similar broadly defined, sectors, i.e. transport, energy, social, water/wastewater, environment, ICT and access to finance for MSMEs. Partners in the beneficiary country can be public or private, with public partners dominating the current projects aside from MSME support.

The European Commission also plays an active role in the sector approach, mainly through Trust Funds in cooperation with Member States.

Box 3.2.1.2 Example of Blending Mechanisms

The Global Energy Efficiency and Renewable Energy Fund (GEEREF) is an innovative Fund-of-Funds, providing global risk capital through private investment for energy efficiency and renewable energy projects in developing

[103] http://acpbusinessclimate.org/bizclim/index.php?option=com_content&view=article&id=50&Itemid=28&lang=en

countries and economies in transition. Launched in 2004, GEEREF aims to accelerate the transfer, development, use and enforcement of environmentally sound technologies for the world's poorer regions, helping to bring secure, clean and affordable energy to local people. GEEREF is sponsored by the European Union, Germany and Norway and advised by the European Investment Bank Group.

Support to the Facility for Euro-Mediterranean Investment and Partnership (FEMIP) promotes private sector development in the Mediterranean region by providing capital to the private sector on terms that are not available locally. This is done mainly through risk capital operations and facilitated through technical assistance. Managed by the EIB, the Support to FEMIP's risk-capital portfolio includes more than 500 operations.

Guarantee mechanisms can reduce risk and enhance access to finance. Such mechanisms can be put in place to promote trade and investment. These instruments are managed and implemented by specialised agencies within EU Member States. Most Member States have established banks for this purpose, including Romania, Hungary and Slovakia's Eximbanks, also Estonia's Fund KredEx and the Latvian Guarantee agency. Austria, Estonia, Hungary and Italy are also amongst the countries that also provide political risk insurance and/or investment guarantees. The case of Austria helps illustrate how such schemes work. The Austrian export credit agency, assumes guarantees for political risks. The "Austria Wirtschaftsservice" (AWS) assumes investment guarantees which cover the commercial risk of Austrian private investments abroad. Being an Austrian government promoted bank, it is the key focus of AWS international activities, to support the establishment and formation of subsidiaries and joint ventures or to enable the acquisition of companies abroad[104].

Finally, MSME access to finance can be improved through the **strengthening of the financial sector** and most Member States also have on-going, mutually reinforcing programmes **supporting private sector development through improved access to finance.** The insufficient availability of term finance may hinder the ability of the financial sector in many developing countries to fund investments through medium-term to long-term loans targeting MSMEs and larger private projects. Donors address this problem by providing term resources on both commercial and concessional terms, including through the provision of lines of credit and/or equity funding and guarantees. Further, the lack of capacity and/or know-how at the level of the financial intermediaries as well as beneficiaries may affect implementation of lines of credit, equity and guarantee funds. Donors thus often use a small part of the resource envelope to provide complementary technical assistance.

Some of these programmes are quite broad in type and coverage. For example, Germany cooperates bilaterally with over 70 partner countries in over 200 programmes to advance financial sector development, including the banking sector. It is active in several international initiatives that aim at improving the overall banking system, e.g. Financial Sector Reform and Strengthening Initiative (FIRST), Alliance for Financial Inclusion (AFI), Consultative Group to Assist the Poor (CGAP, an independent policy and research centre dedicated to advancing financial access for the world's poor also funded by the EU), and Access to Insurance Initiative (A2II). Other EU Member States reported activities in these areas are:

- **Germany** co-chairs the working group on SME Finance in the G20 Global Partnership for Financial Inclusion, particularly aiming at improving access to finance for SMEs in developing countries also focusing on improving access for agricultural enterprises and women entrepreneurs. Germany contributes to the Partnership for Making Finance Work for Africa. Jointly with other donors, the regional MSME Fund for Sub-Saharan Africa (REGMIFA[105]) and SANAD[106] (set up in 2011, also with EU funding) in the MENA region aims to enhance long

[104] While there is a general agreement that guarantees link to a development project have a positive impact, the value of this approach if supply driven needs to be assessed on case by case basis.
[105] http://www.regmifa.com/
[106] http://www.microfinancegateway.org/p/site/m/template.rc/1.11.170553/

and medium financial needs of local financial intermediaries. The AATIF[107] fund invests in the agricultural sector in Africa with a focus on agricultural value chains. The European Fund for Southeast Europe[108] (EFSE) provides sustainable funding to entrepreneurs and private households in Southeast Europe.

- The **Austrian** Development Bank (OeEB) supports the private sector in developing countries by providing long-term finance on commercial terms. Particular attention is given to the financing of micro finance institutions in partner countries. Additional technical support to projects is funded separately, but usually linked to financing provided by OeEB.

- **Italy** provides grants and loans to support investments in developing countries including Lebanon, Serbia, Albania, Jordan, Tunisia, Afghanistan, India, Senegal, Ghana, Uruguay, Vietnam and Iraq.

- **Portugal** provides long-term finance for upgrade, expansion or new agricultural, industrial, tourism, infrastructural and financial projects from private companies, in Portuguese Speaking African countries, Northern Africa, Latin America and Asia.

- The **Danida** Business Finance[109] facility is an example of term credit that targets the infrastructure sector while promoting climate-friendly and clean technology development projects. A minimum investment of EUR 1 million is eligible and interest-free or low-interest loans are extended.

- **Luxembourg** provides TA to support activities and institutions in the financial sector.

- The **Belgian** Development Cooperation supports micro finance activities, notably in Morocco, Rwanda, Senegal and Vietnam. Latvia funds loans for the development MSMEs and Co-operative Unions Providing Agricultural Services. **Sweden** extends equity and loans also to SMEs primarily through the Swedish Swedfund.

- "The Currency Exchange" (TCX), supported by **Germany, France and others**, provides market risk management products in developing and emerging markets by focusing on currencies and maturities which are not covered by regular market providers.

- **Greece** provides subsidies to private productive investments in the framework of implementation of the "Hellenic Plan for the Economic Reconstruction of the Balkans".

- **Finnfund** is a Finnish development financing institution that offers long-term risk funding for commercially profitable investments in developing and transition countries.

- The **UK** uses a range of financial instruments to catalyse private investment in developing countries. Instruments include grants to support activities such as capacity building and seed funding channelled through their challenge funds; risk-sharing instruments including equity, debt and guarantees deployed through intermediaries such as the Private Infrastructure Development Group. The UK also supports private investment through shareholdings in CDC and the Investment Finance Corporation.

[107] http://www.rural21.com/english/news/detail/article/kfw-entwicklungsbank-and-deutsche-bank-launch-africa-agriculture-trade-and-investment-fund-aatif/
[108] http://www.efse.lu/
[109] http://um.dk/en/danida-en/activities/business/finance/

- **France** provides a guarantee fund for Sub-Saharan SMEs, which are estimated to have contributed to the creation of 90,000 jobs, as well as investment finance through FISEA[110] and AFD loans. AFD also supports upscaling of microfinance institution and downscaling of bank to better serve MSMEs.

3.2.1.3. Access to finance programmes

Most of the access to finance programmes aims to facilitate availability of financing to the MSME sector. Programmes reported by Member States are:

- The **Belgian** Development Cooperation supports micro finance activities, notably in Morocco, Rwanda, Senegal and Vietnam. Latvia funds loans for the development MSMEs and Co-operative Unions Providing Agricultural Services. Sweden extends equity and loans also to SMEs primarily through the Swedish Swedfund.

- **Germany** co-chairs the working group on SME Finance in the G20 Global Partnership for Financial Inclusion, particularly aiming at improving access to finance for SMEs in developing countries also focusing on improving access for agricultural enterprises and women entrepreneurs. Germany contributes to the Partnership for Making Finance Work for Africa. Jointly with other donors, the regional MSME Fund for Sub-Saharan Africa (REGMIFA[111]) and SANAD[112] (set up in 2011, also with EU funding) in the MENA region aims to enhance long and medium financial needs of local financial intermediaries. The AATIF[113] fund invests in the agricultural sector in Africa with a focus on agricultural value chains. The European Fund for Southeast Europe[114] (EFSE) provides sustainable funding to entrepreneurs and private households in Southeast Europe.

- **France** provides a guarantee fund for Sub-Saharan SMEs, which are estimated to have contributed to the creation of 90,000 jobs, as well as investment finance through FISEA[115] and AFD loans. AFD also supports upscaling of microfinance institution and downscaling of bank to better serve MSMEs.

3.2.1.4. Support for Public-Private Partnerships for the delivery of goods and services

A Public-Private Partnership (PPP) is a partnership between the public and the private sector for the purpose of delivering a project or a service traditionally provided by the public sector. PPPs leverage private funding, can draw on the operational efficiencies of the private sector, allow faster implementation and can enhance the quality of the service delivered. **PPPs may be especially important in poorer countries where over-extended governments do not have the human resources and fiscal space to fulfil the requirements of their growing economy**. It should be noted that PPPs can take many forms, ranging from private investment in the sector concerned and private provision of service, with regulatory oversight provided by a specialised public institution, to some type of "enhanced lease" where the operator is only responsible for service delivery and part of the maintenance. Another feature of PPPs is that they are typically time-bound. PPPs are usually undertaken in infrastructure, even though there is growing opportunities in social sectors and other developmental activities.

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110 http://www.proparco.fr/lang/en/Accueil_PROPARCO/fisea-proparco
111 http://www.regmifa.com/
112 http://www.microfinancegateway.org/p/site/m/template.rc/1.11.170553/
113 http://www.rural21.com/english/news/detail/article/kfw-entwicklungsbank-and-deutsche-bank-launch-africa-agriculture-trade-and-investment-fund-aatif/
114 http://www.efse.lu/
115 http://www.proparco.fr/lang/en/Accueil_PROPARCO/fisea-proparco

The Private Infrastructure Development Group (PIDG) is a multidonor organisation[116], including Austria, Germany, Ireland, Netherlands, Sweden and UK. It was established in 2002 to promote private participation in infrastructure in developing countries with a strong focus on Africa. It provides long-term capital and local currency guarantees, and TA. **The Public-Private Infrastructure Advisory Facility** (PPIAF)[117] is a multi-donor technical assistance facility, set up in 1999 and financed by 17 multilateral and bilateral donors including Austria, France, Germany, Italy, Netherlands, Sweden, and United Kingdom. It is a complementary scheme to deliver technical assistance to developing country governments.

In terms of bilateral initiatives, AFD supports PPPs through funding of concessions and enhanced leases, including in the education and vocational training sector. Complementary TA may also be provided. The UK is investing £130 million in a Climate Public Private Partnership (CP3). CP3 will support projects delivering renewable and efficient energy, new technology and protect natural resources in emerging and developing countries including Africa and Asia.

3.2.1.5. Other partnerships

Complementary measures used by donors to promote private investments include matching-grants and match-making for know-how and technological acquisitions and upgrading, and technical assistance and studies. The following related activities have been reported by Member States:

- **German** Development Cooperation co-finances feasibility studies and accompanying measures for foreign direct investments in developing countries. It also supports foreign direct investments by SMEs and PPPs through subsidies to cover the administrative costs for advisory services, project review, etc.

- **Danida's** Business Partnerships, Finnpartnership and Austria partnership initiative facilitate the establishment of commercial partnerships that have a significant impact on development in poor communities.

- The **Finnish** business-to-business partnership programme allocates funding for long-term partnerships between Finnish and developing country entities, normally companies. Partnerships must contribute to development. Forms of business partnerships are e.g. long-term trade partnership, investment and joint venture.

- **France** provides grants funded TA complementary to investment projects, as well as various TA to financial institutions. Capacity building is offered to enterprises, including upgrading to international norms, and for trade.

3.2.2. Corporate Social Responsibility (CSR)

CSR concerns the impact of companies on society. It has become an increasingly important concept and is part of the debate about globalisation, climate change, competitiveness and social and environmental sustainability. CSR practices are not a substitute for public policy, but they can

[116] current members are: the UK Department for International Development (DFID), the Swiss State Secretariat for Economic Affairs (SECO), the Netherlands Ministry of Foreign Affairs (DGIS), the Swedish International Development Cooperation Agency (Sida), the World Bank Group (currently represented by IFC), the Austrian Development Agency, Irish Aid, KfW of Germany and the Australian Agency for International Development (AusAID). Source: http://www.pidg.org/sitePages.asp?step=4&navID=2&contentID=10

[117] http://www.ppiaf.org/ppiaf/

contribute to a number of public policy objectives in developing countries, especially in relation to labour markets, labour standards, skills development, more rational use of natural resources and overall poverty reduction. Developing countries benefit from good practices in CSR in a number of ways notably through the better quality of development and increased private and public financial flows.

3.2.2.1. A renewed EU Policy on Corporate Social Responsibility

On 25 October 2011 the European Commission issued a new CSR Communication[118] which was welcomed by the Council of the European Union in its Conclusions on "Reinforcing Industrial Policy in the EU".[119] In particular, the Council encouraged Member States to develop or update their plans and/or priority actions in this area, and recognised CSR as a voluntary assumption of social responsibility.

The CSR Communication states that to fully meet their social responsibility, enterprises *"should have in place a process to integrate social, environmental, and ethical and human rights concerns into their business operations and core strategy in close collaboration with their stakeholders"*. The aim is both to enhance positive impacts – for example through the innovation of new products and services that are beneficial to society and enterprises themselves – and to minimise and prevent negative impacts.

The Communication puts forward an action agenda for the period 2011-2014 covering 8 areas:

- Enhancing the visibility of CSR and disseminating good practices.
- Improving and tracking levels of trust in business.
- Improving self- and co-regulation processes.
- Enhancing market reward for CSR by leveraging EU policies in relevant fields.
- Improving company disclosure of social and environmental information.
- Further integrating CSR into education, training and research.
- Emphasising the importance of national and sub-national CSR policies: EU Member States to present or update their own plans for the promotion of CSR by mid-2012[120].
- Better aligning European and global approaches.

The new European strategy on CSR makes reference to a number of international initiatives. Among these are the OECD Guidelines for Multinational Enterprises. The Guidelines[121] were updated in 2011 and include chapters on human rights, due diligence and responsible supply chain management, and important changes in many specialised chapters, such as on Employment and Industrial Relations; Combating Bribery, Bribe Solicitation and Extortion, Environment, Consumer Interests, Disclosure and Taxation. There is also guidance to strengthen the mediating role of the

[118] COM(2011) 681 final, A renewed EU strategy 2011-14 for Corporate Social Responsibility, http://ec.europa.eu/enterprise/policies/sustainable-business/files/csr/new-csr/act_en.pdf
[119] http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/en/intm/126548.pdf
[120] See compendium of CSR Policies in the EU as of end-2010 in: CSR - National Public Policies in the European Union, dated November 2010. Further insights may be found in a report by CSR Europe (network of 70 multinationals and 27 partner organizations) dated October 2010. http://ec.europa.eu/social/main.jsp?catId=331&langId=en and http://www.reportingcsr.org/force_document.php?fichier=document_495.pdf&fichier_old=guide_to_csr_2010[1].pdf
[121] OECD guidelines for multinational enterprises, 2011 edition; http://www.oecd.org/dataoecd/43/29/48004323.pdf

National Contact Points and a pro-active implementation agenda. EU and some Member States contributed to this document.[122]

Other important international initiatives to which the European Commission participates, are the UN Guiding Principles on business and human rights[123] (the "protect, respect, remedy" framework), in respect of which the Commission will provide a priorities report for the end of 20120), the ILO Tripartite Declaration on Multinational Enterprises and Social Policy[124], and the UN's Global Compact.[125]

3.2.2.2. Update on activities relating to CSR

The EU and a majority of Member States undertook/continued national action to promote CSR principles, and 15 of them, including the Commission, report on-going or new activities in this area. In addition to areas already reported in the 2011 Accountability Report, there are a variety of other activities with important contribution to the financing for development agenda supported by Member States:

The UK food retail Industry Challenge Fund aims to increase African farmers and farm worker incomes through access to international food supply chains, including ethical and fair trade. The UK also expanded the operations of the Business Innovation Facility with an increased focus on lesson learning on inclusive business.

The Austrian Government supports private sector projects on CSR activities and on setting up/strengthening of value chains.

The Netherlands funds a small pilot-programme for 50 international CSR-vouchers. These vouchers give SME's a reduction (50% with a maximum of EUR 10,000) in the fee of a CSR-consultant for advice on how to encourage CSR in the supply chain in developing countries.

Initiatives contributing to better aligning approaches to CSR included (a) UN Global Compact; continued support to its secretariat was provided by Denmark, mandate of local group was renewed by Latvia, and Italy hosted a meeting of local European Networks; (b) the UN Guiding Principles signed by Spain in 2011; and (c) the ISO 26000; capacity building in this area in favour of 19 Latin America countries was funded by Germany in November 2011 and self-evaluation was undertaken by 50 Latvian enterprises.

Strategic, training and dissemination activities by Member States during 2011 included: (a) an Organisational Capacity Assessment Instrument (OCAI) to support companies in Germany and worldwide to adopt the new UN-principles on business and human rights, and the promotion of the new OECD-Guidelines for Multinational Companies in German; (b) approval of the work plan for the Spanish CSR working group; (c) Employers' Confederation of Latvia with support of organised business society and European Social Fund organised a social campaign "Against shadow economy – for business competitiveness; and (d) national strategy to promote CSR, for the period 2011-2016 has been adopted by the Romanian Government.

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[122] For example, France reports that it advocated the introduction of a comprehensive approach to due diligence and responsible supply chain management.

[123] http://www.un.org/apps/news/story.asp?NewsID=38742&Cr=human+rights&Cr1=

[124] http://www.ilo.org/wcmsp5/groups/public/---ed_emp/---emp_ent/documents/publication/wcms_094362.pdf

[125] http://www.unglobalcompact.org/

The EU is in the process of funding the fourth tranche of the SWITCH Asia Programme.[126] Its aim is to promote Sustainable Consumption and Production (SCP) in Asia so as to minimise the use of natural resources and the emissions of greenhouse gases, waste and other pollutants. To achieve this objective, the Programme works simultaneously on the ground, with producers and consumers, and at the level of policy-making through supporting for formulation and implementation of SCP-related policies. The allocation of the present tranche is about EUR 30 million. So far, the Programme is funding 47 projects in 15 Asian countries in areas such as Green Public Procurement, Cleaner Production, Eco-labelling, etc. Each of the funded projects will bring about quantifiable reductions of CO2 emissions and resource, water and energy consumption. In the area of policy enhancement four countries have already gathered experience in applying SCP tools. An example of this programme is illustrated in Box 3.2.2.2 below.

Box 3.2.2.2 Green Philippines Islands of Sustainability (GPIoS)[127]

The key objectives of GPIoS are to minimise the environmental impacts caused by SME's in the target region (Metro Manila and the Calabarzon region), by adopting preventive environmental production and to integrate sustainable growth, social progress and environmental protection within the businesses of participating companies. Partnership agreement was signed between GPIoS and Plantersbank last December 14, 2011.

GPIoS will serve as a tool to increase profitability while being environmentally friendly, making SMEs more bankable. Results of the project show significant financial and environmental benefits:

– Total energy savings can light up 47, 367 street lamps during one year 12 hours each day
– The amount of water savings can fill 256 Olympic sized pool
– The amount of waste avoided can fill up 23 garbage trucks
– Return of Investment = 0.8 and Payback time of 9.6 months

[126] http://ec.europa.eu/europeaid/where/asia/regional-cooperation/environment/switch_en.htm
[127] http://www.switch-asia.eu/switch-projects/project-progress/projects-on-greening-supply-chains/creating-greenphilippines-islands-of-sustainability.html

4. INTERNATIONAL DEVELOPMENT FINANCE: EU SUPPORT TO GLOBAL GOALS

4.1. Scaling up Official Development Assistance (ODA)[128]

EU Commitments

● *In 2002, the EU Member States adopted joint commitments on ODA increases. These commitments were further developed and broadened, and endorsed by the European Council in 2005 ahead of the UN World Summit that undertook the first review of progress on the Millennium Declaration and the MDGs. The EU and its Member States agreed to achieve a collective ODA level of 0.7% of GNI by 2015 and an interim target of 0.56% by 2010, both accompanied by individual national targets. The EU Member States agreed to increase their ODA to 0.51% of their national income by 2010 while those countries which had already achieved higher levels (0.7% or above) promised to maintain these levels. The Member States that acceded to the EU in or after 2004 (EU-12) promised to strive to spend 0.17% of their GNI on ODA by 2010 and 0.33% by 2015.*[129]

● *In addition the EU committed in 2005 to: (a) increase ODA to Sub-Saharan Africa and (b) provide 50% of the ODA increase to Africa as a whole (North Africa and Sub-Saharan Africa).*

● *In 2008 the EU as a whole also committed to provide between 0.15 and 0.20% ODA/ GNI to the Least Developed Countries by 2010.*[130]

4.1.1. EU ODA Commitments in the Global Context

Although the goal of allocating annually 0.7% of GNI to ODA is accepted by all DAC donors except the United States of America, only EU donors and Norway have set a date to achieve it, transforming the long-standing UN 0.7% goal, considered by many as aspirational, into a realistic, time-bound target. The EU decided to move forward and achieve this goal in steps within 15 years (2000 – 2015), in line with the deadlines of the Millennium Declaration and based on a mix of individual and collective intermediate targets. The first intermediate EU ODA objectives were defined in 2002 during the preparation for the Monterrey International Conference on Financing for Development, based on the EU's ODA levels in 2000.

[128] Depending on data availability, the text sometimes refers to EU15 and EU20, which can nevertheless be taken as approximations of the EU's collective performance. For explanations, see Annex 2: Methodology.

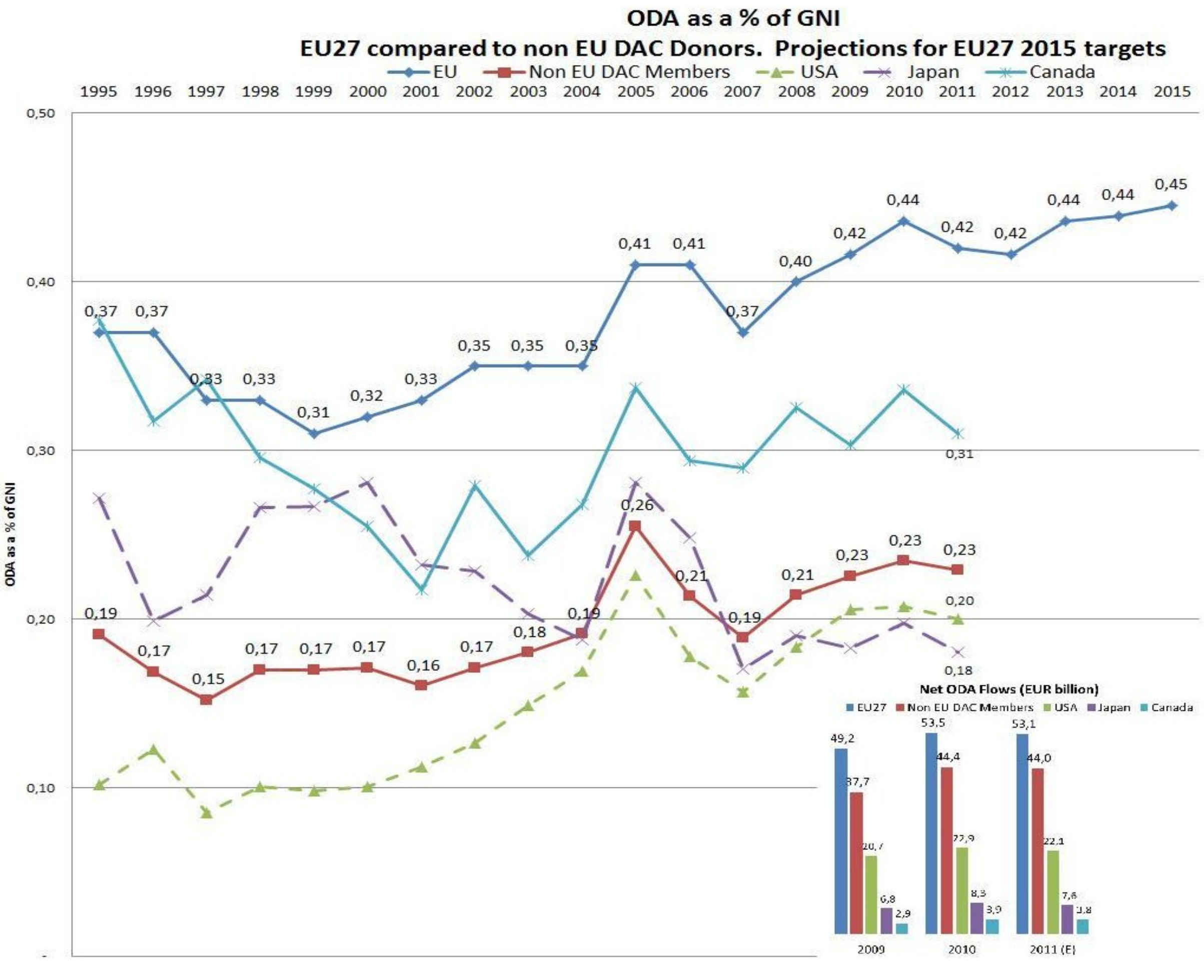
[129] The exact wording is as follows: 'In the context of the commitment to attain the internationally agreed ODA target of an ODA/GNI ratio of 0.7%, the European Council notes with satisfaction that its Member States are on track to achieve the 0.39% target of GNI in 2006 for ODA volumes contained in the Barcelona commitments. While reaffirming its determination to fulfil these commitments, the Council decided on a new collective European Union target of an ODA/GNI ratio of 0.56% by 2010. That would result in an additional EUR20 billion a year in ODA. In this context, the European Council can reiterate, in accordance with the outcome of the Council on 24 May 2005 that Member States, which have not yet achieved an ODA/GNI ratio of 0.51% undertake to attain that level, within their respective budget allocation processes, by 2010, while those that are already above that level undertake to continue their efforts. Member States which joined the EU after 2002, and have not yet achieved an ODA/GNI ratio of 0.17%, will endeavour to increase their ODA to attain that level, within their respective budget allocation processes, by 2010, while those that are already above that level undertake to continue their efforts; Member States undertake to achieve the target of an ODA/GNI ratio of 0.7% by 2015, while those which have achieved that target commit themselves to remaining above that target; Member States which joined the EU after 2002 will endeavour to increase their ODA/GNI ratio to 0.33% by 2015. European Council, 18 June 2005, Doc. 10255/05 Conc. 2.

[130] European Council, 11 November 2008, Doc. 15075/1/08, Rev. 1

4.1.2. EU ODA Performance 2005-2011 compared to other donors

The EU has not only pledged to deliver more aid, but its combined efforts are already delivering substantially greater amounts of ODA than non EU donors, and individual EU countries (with a few exceptions) are also making more substantial efforts in relative terms.

Figure 4.1.2 –ODA/GNI by Donor (% and EUR million, current prices)



Source: OECD DAC and European Commission

As shown in **Figure 4.1.2** and **Table 4.1.2**, both **the EU's per capita ODA and its ODA/GNI ratios are greater than those of non-EU DAC Members**. Indeed, its ODA/GNI ratio is more than double that of Japan and the USA. Collectively, the EU outperforms most other donors by a wide margin. The USA, Japan and Switzerland have higher per capita income than rge average for EU Member States but much lower per capita ODA. The US GNI is close to 90 % of the EU27 GNI, but US ODA is only 40 % of EU ODA. It is clear that most of the gap to achieving the global 0.7 % target is outside the EU.

Table 4.1.2 – ODA/GNI and ODA per capita of EU Member States and Non-EU DAC Members

Donor	ODA per capita (EUR)			ODA/GNI (%)			ODA (EUR Billion)		
	2009	2010	2011	2009	2010	2011 (E)	2009	2010	2011 (E)
EU	98	107	105	0.42	0.44	0.42	49.2	53.5	53.1

Non EU DAC Members	68	79	78	0.23	0.23	0.23	37.7	44.4	44.0
USA	67	74	71	0.21	0.21	0.20	20.7	22.9	22.1
Japan	53	65	60	0.18	0.20	0.18	6.8	8.3	7.6
Canada	85	115	111	0.30	0.34	0.31	2.9	3.9	3.8

Source: OECD DAC/European Commission

4.1.3. Performance on ODA targets (2005-2011)

ODA figures on 2011 net disbursements are preliminary, based on information provided by EU Member States and the European Commission. For those EU Member States that report to the OECD/ DAC final and more comprehensive ODA figures will become available towards the end of 2012.

The EU collective ODA spending in 2011 was EUR 53,1 billion, which translates into the ODA/GNI ratio decline from 0.44% in 2010 to 0.42%.[131] The reduction in absolute terms was of EUR 342 million.

Since making its ODA commitments in 2002, EU ODA has seen fluctuations, but overall has been on an upward trend. The growth of EU ODA is especially significant if one considers the declining importance of debt relief in the overall ODA effort of EU Member States. Over the period 1995-2011, EU15 ODA net of debt relief grew by 0.07% of GNI from 0.34% in 1995 to 0.41% in 2011.

Since 2008, the financial crisis has hit EU Member States hard, triggering the deepest global economic recession in decades. State-financed rescue packages for the affected banking sector, higher social protection costs and lower budget revenues have dramatically changed the fiscal situation in many Member States. Low or negative economic growth rates in the EU as a consequence of the crisis, and the related austerity measures that Member States introduced, led to different pressures on ODA. Due to economic contraction, the aid level could appear higher when expressed as a percentage of GNI, but provides no additional ODA funding for developing countries.

Also, lower GNI growth combined with need for higher public expenditure elsewhere led to restrictions to spending on development cooperation. Through the first three years of the crisis, the EU continued aid increases, but succumbed to the pressure in 2011, resulting in a lower trajectory of scaling up to meet 2015 targets.

The 2011 decline in ODA by EUR 342 million was the outcome of mixed performance by Member States. Eleven Member States reduced their ODA by a total of EUR 2.5 billion, while sixteen Member States increased their ODA in nominal terms by a total of EUR 2.2 billion. **The biggest cuts in nominal terms** were in Spain (1.4 billion), France (400 million), Belgium (250 million) and Greece (EUR 145 million). **As a proportion of 2010 ODA**, biggest cuts were in Greece (38%), Spain (32%) and Cyprus (29%).

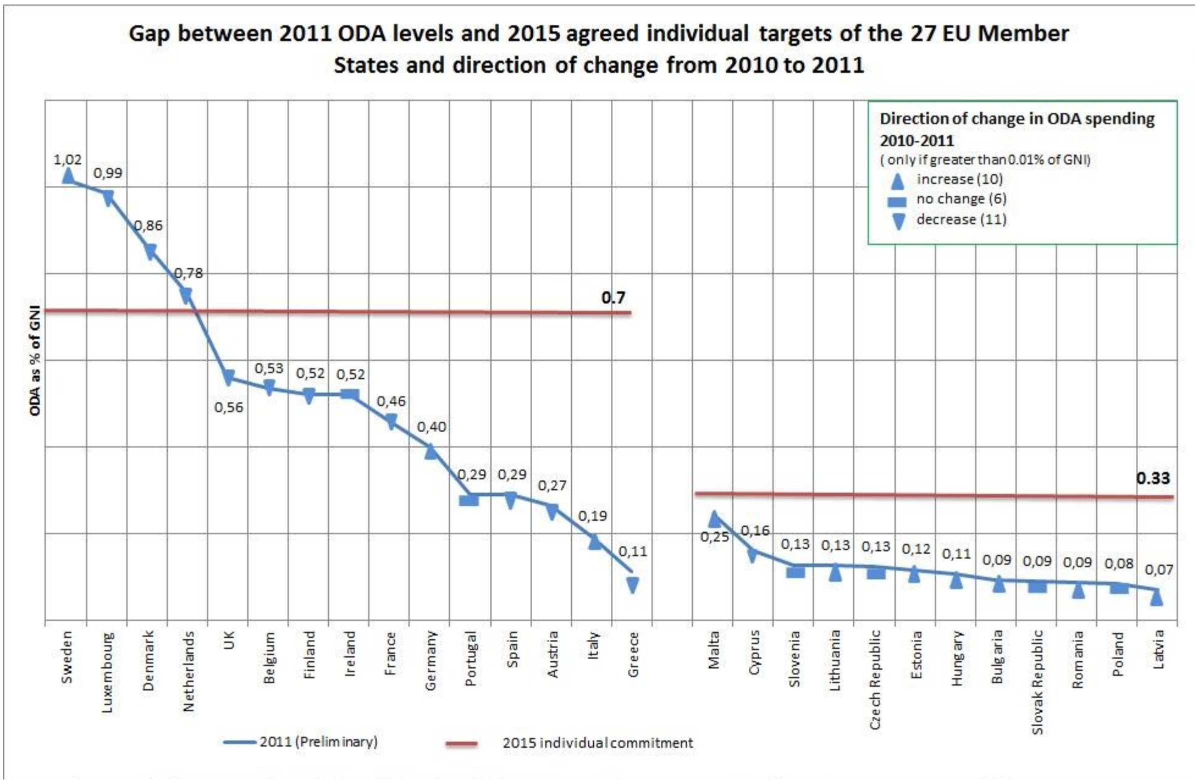
Biggest increases in nominal terms were in Italy (EUR 788 million), Germany (EUR 648 million) and Sweden (EUR 609 million). The ODA/GNI ratios of Germany and Italy are, respectively, over

[131] The final 2010 ODA/GNI ratio of 0.44% is 0.01 higher than the estimated ratio included in the 2011 EU Accountability Report due to revised GNI statistics.

20% and almost 70% below their individual targets for 2010. **As a proportion of 2010 ODA,** biggest increases were in Malta (43%), Romania (37%), Lithuania and Italy (35% both). We can note that all EU12 with the exception of Cyprus have either raised or maintained their aid levels, in part due to the fact that several contributed to the EDF for the first time.

Looking at overall developments since 2004, all countries except Portugal and Greece saw their ODA/GNI ratio grow between 2004 and 2011 (see **Annex 3** for details). For Germany, UK, Lithuania, Bulgaria, Romania, Malta, Estonia, 2011 was the highest or very close to the highest ODA/GNI ratio in the period. Sweden, Luxembourg, Belgium, Finland, Ireland, Cyprus had grown above their 2011 level and then back-tracked a little but progress since 2004 has remained substantial. Denmark, Netherlands, France, Poland had grown above their 2011 level and then *back-tracked a little*, with limited progress since 2004; Denmark and France had gone below their 2004 level and recovered. ODA/GNI ratios of Spain, Austria, Italy grew well above their 2011 level and then *back-tracked substantially* so that progress since 2004 has been limited.

Figure 4.1.3 – Gap between 2015 targets and 2011 results



Source: OECD DAC and European Commission (EU annual questionnaire on financing for development)

In 2011, the EU Member States stand in different position with regard to 2015 target. Four EU Member States (Sweden, Denmark, the Netherlands and Luxembourg) continue to exceed the 0.7% target, with Denmark, Luxembourg and Sweden aiming to reach 1% of GNI by 2015. Despite stalling in 2011, the UK with 0.56% is above the linear track from 2010 target towards the 0.7% target. Belgium, Finland and Ireland are above the 2010 target of 0.51% of GNI, but below the linear track. With the exception of Malta, no EU12 Member State is above the 2010 ODA target (see figure Figure 4.1.3).

4.1.4. *Achievement of the 0.7% ODA/GNI Target by 2015*

Based on the projections provided by Member States and/or estimates prepared using their 2006-2011 compound annual growth rate,[132] the EU27 ODA is expected to increase to 0.44% by 2015. Considering the expected GNI growth rate till 2015, reaching the 0.7% ODA/GNI target would require the EU and its Member States to dramatically step up efforts and almost double their current ODA in nominal terms. **Figure 4.1.4** below shows the long-term trends in ODA volumes for the EU27. At the current pace, there is a delay equivalent to about 25 years on the path to 0.7%, as ODA is projected to increase at an annual rate of 0.01% of GNI.

The EU scaling-up process has been uneven, with asymmetric efforts. Those Member States not contributing their fair share to the burden-sharing effort have kept the collective EU performance below the targets, and would also need to make the greatest efforts to reach the 2015 targets.

Table 4.1.4a: Estimates and gaps to be bridged for reaching the 2015 ODA targets, based on Member States' forecast information and Commission simulation

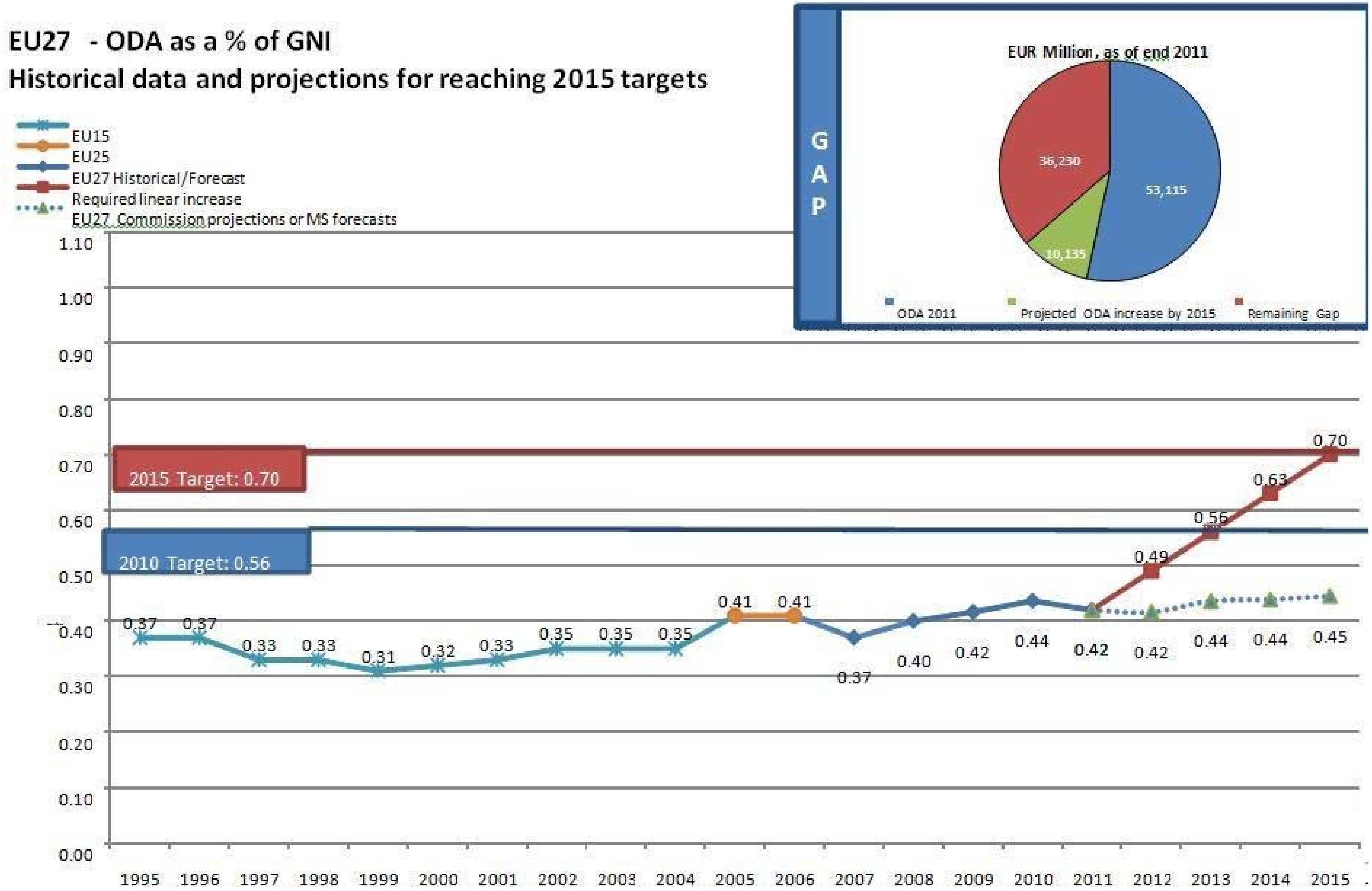
Member State	2010		2011 (preliminary)		2012 (forecast/ simulation)		2013 (forecast/ simulation)		2014 (forecast/ simulation)		2015 (forecast/ simulation)		2015 (commitments)		2015: Gap to meet national targets from 2011 level
	EUR Million	% of GNI	EUR Million	% of GNI	EUR Million	% of GNI	EUR Million	% of GNI	EUR Million	% of GNI	EUR Million	% of GNI	EUR Million	% of GNI	EUR million
Austria	912	0,32	796	0,27	1 469	0,47	1 361	0,42	1 523	0,46	1 404	0,41	2 384	0,70	1 587
Belgium	2 268	0,64	2 014	0,53	2 172	0,56	2 040	0,51	2 083	0,50	2 972	0,70	2 977	0,70	964
Bulgaria	31	0,09	35	0,09	36	0,09	43	0,10	51	0,12	61	0,14	149	0,33	114
Cyprus	39	0,23	28	0,16	29	0,16	30	0,16	32	0,17	32	0,16	65	0,33	37
Czech Republic	172	0,13	184	0,13	184	0,13	182	0,12	194	0,13	209	0,13	533	0,33	349
Denmark	2 168	0,91	2 144	0,86	2 093	0,82	2 189	0,83	2 240	0,83	2 324	0,84	2 782	1,00	638
Estonia	14	0,10	18	0,12	21	0,13	23	0,14	27	0,15	30	0,17	60	0,33	42
Finland	1 006	0,55	1 013	0,52	1 124	0,56	1 129	0,54	1 134	0,52	1 160	0,52	1 563	0,70	550
France	9 751	0,50	9 345	0,46	10 461	0,51	10 168	0,48	10 376	0,48	10 588	0,47	15 657	0,70	6 312
Germany	9 804	0,39	10 452	0,40	10 728	0,40	11 230	0,41	11 757	0,42	12 307	0,42	20 288	0,70	9 836
Greece	383	0,17	238	0,11	222	0,11	207	0,10	193	0,09	180	0,08	1 548	0,70	1 310
Hungary	86	0,09	101	0,11	99	0,11	100	0,10	100	0,10	100	0,10	341	0,33	241
Ireland	676	0,52	650	0,52	639	0,51	644	0,50	697	0,52	699	0,50	978	0,70	328
Italy	2 262	0,15	3 050	0,19	1 880	0,12	2 755	0,17	2 783	0,17	2 811	0,16	12 086	0,70	9 036
Latvia	12	0,06	14	0,07	16	0,07	17	0,08	18	0,08	20	0,08	79	0,33	65
Lithuania	28	0,10	38	0,13	43	0,14	48	0,14	55	0,16	62	0,17	118	0,33	81
Luxembourg	304	1,05	297	0,99	295	1,00	306	1,00	316	1,00	328	1,00	328	1,00	31
Malta	10	0,18	14	0,25	16	0,27	18	0,29	20	0,31	22	0,33	22	0,33	8
The Netherlands	4 800	0,81	4 698	0,78	4 424	0,72	4 463	0,70	4 674	0,71	4 917	0,72	4 781	0,70	83
Poland	285	0,08	300	0,08	309	0,08	325	0,08	341	0,08	357	0,08	1 389	0,33	1 089
Portugal	490	0,29	481	0,29	471	0,29	513	0,31	558	0,33	607	0,35	1 219	0,70	738
Romania	86	0,07	118	0,09	125	0,09	136	0,09	148	0,09	161	0,10	538	0,33	420
Slovak Republic	56	0,09	62	0,09	69	0,10	66	0,09	67	0,09	69	0,09	260	0,33	198
Slovenia	44	0,13	45	0,13	51	0,14	54	0,15	59	0,16	65	0,16	130	0,33	85
Spain	4 492	0,43	3 067	0,29	2 405	0,23	2 409	0,22	2 414	0,21	2 418	0,21	8 136	0,70	5 069
Sweden	3 423	0,97	4 032	1,02	4 058	0,98	4 248	0,99	4 462	1,00	4 688	1,02	4 587	1,00	555
UK	9 855	0,57	9 881	0,56	10 613	0,56	13 688	0,70	14 135	0,70	14 659	0,70	14 659	0,70	4 778
EU 15 TOTAL	**52 594**	**0,46**	**52 159**	**0,45**	**53 053**	**0,44**	**57 351**	**0,46**	**59 343**	**0,47**	**62 064**	**0,47**	**93 973**	**0,72**	**41 814**
EU 12 TOTAL	**863**	**0,09**	**957**	**0,10**	**997**	**0,10**	**1 043**	**0,10**	**1 111**	**0,10**	**1 187**	**0,11**	**3 685**	**0,33**	**2 729**
EU 27 TOTAL	**53 457**	**0,44**	**53 115**	**0,42**	**54 050**	**0,42**	**58 394**	**0,44**	**60 454**	**0,44**	**63 251**	**0,45**	**97 658**	**0,69**	**44 543**

Gap to collective 2015 target 0.7%	
Target in EUR million:	99 481
Gap in EUR million	46 366

Shaded cells are Commission estimates

[132] **Annex 2** outlines the methodology used to analyse ODA indicators and forecasts provided by Member States.

Figure 4.1.4 - EU 27 ODA/GNI Ratios (1995-2015)



Source: OECD DAC and European Commission (EU annual questionnaire on financing for development)

Table 4.1.4a shows the projections and the sometimes drastic increases needed by individual Member States in their budgets of 2012-2015. For example, to reach the 2015 target Latvia and Greece would need to sextuple their current ODA volumes over the next four years, Poland and Romania quintuple; Bulgaria, Italy, and the Slovak Republic would need to quadruple; and Austria, the Czech Republic, Estonia, Hungary, Lithuania, Portugal, Slovenia and Spain would need to triple their aid allocations.

The projections confirm that Member States do not plan to make these increases under the current tight budget conditions. 20 Member States provided some projections for their ODA in the coming years and 13 have provided projections up to 2015. Excluding 4 Member States that are already above 0.7% ODA/GNI, only Belgium, Malta and the United Kingdom foresee reaching their 2015 targets. Of the other 20 Member States, we foresee either lower pace of increases or even decreases, remaining far from the 2015 target. Based on these indications and the Commission projections, we expect 17 Member States to at least marginally increase their ODA/GNI ratio by 2015, however remaining far from reaching their individual targets.

For 2012, the projections based on Member Sates' replies or budget data available online, point to a stagnation in ODA budgets. This is due in great part to significant ODA budget cuts in Spain, Italy, and the Netherlands (in order of magnitude), only partially compensated by relevant projected increases in the United Kingdom, France, and Austria ODA allocations. The expected rebound in subsequent years is largely based on the positive average trend of 2006-2011.

The ODA graphs in **Annex 3** show each EU Member State's readiness to meet the individual ODA target levels of 0.7% and 0.33% of GNI for EU15 and EU12 respectively in 2015, as well as the size of the gap and how much is likely to be filled by 2015.

There are several factors that reduce the likelihood of achieving the 2015 target under the *status quo*:

First, the **reduced ambition** of some national plans has had a real impact on collective progress on ODA. Some of the more ambitious Member States have reduced their targets compared to the ones that formed the basis for the 2005 Council Conclusions. Most of the Member States do not plan for reaching their individual targets.

Second, the **current fiscal crunch** has led some countries to revise downwards their commitments and targets. **Spain**, after increasing ODA substantially until 2009, has reduced its ODA in 2010 and 2011 and announced a further reduction of EUR 1.3 billion for 2012. After remaining above 0.80% since 2005, the **Netherlands** is reducing its ODA target to 0.70%. **Italy** has consistently missed targets and its aid has been declining for most of the past decade. Net of debt relief, Italy's ODA is projected to remain essentially unchanged in nominal terms (below EUR 2 billion per year) between 2012 and 2013 at already minimal levels.

Third, **back-loading the increase in ODA expenditure** has been one of the main factors in missing target levels. Experience shows that missing intermediate targets in a significant way leads to missing subsequent targets too. A good example is provided by the Member States that significantly missed the 2006 target of 0.33% GNI: **Greece, Italy and Portugal**. Once the target was missed, statements were made that the 2006 target would be achieved by 2007 or 2008. In reality, the 2006 target has not been met by any of them even by 2010 and these three Member States ended up missing both the 2006 and the 2010 targets.

Fourth, **reaching the EU ODA targets is contingent** not only on the medium-sized donors, but also **on EU countries with large economies** such as France, Germany, Italy and the UK to boost average aid levels so as to reach targets. These countries account for almost 70% of the gap to be filled between 2010 and 2015. If the EU as a whole is to meet the collective target of 0.7% ODA/GNI by 2015, it is imperative that all the big players step up their efforts, whereas only the **United Kingdom** has so far committed to do so.

Table 4.1.4b below shows the funding gap between the 0.7% target and the current level of ODA from EU Member States. It is clear that unless decisive action is taken, the 2015 target will be missed by a large margin.

Table 4.1.4b - Gap between 2011 ODA levels and 0.7% and 0.33% ODA/ GNI individual targets, by Member State

Member State	**ODA 2011**		**Projected increase in ODA by 2015**	**Remaining gap to national targets**		**Total ODA in 2015 to meet national targets**	
	EUR Million	*% of GNI*	*EUR Million*	*EUR Million*	*% of gap*	*EUR Million*	*% of GNI*
Austria	796	*0,27*	608	979	*2,7*	2 384	*0,70*
Belgium	2 014	*0,53*	958	6	*0,0*	2 977	*0,70*
Bulgaria	35	*0,09*	26	88	*0,2*	149	*0,33*
Cyprus	28	*0,16*	5	33	*0,1*	65	*0,33*
Czech Republic	184	*0,13*	24	325	*0,9*	533	*0,33*
Denmark	2 144	*0,86*	180	457	*1,2*	2 782	*1,00*
Estonia	18	*0,12*	12	30	*0,1*	60	*0,33*
Finland	1 013	*0,52*	147	403	*1,1*	1 563	*0,70*
France	9 345	*0,46*	1 243	5 069	*13,8*	15 657	*0,70*
Germany	10 452	*0,40*	1 855	7 981	*21,7*	20 288	*0,70*
Greece	238	*0,11*	- 58	1 368	*3,7*	1 548	*0,70*
Hungary	101	*0,11*	- 1	242	*0,7*	341	*0,33*
Ireland	650	*0,52*	49	280	*0,8*	978	*0,70*
Italy	3 050	*0,19*	- 239	9 275	*25,2*	12 086	*0,70*
Latvia	14	*0,07*	6	59	*0,2*	79	*0,33*
Lithuania	38	*0,13*	25	56	*0,2*	118	*0,33*
Luxembourg	297	*0,99*	31	-	-	328	*1,00*
Malta	14	*0,25*	8	-	-	22	*0,33*
The Netherlands	4 698	*0,75*	471	- 238	*- 0,6*	4 930	*0,70*
Poland	300	*0,08*	57	1 032	*2,8*	1 389	*0,33*
Portugal	481	*0,29*	125	613	*1,7*	1 219	*0,70*
Romania	118	*0,09*	43	377	*1,0*	538	*0,33*
Slovak Republic	62	*0,09*	6	192	*0,5*	260	*0,33*
Slovenia	45	*0,13*	19	65	*0,2*	130	*0,33*
Spain	3 067	*0,29*	- 1 317	6 386	*17,4*	8 136	*0,70*
Sweden	4 032	*1,02*	657	- 102	*- 0,3*	4 587	*1,00*
UK	9 881	*0,56*	4 778	-	-	14 659	*0,70*
Total EU MS	**53 115**	***0,42***	**9 719**	**34 974**	***95,0***	**97 808**	***0,69***
Unassigned gap to collective target				1 823	*5,0*	1 823	*0,01*
EU27	**53 115**	***0,42***	**9 719**	**36 797**	***100,0***	**99 631**	***0,70***

Source: OECD DAC and European Commission (EU annual questionnaire on financing for development)

4.1.5. The Way Forward

The European Union and its Member States have repeatedly reiterated their commitments to achieve the 0.7% ODA to GNI ratio by 2015, as a concrete, time-bound goal. The rationale for a time-bound target was to provide adequate funding to achieve the Millennium Development Goals. This was not solely an act of solidarity but a strategy to tackle the root causes of poverty and fragility before they spiral out of control, generating refugee flows and security threats. It was also designed to face challenges that know no boundaries and that affect the entire planet, such as climate change, loss of biodiversity, desertification or the spread of infectious diseases. EU Heads of State and Government confirmed that ODA remains an important element of the EU support to developing countries, and repeatedly reaffirmed their commitment to reaching the individual and collective ODA targets by 2015. At the same time, the Council has not agreed any concrete measures to ensure the national steps necessary for fulfilling this commitment.

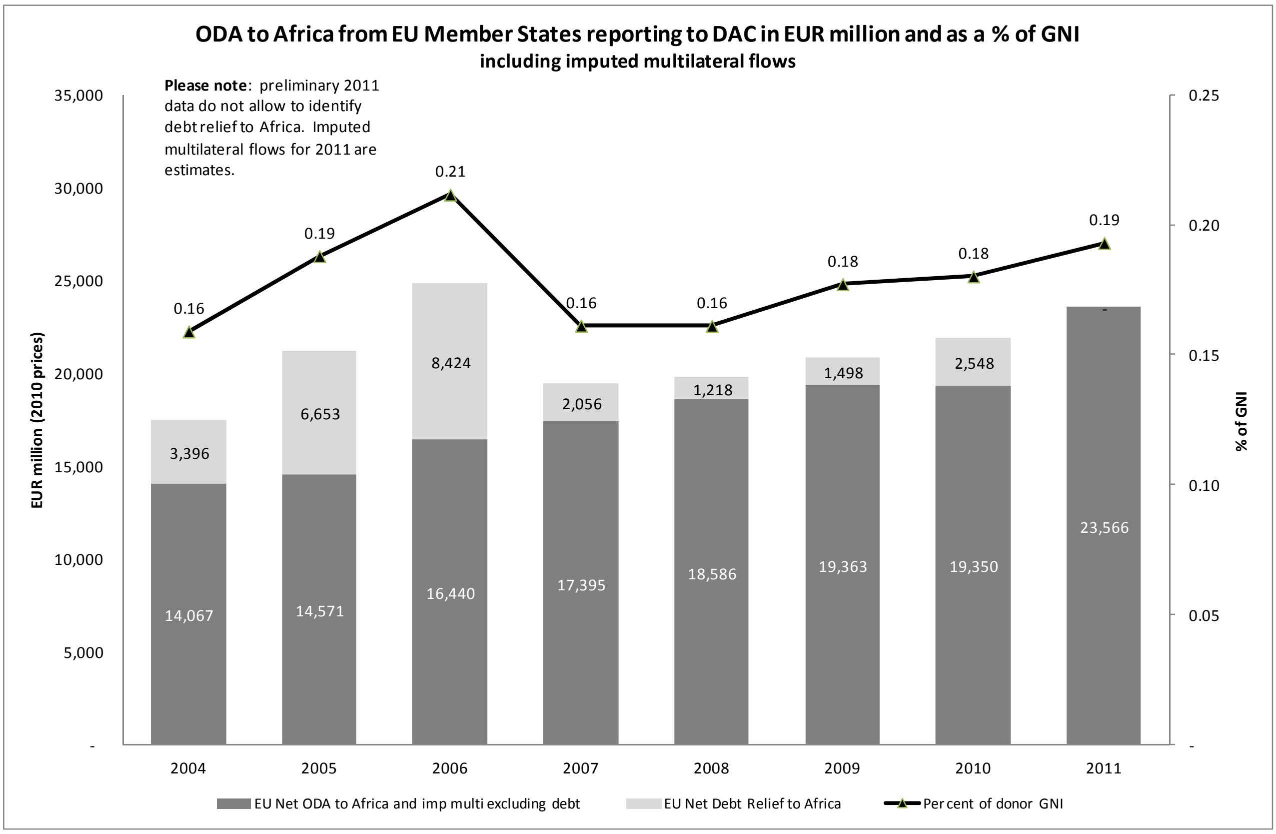
The Commission has, in the last five annual reports, proposed three ways ways to step up efforts: (a) drawing up of realistic and verifiable national ODA action plans outlining how Member States aim to scale up and strive to achieve the 2015 ODA targets; (b) introducing a peer review mechanism whereby the European Council would assess the progress of each Member State and give guidance for further joint EU progress for attaining the agreed ODA targets; and (c) enacting national legislation ring-fencing ODA.

4.1.6. Falling short of EU's promise on ODA to Africa

Since making the commitment to direct 50% of EU aid increases to Africa in 2005 (based on 2004 aid levels), the combined EU aid to Africa has risen by about EUR 6.2 billion at constant prices so that 28% of total EU ODA growth between 2004 and 2011 went to Africa, as shown in **Figure 4.1.6**.

In Member States' replies on their individual actions, the target of allocating 50% of the ODA *increase* to Africa does not seem to be considered relevant, as no reference is made to this. On the other hand, Member States often cite the share of Africa in their overall ODA or geographically programmable ODA for measuring/displaying their effort. Most EU Member States are taking actions to increase ODA targeted to Africa. For some, aid to Africa already accounts for most of their bilateral ODA (e.g. 80% for Ireland, 65% for Portugal). A few Member States will not contribute to that target through their bilateral ODA as they believe their comparative advantage is in other regions of the world. An important dimension is the imputed multilateral share of EU aid to Africa, which amounted to an estimated EUR 11 billion in 2011 and contributed 50% of the collective EU increase from 2004 to 2011. Overall 43% or EUR 25.3 billion of EU ODA was targeted to Africa in 2011.

Figure 4.1.6 - ODA to Africa from EU15 in EUR million and as a % of GNI (including imputed multilateral flows)



Source: OECD DAC data for 2004 – 2010 and Commission simulation on DAC data for 2011

How did EU ODA to Sub-Saharan Africa increase since 2005?

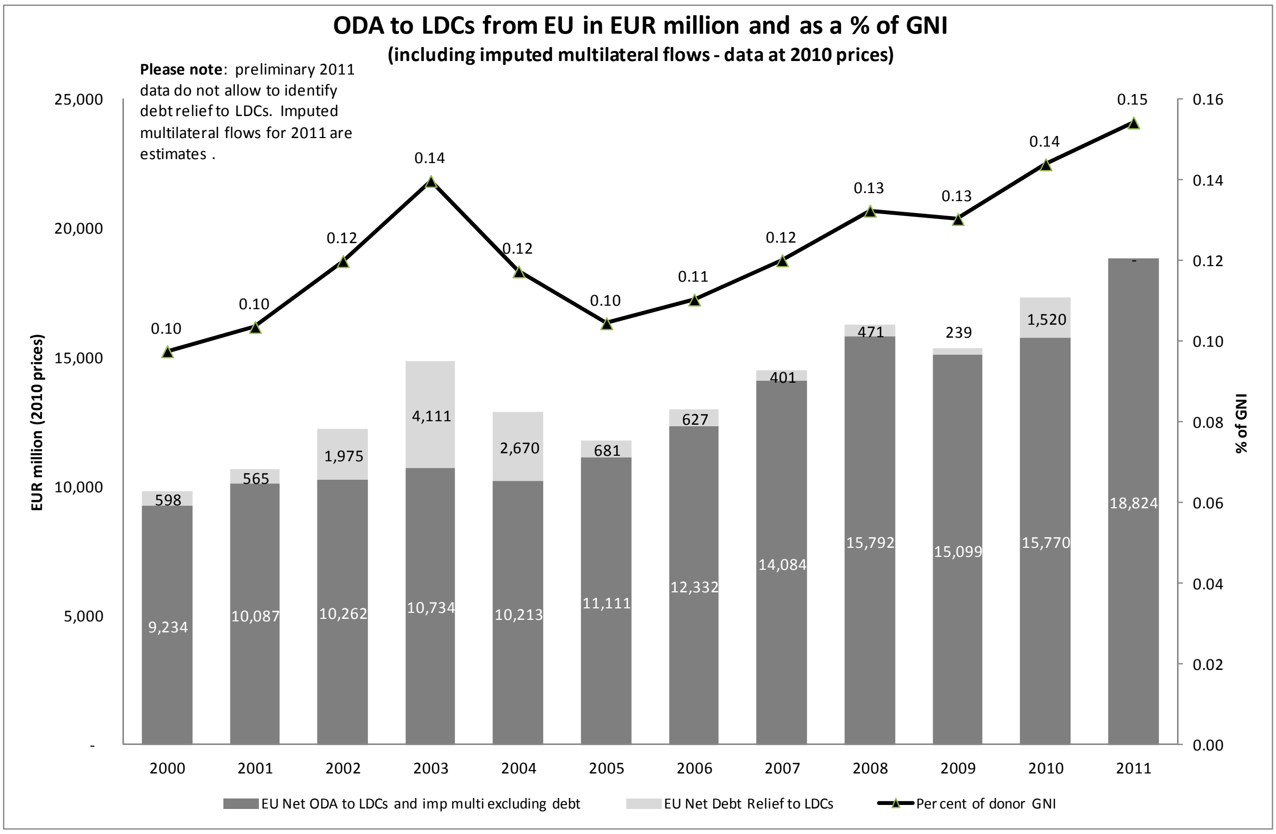
EU ODA to Sub-Saharan Africa grew by around EUR 5.5 billion in real terms over the period 2004-2011, thus meeting the less demanding target of increasing EU aid to Sub-Saharan Africa. 80% of this growth was due to aid through multilateral channels. Only Austria, Greece, Netherlands and Portugal decreased their ODA to Sub-Saharan Africa over this period. Estimates for 2011 indicate there was no further growth.

4.1.7. Honouring the EU commitment on ODA to Least Developed Countries

In November 2008, Member States promised, as part of the EU's overall ODA commitments, to provide collectively 0.15% to 0.20% of their GNI to Least Developed Countries (LDCs) by 2010 while fully meeting the differentiated commitments set out in the 'Brussels Programme of action for the LDCs for the decade 2001-2010'.

Since making the commitment to direct 50% of EU aid increases to Africa in 2005 (based on 2004 aid levels), the combined EU aid to Africa has risen by about EUR 6.2 billion at constant prices so that 28% of total EU ODA growth between 2004 and 2011 went to Africa, as shown in **Figure 4.1.6**.

Figure 4.1.7 - EU ODA to LDCs as a % of GNI including imputed multilateral flows



Source: OECD DAC

The LDCs' share of EU ODA has increased both in absolute and relative terms since 2004 and reached **EUR 18.8 billion in 2011, corresponding to 35% of EU ODA or 0.15% of EU GNI, thus meeting the target**.

Figure 4.1.7 summarises the evolution of ODA to LDCs over GNI ratios for EU Member States reporting to DAC over the period 2004-2011. The peak in 2005 and 2006 is due to large debt relief operations in those years. **Belgium, Denmark, Finland, Ireland, Luxembourg, Portugal, Sweden and the United Kingdom** remained above the ODA to LDC target in 2011. **Ireland** is the only Member State that has kept a share of ODA to LDC greater than or equal to 50% for the entire period. Member States that have not reached the target need to make enhanced efforts to increase their overall ODA and, within this, to increase the proportion of aid that goes to LDCs, although a majority of Member States (14 - including all the EU12 Member States) do not expect to be able to reach the 0.15 target any time soon.

4.2. Scaling up funding for tackling Climate Change and Biodiversity in the context of Sustainable Development

4.2.1. Climate change fast-start finance

EU Commitments
European Council Conclusions on 10/11 December 2009[133]: The EU and its Member States are ready to contribute with fast-start funding of EUR 2.4 billion annually for the years 2010 to 2012.

4.2.1.1. Background

The EU as a whole is committed to playing a leading role in the fight against global warming and is an active participant in the negotiations on climate change under the United Nations Framework Convention on Climate Change (UNFCCC).

The EU and its Member States have pledged to contribute fast-start funding totalling EUR 7.2 billion for the years 2010 to 2012. Developed countries also committed to a long-term goal of jointly providing USD 100 billion per year by 2020 to address the needs of developing countries in the context of meaningful mitigation action and transparency of implementation. This funding will come from a variety of sources, public and private, bilateral and multilateral, including alternative sources of finance. Through numerous Council Conclusions, the EU and its Member States have reaffirmed their commitment to doing their fair share in this context and actively working towards identification of a pathway for scaling up available financing together with international partners.

The Commission has proposed that for the next **Development Cooperation Instrument** (DCI) (2014-2020) "*no less than 50% of the programme for Global Public Goods and Challenges will be spent on climate change and environmental objectives."* The Commission proposal also foresees an overall climate expenditure target of 20% applied to all of the external heading instruments during the next multiannual financial perspectives. To validate progress towards this objective the provisions in the respective horizontal regulations introduce both *ex-ante* and *ex-post* tracking in line with the OECD Development Assistance Committee's Rio-markers definitions.

Better policies are at least as important as more funding. For example, the agreement by the G20 to rationalise and phase out fossil fuel subsidies (amounting to EUR 308.8 billion - USD 409 billion - in emerging and developing countries in 2010) is a step in the direction that the EU has adopted for several years. As a matter of fact, a recent OECD study[134] shows that removing consumer subsidies for energy over the next decade would reduce global greenhouse gases emissions by over 10 % in 2050.

4.2.1.2. Volume and focus of EU support

Monitoring ODA which is related to climate change and other environmental issues has long been a difficult task due to the complexity of the issues and their multidimensional character. To help carry out this task, two markers have been set up within the DAC/CRS system: "climate change-

[133] European Council Conclusions on 10/11 December 2009, EUCO 6/09

[134] For reference and a summary of other relevant studies see for example: OECD (2011), *Tackling Climate Change and Growing the Economy. Key messages and recommendations from recent OECD work* http://www.oecd.org/dataoecd/28/18/44287948.pdf

adaptation" and "climate change-mitigation".[135] Data prepared using these markers have been released for the first time in January 2012, covering ODA disbursed during 2010.

Different conversion factors are used by the Commission where only 40% of total project costs are considered for Rio Marker 1. Several EU Member States apply similar methodologies. EU estimates on climate change related ODA are therefore quite conservative. There are no guidelines on the application of such conversion factor internationally or at EU level.

Based on the 2011 and 2012 EU annual questionnaire on Financing for Developments, **the EU and its Member States committed in their budgets EUR 2.26 billion in 2010 and EUR 2.33 billion in 2011 respectively. Accordingly the EU, having collected EUR 4.59 billion in 2010-2011, remains on track to achieve the goal of EUR 7.2 billion over the period 2010-2012, despite difficult economic situation and budgetary constraints**. These are preliminary figures as the accounting year for many Member States has not been concluded yet. Non fast start finance for climate change increased from EUR 2.8 billion in 2010 (as recorded in the DAC CRS) to an estimated EUR 3.5 billion in 2011, based on the answers given by Member States to the 2012 questionnaire. It must be emphasised that, as shown in **Table 4.2.1.2** below, data on the overall climate finance envelope is not available for all Member States.

Table 4.2.1.2 below analyses ODA provided in 2010 for climate change adaptation and mitigation by all donors and combines two sources: (a) new CRS data that allow us to determine how much ODA was given for adaptation and mitigation (last year's report included an estimate); and (b) data from last year's questionnaire to determine the share of fast start climate finance. Unfortunately, detailed ODA data are released over a year after the close of the financial year they refer to, and 2011 data will only be available by January 2013, too late to be included in this report.

The **EU has been by far the largest contributor to both mitigation-related and adaptation-related ODA in 2010 with a share above 70%, demonstrating strong commitment to fight climate change at a time of significant budget cuts in many Member States.** Non fast start and fast start finance were broadly equivalent, unlike last year's estimations which anticipated that the latter would be almost twice the former. The high EU share could be due to uneven reporting by other DAC Member States on the new climate change markers, but it is nevertheless a good indication of the efforts made by the EU.

[135] An activity should be classified as adaptation related (with a score of principal – 2, significant – 1, or 0 – not targeted, in declining order of importance) if it intends to reduce the vulnerability of human or natural systems to the impacts of climate change and climate-related risks, by maintaining or increasing adaptive capacity and resilience. An activity should be classified as mitigation (with the same scoring grid) if it contributes to the objective of stabilisation of greenhouse gas (GHG) concentrations in the atmosphere at a level that would prevent dangerous anthropogenic interference with the climate system by promoting efforts to reduce or limit GHG emissions or to enhance GHG sequestration. Some development cooperation activities could do both, and there are therefore overlaps.

Table 4.2.1.2 - ODA estimate for Climate Change Adaptation and Mitigation in 2010

(Net disbursements, EUR million at current prices)[136]

Type	All	% of total	EU	Non EU	EU Share
Adaptation	**1,664.71**	**23%**	**979.63**	**685.09**	**59%**
Principal	*532.69*	*7%*	*161.59*	*371.10*	*30%*
Significant	*1,132.02*	*16%*	*818.04*	*313.98*	*72%*
Mitigation	**3,831.62**	**53%**	**2,842.12**	**989.50**	**74%**
Principal	*2,679.69*	*37%*	*1,867.12*	*812.56*	*70%*
Significant	*1,151.93*	*16%*	*975.00*	*176.94*	*85%*
Adaptation and Mitigation	**1,761.15**	**24%**	**1,341.53**	**419.61**	**76%**
Both Principal	*1,126.05*	*16%*	*741.64*	*384.42*	*66%*
Both Significant	*635.09*	*9%*	*599.90*	*35.20*	*94%*
Total Climate Change	**7,257.48**	**100%**	**5,163.28**	**2,094.20**	**71%**
of which:					
Fast-start finance (as reported in May 2011)			2,340.00		
Non Fast-start finance (actual)			2,823.28		
Non Fast-start finance (est. in 2011)			3,959.92		
Climate change ODA 2010/Average 2007-2009			1.30		

Sources: DAC CRS for all data except Fast Start Finance which is from the 2011

4.2.1.3. Measuring additionality

In 2009, the Council agreed that climate financing required additional resources, and that ODA should continue to play a role in supporting adaptation (including disaster risk reduction) in the most vulnerable and least developed countries.[137]

A methodology to determine additionality was proposed in last year's report. The average EU total ODA for the period 2007 to 2009, net of climate change related activities, was set as benchmark

[136] The table avoids double counting using the following method. Principal (2) always prevails over substantial (1). If mitigation is set as principal and adaptation substantial for the same activity, the higher mark prevails and the activity is classified as mitigation. When the ratings are equal, the ODA is classified under "Adaptation and Mitigation". The combinations are as follows. Mitigation or Adaptation: Principal (2-0 and 2-1); Substantial (1-0). Mitigation and Adaptation: Principal (2-2); Substantial (1-1).

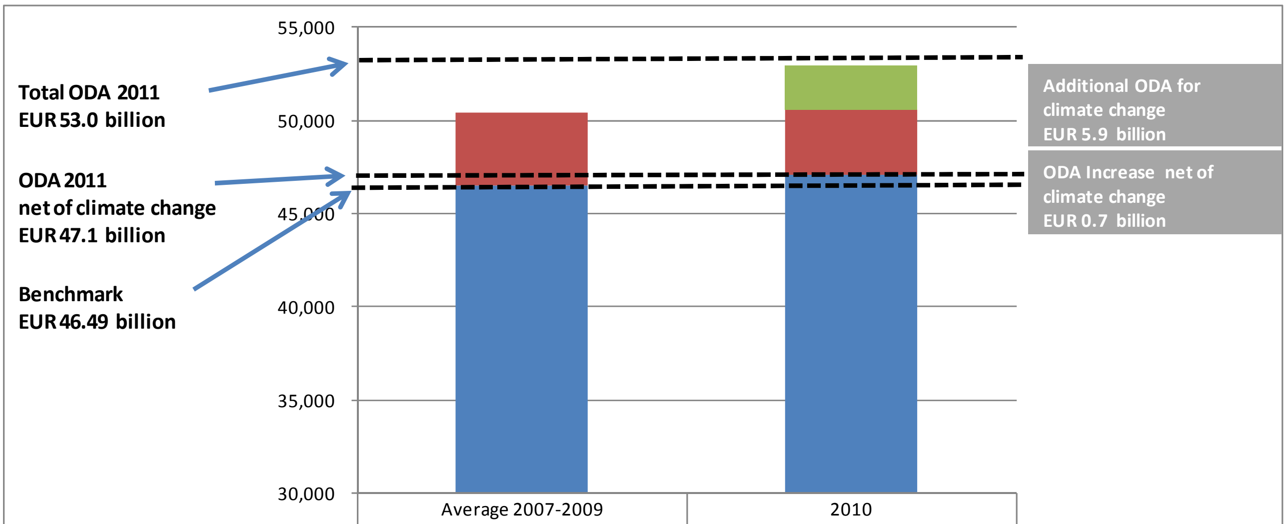
[137] Council Conclusions on Climate Change and Development, 16071/09, 17 November 2009

and estimated at EUR 46.5 billion in constant 2010 prices.[138] By this reasoning, if climate finance is to be additional, the EU's total ODA excluding climate-related ODA, should be higher than this benchmark level in the years 2010-12.

The above criterion for additionality was met in 2010, using this report's data for the EU's total ODA in 2010 – namely EUR 53.5 billion in constant 2010 prices. This is EUR 0.7 billion above the benchmark level, which corresponds to the maximum potential volume of climate finance that would be additional without cutting into support to other sectors. This is enough to cover the EUR 2.3 billion dedicated to fast-start finance and EUR 2.8 billion of non-fast-start finance for 2010 determined using the latest CRS data.

As shown in **Figure 4.2.1.3,** the preliminary figures available for 2011 seem to indicate that **the above criterion for additionality was met also in 2011,** although with a further contraction of the margin above the 2007-2009 benchmark.

Figure 4.2.1.3: Calculating the additionality of climate finance in 2011 – EUR million in 2010 prices



	Average 2007-2009	2010
Fast Start	-	2,395
Non Fast Start	3,960	3,474
Other ODA	46,486	47,097

Source: OECD DAC for ODA and mitigation data 2007-2009 for DAC reporting Member States as well as climate change adaptation and mitigation for 2010. EU annual questionnaire on Financing for Development for fast-start finance.

[138] See last year's report for a description of the methodology. We have updated the volumes using the latest DAC deflators to convert ODA at 2008 prices into ODA at 2010 prices.

4.2.2. Biodiversity

EU Commitments
● *European Council Conclusions on the Convention on Biological Diversity (CBD): outcome of and follow-up to the Nagoya biodiversity conference, 20 December 2010.*[139] *The EU and its Member States have committed to implementing the strategy for resource mobilisation and to substantially increasing resources (financial, human and technical) from all possible sources balanced with the effective implementation of the CBD and its strategic plan. The EU will actively involve in developing baselines for monitoring the implementation of the strategy, and in implementing the COP 10 decision to adopt targets at CBD COP 11, provided that robust baselines have been identified and endorsed and that an effective reporting framework has been adopted.*
● June 2011 *Council Conclusions on the EU Biodiversity Strategy*[140] *and succeeding December 2011 Conclusions on implementation of the Europe 2020 Biodiversity Strategy.*[141]

4.2.2.1. Background

A global strategy to combat biodiversity loss for the coming decade was adopted at the tenth meeting of the Conference of the Parties (COP 10) of the Convention on Biological Diversity (CBD) in Nagoya (Japan) in October 2010.[142] The plan is backed up by a strategy for mobilising resource to help achieve the CBD's three objectives.

The Council adopted Conclusions on the implementation of the Europe 2020 Biodiversity Strategy at its meeting on 19 December 2011.[143] The new strategy has six main targets with 20 actions to help the EU address biodiversity challenges. Internationally, the EU contribution to averting global biodiversity loss is to be stepped up, through a reduction of indirect drivers of biodiversity loss (e.g. changing consumption patterns, reducing harmful subsidies, and including biodiversity issues in trade negotiations) and mobilisation of additional resources for global biodiversity conservation. Specifically, the EU and its Member States committed to "contributing their fair share to international efforts to significantly increase resources for global biodiversity as part of the international process aimed at estimating biodiversity funding needs and adopting resource mobilisation targets for biodiversity at CBD CoP11" to be held in Hyderabad, India on October 8-19, 2012. The Council Conclusions of 11 June 2012 on the preparation of CBD COP 11 emphasise the need to continue to play a proactive role to fulfil those commitments and keep the momentum from Nagoya. They also recognise the need to further improve the effectiveness of existing funding and mobilise new types of funding sources, including the private sector and other stakeholders, e.g. through mainstreaming and integration of biodiversity considerations at all levels. The importance of IFM as an essential and necessary funding source, in addition to traditional financing mechanisms, and as a tool for mainstreaming biodiversity is also emphasised.

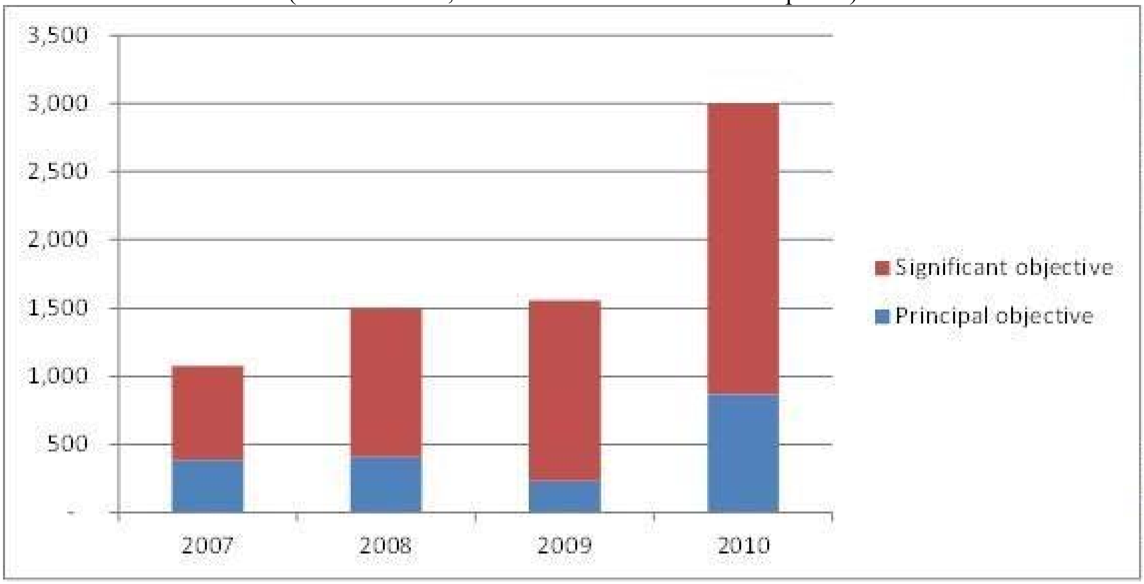
[139] http://www.eu-un.europa.eu/articles/fr/article_10510_fr.htm
[140] Council Conclusions on the EU Biodiversity Strategy to 2020, 11978/11, 23 June 2011, http://register.consilium.europa.eu/pdf/en/11/st11/st11978.en11.pdf
[141] Council Conclusions on the EU Biodiversity Strategy to 2020 – Towards implementation, 18862/11, 19 December 2011, http://consilium.europa.eu/media/1379139/st18862.en11.pdf
[142] The Convention on Biological Diversity entered into force in 1993 and has three main objectives: i) the conservation of biological diversity; ii) the sustainable use of the components of biological diversity; and iii) the fair and equitable sharing of the benefits arising out of the utilisation of genetic resources. The Convention obliges developed countries to provide new and additional financial resources related to the implementation of the Convention (Article 20).
[143] See http://ec.europa.eu/environment/nature/biodiversity/comm2006/2020.htm for details.

The EU recognises that the link between ecosystems, on the one hand, and employment, income and livelihoods, on the other hand, is even stronger in developing countries than in developed countries.[144] In that connection, the Commission's 2010 Work Programme on Policy Coherence for Development and the PCD report of 2010 have specific sections on biodiversity. This ambition is carried forward in the new EU Development Policy framework as set forth in the 'Agenda for Change', which states that "EU development policy should promote a 'green economy' that can generate growth, create jobs and help reduce poverty by valuing and investing in natural capital."[145]

4.2.2.2. Volume and focus of EU support

Similar to climate finance, support to biodiversity is measured through a specific marker in the CRS, and may suffer irregularities from uneven reporting by DAC members. Based on this data, **the volume of EU ODA relating to biodiversity increased by over 140% during the period 2006-2010 in real terms, from EUR 1.3 billion in 2006 to EUR 3 billion in 2010** (see **Figure 4.2.2.2**), although only 26% had biodiversity as a principal objective. During this period, the EU committed, on average, EUR 1.7 billion per year for biodiversity-related aid, representing 53% of total ODA for biodiversity from all bilateral donors and multilateral organisations reporting to DAC CRS.

Figure 4.2.2.2a: EU's biodiversity-related ODA by objective. 2007-2010
(Commitments, EUR million at constant 2010 prices)



Source: OECD DAC/CRS[146]

Among EU Member States, France, the United Kingdom, Germany and Spain were the largest donors in 2010, but several other countries also donated substantial amounts during this period (see **Table 4.2.2.2 below**).

The EU's biodiversity-related aid as a share of total EU ODA increased from 2.1% in 2006 to 5.6% in 2010, in line with the increasing focus on sustainable development. Most Member States see biodiversity and its associated ecosystem services both as a crosscutting and a sectoral issue in their development cooperation, and thus mainstream it in their development programmes, though more efforts are needed to ensure that biodiversity is included in the priorities of partner countries.

[144] Council conclusions on Biodiversity: Post-2010 EU and global vision and targets and international ABS regime, 7536/10, 15 March 2010
[145] http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2011:0637:FIN:EN:PDF
[146] Luxembourg does not report on the Rio markers. No data for the Netherlands for 2009

Table 4.2.2.2: EU's biodiversity-related bilateral aid, 2006-2010[147] adjusted deflators
(Commitments, EUR million at constant 2010 prices)

Member State	2006	2007	2008	2009	2010	Average 2006-2010
Austria	13	11	24	22	12	16
Belgium	29	52	92	95	135	81
Denmark	122	81	128	87	191	122
EU Institutions	378	226	254	526	502[148]	377
Finland	3	38	98	84	90	63
France	111	126	166	171	649	244
Germany	231	182	205	223	441	256
Greece	2	3	3	6	3	4
Ireland	-	20	13	70	31	27
Italy	10	88	59	46	4	42
Luxembourg	-	-	-	-	3	1
Netherlands	236	170	183	-	75	133
Portugal	1	2	2	3	3	2
Slovenia		1	1	1	1	1
Spain	67	73	255	209	229	166
Sweden	24	0	11	5	150	38
United Kingdom	9	6	10	11	451	97
Total	**1,234**	**1,079**	**1,503**	**1,558**	**2,969**	**1,670**

Source: OECD DAC/CRS[149]. EU annual questionnaire on Financing for Development for Slovenia. Hungary and Romania reported amounts below Euro 0.5 million and are therefore not included.

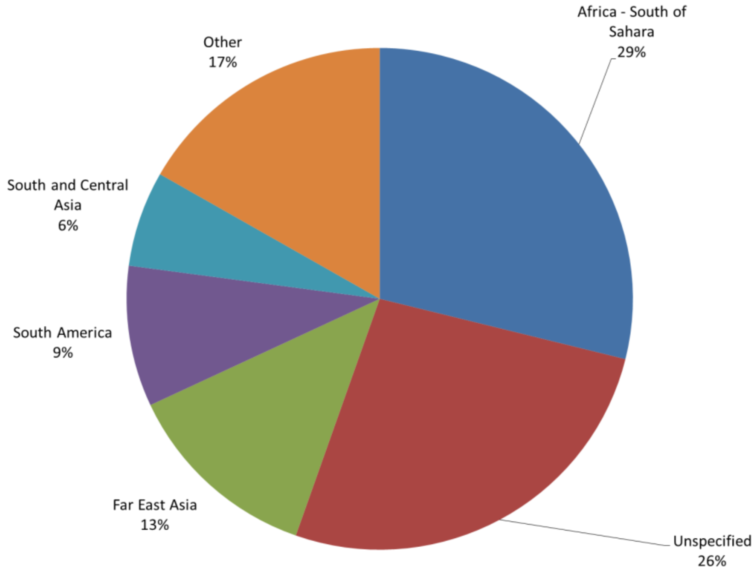
Over a third of the EU's biodiversity-related aid goes to Africa and around one fifth to Asia and one seventh to America (see **Figure 4.2.2.2.b**). The support is divided among 145 countries and territories. One fourth of the support has no specific geographical focus.

[147] The breakdown between principal and significant objective is not available for 2006. Data for years 1998-2006 were obtained by DAC on a trial basis; reporting became mandatory starting with 2007 flows.

[148] The 2010 data for EU Institutions is currently being updated in the OECD DAC statistics.

[149] Luxembourg did not report on the Rio markers up to 2009 and there is no data for the Netherlands for 2009. OECD DAC Full List of biodiversity aid activities (2007-2009) (http://www.oecd.org/dataoecd/14/30/46809641.xls), OECD DAC Full List of biodiversity aid activities (2010) (http://www.oecd.org/dataoecd/27/25/49450525.zip), and OECD DAC Aid targeting the objectives of the Rio Conventions 1998-2007 (http://www.oecd.org/dataoecd/58/60/48895957.pdf).

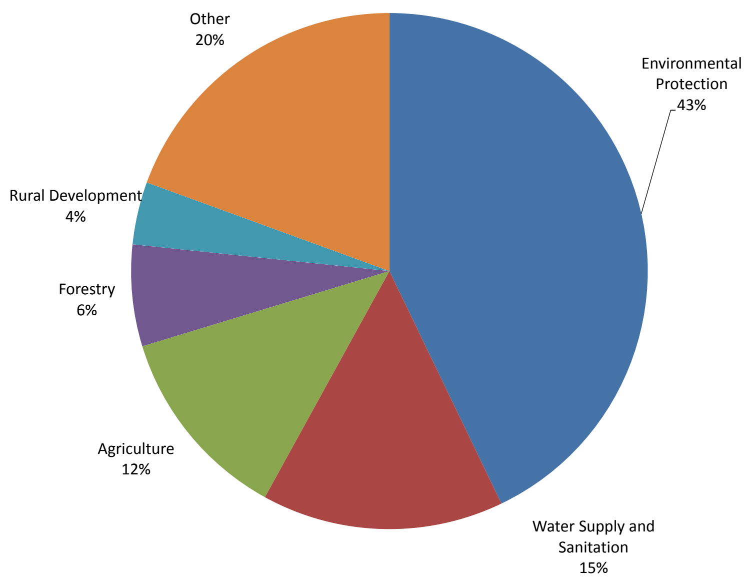
Figure 4.2.2.2b - EU's biodiversity-related bilateral aid by geographic area, 2007-2010, percentage share, commitments



Source: OECD DAC/CRS

In terms of sectors, the EU's biodiversity-related aid falls primarily within environmental protection, followed by water supply and sanitation, agriculture and forestry (see **Figure 4.2.2.2.c**).

Figure 4.2.2.2c: EU's biodiversity-related bilateral aid by sector, 2007-2010, percentage share, commitments



Source: OECD DAC/CRS[150]

[150] Luxembourg does not report on the Rio markers and there are no data for the Netherlands for 2009. Activities marked with a 'principal' or a 'significant' objective are included.

4.2.3. Sustainable Development

The 'Agenda for Change' aims at putting a greater focus on investing in drivers for inclusive and sustainable economic growth. It envisages a greater focus on helping reduce developing countries' exposure to global shocks, such as climate change, ecosystem and resource degradation, and volatile and escalating energy and agricultural prices, by concentrating investment in sustainable agriculture and energy. It foresees support to the decent work agenda, social protection schemes and floors, providing the workforce with the right skills and encouraging policies to facilitate regional labour mobility.

The United Nations Conference on Sustainable Development (Rio+20), held in Rio de Janeiro on 20-22 June 2012 provided a unique opportunity for all involved to renew strong political commitment to sustainable development at all levels, to assess the progress made to date, identify remaining implementation gaps and address new and emerging challenges.

In the **EU Common position for Rio+20**[151], two priorities were highlighted. First, the need for a green economy roadmap with specific goals, objectives and actions at international level; second, the need for a package of reforms in the Institutional framework for sustainable development, which should lead to a strengthened international environmental governance (IEG).

During preparations, the Council of the European Union highlighted in March 2012[152] that **funding for the implementation of sustainable development will have to come from both public and private sources,** and called for a more effective use of existing resources and the identification of innovative sources. It underscored that mobilisation of funding must be undertaken in a way that is consistent with the objectives of global economic recovery, and underlined the important role of International Financial Institutions and the Global Environment Facility (GEF). In that connection, the EU submission to UN DESA in November 2011, stated that *"a joint approach by traditional donors, emerging economies, international financial institutions (IFIs) and the private sector is needed, addressing the 'silo' approach to channelling funds and ensuring a more effective identification and use of existing resources, as well as mobilisation of available and innovative sources of finance."*

The EU is also constructively engaging in the discussion about launching a process on **Sustainable Development Goals (SDG)** to be coordinated by the UN Secretary General. The establishment of SDGs, fully encompassing all three dimensions of sustainable development, will provide the opportunity to focus efforts at the global, regional and national level and could be an important driver for mainstreaming sustainable development and integration of its three dimensions in a balanced and synergistic way. The work on SDGs should be coordinated and coherent with the Millennium Development Goals (MDG) review process, without deviating efforts from the achievement of the MDGs by 2015. Furthermore, the EU considers that it would be important to have an overarching framework for post 2015 that encompasses the three dimensions of sustainable development with goals that address key challenges in a holistic and coherent way to ensure the optimal mix of measures for attaining lasting solutions.

[151] Council Conclusions on Rio+20: Towards achieving sustainable development by greening the economy and improving governance, 15388/11, 11 October 2011, http://register.consilium.europa.eu/pdf/en/11/st15/st15388.en11.pdf
[152] European Council Conclusions on 9 March_2012, Rio+20 Pathways to a Sustainable Future

4.3. Seeking synergies in EU support

In the context of ongoing various international processes, discussions on ODA, all aspects of sustainable development and global public goods in general are closely linked. For example, building a dam provides various services in a developing country: job creation, resilience to droughts (climate adaptation), sustainable energy (green growth and climate mitigation), and may at the same time have negative social and environmental impacts (need for moving people and changed river flows) that needs to be mitigated – all these services and impacts are aspects of sustainable development in the widest sense. This calls for an integrated approch that truly integrates all three dimensions of sustaianble development in a balanced and synergistic way, and for seeking coherence across different policy areas.

There seems to be an emerging international consensus that better measures of progress and development efficiency are needed to tackle global challenges. The proposals for defining new aggregates that would enhance accountability fall into three broad categories: (a) changing how we measure ODA efforts (notably by revising the ODA concept)[153]; (b) changing what we measure (including by complementing/replacing ODA with a broader aggregate like "total net resource flows for development"[154]); or (c) changing where we measure ODA/GNI ratios (at the recipient level rather than at the donor's level).[155]

[153] See for example, Brzoska, Michaela (2010). *Analysis of and recommendations for covering security relevant expenditures within and outside of official development assistance*, Paper 53, Bonn International Center for Conversion

[154] See for example, OECD DAC (2011), *Identifying New Measures for Non-ODA Development Contributions*, DCD/DAC(2011)43; or Severino, Jean-Michel and Ray, Olivier (2009). *The End of ODA: Death and Rebirth of a Global Public Policy*. CGD - Center for Global Development - Working Paper Number 167.

[155] See for example, ODI (2012), *From high to low aid: a proposal to classify countries by aid receipt*, Background Note, March 2012.

5. MAKING EU ACTIONS MORE EFFECTIVE FOR DEVELOPMENT

5.1. Making EU aid more effective

EU Commitments
• *On 17 November 2009[156], the Council (General Affairs and External Relations) adopted the Conclusions on an Operational Framework on Aid Effectiveness, with additions made in June 2010 (cross country division of labour DoL) and December 2010 (accountability and transparency).[157]* • *The Operational Framework includes detailed commitments on accelerating Division of Labour (DoL); increased use of country systems; ensuring technical cooperation for enhanced capacity development; and strengthening accountability and transparency.*

The EU and its Member States are working on a range of measures to implement commitments in relation to the Paris Declaration principles, the Accra Agenda for Action, and the Busan Partnership for Effective Development Cooperation. Since the Rome Declaration on aid harmonisation of 2003, the EU has embedded the evolving international aid effectiveness consensus in various Council Conclusions and has reviewed the related efforts of EU Member States in all previous editions of the present report.

In November 2009, the General Affairs and External Relations Council adopted *an Operational Framework on Aid Effectiveness* containing measures in key areas of the aid effectiveness agenda, such as division of labour, use of country systems and technical cooperation for enhanced capacity development. Based on Commission proposals, the *Operational Framework* was complemented in 2010 by a subchapter on cross-country division of labour[158] and a new chapter on a common EU approach for implementing commitments on mutual accountability and transparency.[159]

The Council Conclusions on the EU Common Position for the Fourth High Level Forum on Aid Effectiveness[160] emphasised the need for an inclusive Post-Busan Agenda, building bridges towards different development actors, notably emerging economies, civil society organisations and the private sector as well as for domestic accountability mechanisms in partner countries.

The Council Conclusions of 14 May 2012[161] on "Increasing the impact of EU Development Policy: an Agenda for Change" emphasise the importance of improved mutual accountability, sector concentration, targeting of resources, joint multiannual programming, cross-country division of labour, ownership, sustainable growth and transparency. In particular, they stress that "the EU should develop a common framework for measuring and communicating the results of development policy, including for inclusive and sustainable growth. In line with the Operational Framework on Aid Effectiveness, the EU will work with partner countries and other donors on comprehensive approaches to domestic and mutual accountability and transparency, including through the building of statistical capacity."

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[156] Council Conclusions on An Operational Framework on Aid Effectiveness, 15912/09, 18 November 2009

[157] Council Conclusions on an Operational Framework on Aid Effectiveness – Consolidated text, 18239/10, 11 January 2011.

[158] Council Conclusions on Cross-country division of labour, 10348/10, 14 June 2010.

[159] Council Conclusions on Mutual accountability and transparency, 17769/10, 10 December 2010.

[160] Council Conclusions on the EU Common Position for the Fourth High Level Forum on Aid Effectiveness, 16773/11, 14 November 2011.

[161] Council Conclusion on Increasing the impact of EU Development Policy: an Agenda for Change, 9369/12, 14 May 2012 http://register.consilium.europa.eu/pdf/en/12/st09/st09369.en12.pdf

Article 210 of the Lisbon Treaty states that the Union and its Member States shall coordinate their policies on development cooperation, and consult each other on their aid programmes, including in international organisations and during international conferences, and may undertake joint action, and contribute if necessary to the implementation of Union aid programmes.

This new legal and policy framework provides a new opportunity to make EU development aid more effective, efficient, and successful in terms of actual impact on the ground. It should also make a real difference in terms of EU political impact and visibility. Studies carried out on behalf of the European Commission[162] found that fully implementing the Aid Effectiveness Agenda[163] would allow efficiency savings and gains of EUR 5 billion per year, and gains from redistribution effects through coordinated country allocation of an additional EUR 7.8 billion per year.

5.1.1. EU and Member States performance in implementing the Paris Declaration (2005-2010)

The 2011 OECD/ DAC Paris Declaration Survey, the results of which were published in September 2011, together with the replies of the Member States to this year's questionnaire provide good evidence for a thorough review of EU aid effectiveness performance.

As noted by the OECD DAC Secretariat in its analysis of the 2011 Paris Declaration Survey's findings, these were "sobering" for all donors, including the EU and its Member States. Reference is made here to the EU collective performance, as individual Member States performed better than others.

The main conclusion is that the EU missed its 2010 ODA quantitative targets, as described above in this report, as well as most of its qualitative targets as enshrined in the Paris Declaration. As a whole, the EU in fact met only one of the twelve indicators relating to donor performance (i.e. coordinated technical cooperation).

However, OECD DAC also concluded that "considerable progress has been made towards many of the remaining targets." Most of the overall progress among bilateral donors worldwide was made possible thanks to progress by EU Member States. Most EU Member States performed above the "all donors" average, showing a significant commitment to the achievement of the goals of the Paris Declaration under difficult global conditions.

Out of twelve indicators and sub-indicators referring to the performance of donors, the EU and its Member States met one and improved eleven over the period 2005-2010. In contrast, non-EU bilateral donors met no target, and improved only three indicators, all closing at a much lower level and further from their target than the EU and its Member States.

The EU was also the group that made most progress on the use of country procurement systems, predictability and the reduction in the number of parallel Project Implementation Units (PIU's).

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[162] HTSPE, *Aid Effectiveness Agenda: Benefits of a European Approach*, October 2009.
[163] SOGES, *The Aid Effectiveness Agenda: The benefits of going ahead*, 2010.

5.1.2. EU and Member States action on alignment

Increasing alignment of aid with partner countries' priorities, systems and procedures and helping to strengthen their capacities is a central principle of the Paris Declaration. To improve alignment donors agreed to **use country systems** (i.e. national arrangements and procedures for public financial management, accounting, auditing, procurement, results frameworks and monitoring) to the maximum extent possible. Using a partner country's own institutions and systems has a positive impact on aid effectiveness: it creates a special incentive to strengthening the partner country's institutional capacities in programme implementation, accounting, monitoring and evaluation and in reporting to Parliament and to its citizens. EU donors also committed to aligning their **conditions**, whenever possible, with their partner's national development strategy, and to make them public. In addition, EU donors have committed to disbursing aid in a timely and **predictable** fashion according to agreed schedules. In terms of technical cooperation, EU donors have significantly reduced the number of parallel **project implementation units**, in order to build on the capacities of partner countries.

Use of Country Systems (UCS)

The use of country systems by the EU and its Member States has improved substantially since 2005, particularly as far as procurement systems are concerned, but still fall short of targets. **On using country systems as a first option**[164], Member States have scaled up their efforts compared to last year.

– 13 Member States revised the design of aid instruments irrespective of modality (up from 11 in 2010);

– staff training was provided by 17 Member States (up from 11 in 2010),

– 19 Member States supported partner country capacity development for improving the quality of country systems (up from 17 in 2010).

– 14 out of 25 Member States supported the use of country systems through an assessment to identify internal constraints, slightly down from the 15 reported one year ago.

The 2011 Communication on *The Future Approach to EU Budget Support to third countries*[165] states that "budget support, in particular 'Good Governance and Development Contracts', should be used to strengthen core government systems, such as public finance management and public administration." The ensuing Council Conclusions of 14 May 2012[166] emphasise the commitment to use budget support effectively to support (…) the use of country systems.

Making aid more predictable

Table 5.1.2 below presents the ratios between actual 2009 and 2010 ODA flows and budgets prepared one, two or three years before (the latter is available only for 2010). Ratios below 100% mean that actual expenditure was below budget, while ratios above 100% indicate that actual expenditure was above budget. **Overall, most EU Member States achieved a good degree of**

[164] See European Council, 11 January 2011, Doc. 18239/10. Operational Framework on Aid Effectiveness – Consolidated text: paragraphs 6, 8, 12 and 13 (A. Use of country systems as a first option),

[165] COM (2011) 638 final.

[166] Council Conclusions on The Future Approach to EU Budget Support to Third Countries, 9323/12, 14 May 2012, http://register.consilium.europa.eu/pdf/en/12/st09/st09371.en12.pdf

predictability with ratios above the DAC average for one-year, two-year, and three-year predictability.

Table 5.1.2 – Predictability Ratios of DAC Members' Country Programmable Aid
(2009-2010, percentages)

DAC Members	Predictability Ratios				
	One-year Predictability ratio		Two-year predictability ratio		Three-year predictability ratio
	2009	2010	2009	2010	2010
	2009 Outturn/ programmed early 2009 (%)	2010 Outturn/ programmed early 2010 (%)	2009 Outturn/ programmed early 2008 (%)	2010 Outturn/ programmed early 2009 (%)	2010 Outturn/ programmed early 2008 (%)
Australia	111	89	134	102	118
Austria	100	82	n/a	n/a	n/a
Belgium	119	95	56	129	67
Canada	67	79	97	70	102
Denmark	91	122	101	97	110
EU Institutions	117	94	100	114	97
Finland	103	104	98	102	98
France	107	122	68	146	97
Germany	120	90	140	152	86
Greece	n/a	n/a	n/a	n/a	n/a
Ireland	88	90	48	76	39
Italy	60	79	63	36	34
Japan	n/a	n/a	n/a	n/a	n/a
Korea	89	113	n/a	126	n/a
Luxembourg	104	109	97	n/a	92
Netherlands	85	89	87	80	83
New Zealand	73	85	86	66	82
Norway	71	110	82	90	83
Portugal	97	200	91	159	232
Spain	82	81	121	45	77
Sweden	101	101	113	85	94
Switzerland	99	92	n/a	n/a	n/a
United Kingdom	99	111	86	98	95
United States	n/a	n/a	n/a	n/a	n/a
DAC countries total	**93**	**100**	**94**	**88**	**90**

Source: OECD DAC forward spending plans (2010 and 2011)

The table shows a satisfactory performance on predictability, with one-year predictability ratios increasing for eight and declining for five Member States, and two-year predictability ratios increasing for nine and declining for four Member States. The European Commission improved its two-year predictability, but worsened its one-year predictability. Only Ireland, Italy, Netherlands and Spain have one-year, two-year, and three year predictability ratios all below DAC average, and only Spain has reduced both its one-year and two-year predictability ratios between 2009 and 2010.

Fifteen EU Member States can make multi-annual commitments for projects, twelve for general programme based support, and eleven for budget support. For several, outer year budgets are indicative and subject to change (e.g., Ireland).

5.1.3. EU and Member States action on complementarity and division of labour effectiveness

The EU and its Member States have strongly promoted the move towards improved complementarity and division of labour in partner countries (in-country division of labour) and across partner countries (cross-country division of labour). Over the recent years, not only did the EU and its Member States adopt a set of key policy documents on implementing the division of labour agenda in the EU context, they also successfully contributed to an international consensus on division of labour, as agreed in the outcome documents of the Aid Effectiveness fora in Paris, Accra and Busan.

In-country division of labour

With the EU Code of Conduct on Complementarity and Division of Labour, EU donors have committed to establishing a more effective **in-country division of labour.** Since 2008, the EU Fast Track Initiative on Division of Labour and Complementarity (FTI DoL), which involves the European Union and Member States as facilitators, has supported DoL processes in approximately 30 partner countries. The network of EU DoL is being continuously updated and is regularly used for communication between EU donors. Most partner countries included in the joint programming exercises described below are also part of the FTI DoL. In general, the regular monitoring of the FTI revealed that the implementation of in-country division of labour principles by the EU and its Member States is progressing.

However, progress in sector concentration has been very limited. Member States entered 71 and exited 90 sectors. Most exits were from social sectors (about two thirds of the total), mostly in Sub-Saharan Africa (34), followed by South and Central America (25) and Middle East and North Africa (15). Most entries concerned the first two regions: Sub-Saharan Africa (28) and South and Central America (22).

Improving multi-donor analysis and response

As shown in **Table 5.1.3**, Member States reported 226 cases of multi-donor analyses in 66 partner countries, of which roughly one third (75) resulted in a multi-donor response. Almost half of the multi-donor analyses concerned Sub-Saharan African countries but only a fourth resulted in multi-donor responses, compared to two thirds in the Middle East and North Africa and three fourths in South America.

Table 5.1.3 – Number of EU Multi-donor Analyses in 2010-2011 by Region

Region	Multi-donor Analyses	% resulting in multi-donor responses
Sub-Saharan Africa	107	25%
East Asia	27	41%
Central America & the Caribbean	23	39%
Middle East and North Africa	21	67%
Europe	19	11%
South America	12	75%
South Asia	11	18%
Central Asia	11	9%
Total	**231**	**32%**

Source: European Commission (EU annual questionnaire on financing for development 2012)

Joint Programming

The EU has taken concrete steps towards making joint programming a reality. Following the Development Council of 14 November 2011, adopting the policy on joint programming through the Council Conclusions for the Busan Forum on Aid Effectiveness, the EU identified 11 country candidates for joint programming in 2012. Ensuing reports from EU Heads of Missions in these countries confirmed that joint programming in 6 of them is feasible for commencement in 2012. Others may follow in subsequent years.

In order to strengthen partner countries' ownership and to better align with their strategies and priorities as well as to facilitate joint programming, the EU is substantially changing its way of programming. As highlighted in the 'Agenda for Change', EU programming will be synchronised with strategy cycles of partner countries and will no longer cover the same period for all partner countries. Member States, too, are adapting their way of programming for the same reasons.

Cross-country division of labour

Increasing the geographical focus can substantially contribute to more aid and development effectiveness by reducing administrative costs of ODA delivery. In recent years, EU Member States have reorganised their bilateral aid portfolios by geographically focusing their assistance, even in the presence of increasing aid budgets. In 2010 and 2011, there were 71 cases of exits by EU Member States from 43 partner countries, 50 already completed and 21 to be completed between 2012 and 2016.

5.1.4. EU and Member States actions on mutual accountability and managing for results

Mutual accountability lies at the heart of the Paris Declaration, and is a process by which two or more partners agree to be held responsible for the commitments that they have voluntarily made to each other. It helps build trust and partnership around shared agendas and provides incentives for behaviour change needed to achieve better results. A central aspect is making aid flows more transparent. As stated in the Operational Framework on Aid Effectiveness[167], "in the Accra Agenda for Action, donors and partner countries agreed to provide timely and detailed information on

[167] Consolidated version: IV Accountability and transparency, paragraph 1

current and future aid flows in order to enable more accurate budget, accounting and audit by developing countries".

The new EU development policy as set forth in the 'Agenda for Change' calls for "comprehensive approaches to domestic and mutual accountability and transparency." At this stage, 16 Member States already participate in mutual accountability arrangements in more than 10% of their priority countries, eight of which do so in 50% or more of their priority countries.

Performance Assessment.

Performance assessments use mostly policy dialogue (16 Member States use them), but consultative groups (12) and joint review panels (10) are also present. Fourteen Member States participate in Performance Assessment Frameworks, but only a few Member States have currently a formal result framework in place. Eleven Member States are active in the post-Busan activities of the Building Bloc on Results and Accountability. Fourteen Member States support partner countries' statistical capacities for monitoring progress and evaluating impact. Fifteen Member States participate in country-level results framework and platforms in more than 10% of their priority countries, and 7 in 50% or more of their priority countries. The Commission has recently proposed a common result reporting framework that could accelerate adoption of a harmonised way to monitor performance at the country level.

Making aid more transparent.

Most EU non-DAC donors report their ODA to the OECD/DAC. The Commission encourages all of them to do so, in line with the OECD/DAC reporting rules, although none of the EU-12 is yet a DAC member. Bulgaria is the only Member State that has yet to start reporting systematically to DAC. The Commission will continue to work with the DAC secretariat to provide support to the EU's non-DAC donors to enhance their statistical reporting capacity. The EU15 countries have all adhered to the new DAC CRS++ reporting formats.

The International Aid Transparency Initiative (IATI) was launched in 2008 to develop consistent and coherent international standards so that donors report more timely information on past and future aid spending. The European Commission and eight Member States (i.e. Denmark, Finland, Germany, Ireland, Netherlands, Spain, Sweden and the United Kingdom) are signatories to IATI, and are implementing or are preparing to implement its standards. Belgium has decided to join IATI, while the Czech Republic is designing a new ODA internal reporting system in full compliance with IATI standards, and Estonia is exploring the possibility of making its ODA statistics compatible with IATI standards.

Nineteen Member States have developed and use national aid transparency tools, usually through their development cooperation's websites, and annual reports. Denmark is preparing a new law on International Development Assistance that will require increased transparency both at partner country level, and domestically. The EU adopted the EU Transparency Guarantee in November 2011, while both Sweden and the United Kingdom launched national Aid Transparency Guarantees in 2010 (see **Box 5.1.4.a**).

Box 5.1.4a – Aid Transparency Guarantees

- In November 2011, EU Foreign Affairs Ministers agreed on **the EU Transparency Guarantee**, ensuring that EU Member states will publicly disclose all information on aid programmes so that it can be more easily accessed, shared and published. It will also make information available on all aid to partner countries, to enable them to report them in their national budget documents and help increase transparency towards parliaments, civil society and citizens.
- In 2010 **Sweden** introduced a transparency guarantee into its development cooperation. The guarantee means that all public documents and public information will be made available online. The information shall explain when, to whom and why money has been made available, and what results have been achieved. Sweden's flagship website - www.openaid.se - was launched in 2011. Openaid.se is a democratic initiative, facilitating accountability towards Swedish tax payers as well as towards people in Sweden's partner countries, by opening up development cooperation to the public. It is a data-hub providing Swedish aid information on disbursements in an open format. This means that the format allows for citizens, CSOs and entrepreneurs to use, refine, and develop the data provided. The aid information is provided on a global scale, at country level, per sector or by implementing agency. It covers a time period of four decades. The Swedish Government is committed to continuing its implementation of the transparency guarantee and supports initiatives such as the Open Government Partnership, the Open Aid Partnership, and the EU Transparency Guarantee (see below).
- The **UK** Aid Transparency Guarantee was launched in June 2010. It commits the United Kingdom to publishing detailed information about new DFID projects and policies in a way that is comprehensive, accessible, comparable, accurate and timely. Information will be published in English and with summary information in major local languages, in a way that is accessible to citizens in the countries in which DFID works. The United Kingdom will allow anyone to reuse its information, including for the creation of new applications which make it easier to see where aid is being spent. The United Kingdom will finally provide opportunities for those directly affected by its projects to provide feedback on their performance.

The European Commission has developed an information gathering tool called Transparent Aid (TR-AID) to support sharing of aid information across major international donors with the aim of using aid funds most effectively. Sharing of aid data with the public and amongst donors has always been a challenge, due to a large number of data formats in use, and because data is available in different repositories. (see **Box 5.1.4.b**).

Box 5.1.4b – TR-Aid

- TR-AID incorporates data from multiple sources in varied formats, and allows the publication of comprehensive information about both development and humanitarian aid. These include data from the OECD (Organisation for Economic Cooperation and Development), UN OCHA (United Nations Office for the Coordination of Human Affairs), and some EU Member States (Greece, Spain and Belgium for example). TR-AID imports data in different formats such as comma separated values, excel, xml etc. TR-AID implements the first phase of IATI thus making it compliant with the standard proposed, and potentially opening TR-AID up to incorporate any data published via the IATI registry.
- TR-AID is not yet available for the public, a step foreseen for late 2012.
- The TR-AID user interface is currently available in English, French, Spanish, Italian and German, with plans to make it available in the 23 official languages of the EU by early 2013. The users can search the database for information relating to projects such as sectors, aid type, flow type, markers, status, countries, regions, etc. They can also search for organisation details such as those relating to recipients, implementing partners and donors.

5.1.5. The Post-Busan Dialogue on Development Effectiveness

The EU and its Member States played an active and constructive role in the Busan Fourth High-Level Forum on Aid Effectiveness as well as during its preparation. The Busan outcome document is in line with the priorities of the EU and its Member States: it is inclusive, it focuses and deepens aid effectiveness commitments while expanding to development effectiveness and, finally, it emphasises country level implementation while scaling down global governance structures.

Final decisions on the mandate and the governance structure of the Global Partnership as well as monitoring framework set in the Busan outcome document were made by the Working Party on Aid Effectiveness in late June. The main function of the Global Partnership will be to ensure continued accountability at the political level based on the evidence arising from country level implementation. Global monitoring arrangements, in turn, will build on country level monitoring processes based on a global set of core indicators on Busan priority themes. The decisions of the Working Party were based on the proposals negotiated by **the Post-Busan Interim Group.** From the EU and its Member States, the Commission (representing the EU), the United Kingdom, Germany and Sweden were members of the group and played an active role in it.

As stated in the EU Common Position for Busan, **the priority after Busan is to focus on the country level implementation of its aid and development effectiveness commitments**. As shown by the available evidence, country-led and country-level results and mutual accountability frameworks are essential elements of country level implementation and partner countries' leadership. Many EU Member States are already engaged in these frameworks. However, there is room for further collective EU action to strengthen these frameworks or support their establishment. The EU and its Member States are progressing in implementing division of labour principles at the country level. This continued progress may provide opportunities to support country level implementation beyond complementarity and division of labour.

5.2. Supporting better Global Governance

5.2.1. The Evolving Global Context

The EU Common Position for the Fourth High Level Forum on Aid Effectiveness emphasised the importance of effective delivery for improving the quality of aid and increasing the impact of development financing from all sources.

Improved global governance is one of the means for achieving this objective. It involves broadening cooperation will all relevant development partners, reducing and streamlining the global governance structure, and using existing mechanisms and fora to promote the aid and development effectiveness agenda and monitor its implementation.

In that context, **reducing aid fragmentation is a central challenge in order to move from individual country strategies towards partner country-led joint assistance strategies and to streamline the multilateral aid architecture.** The EU is committed to self-restraint with regard to avoiding further proliferation of global and thematic programmes or vertical funds, and to use and strengthen the existing channels. The existing structures, notably UN, World Bank/IMF, regional structures, G20 and DAC should be used as fora to discuss aid effectiveness implementation and to strengthen wide development partnerships.

The issue of institutional framework is also taken-up under the auspices of the OECD/DAC as the follow-up to the Busan Forum. The process aims to (a) establish a new, inclusive and representative Global Partnership for Effective Development Cooperation to support and ensure accountability for the implementation of commitments at the political level; and (b) agree on light working arrangements for this Global Partnership, including its membership and opportunities for regular ministerial-level engagement that complements, and is undertaken in conjunction with, other fora. Representatives from the EU, Sweden and UK are members of the working group considering this issue.

EU Member States are contributing to the processes described above. For example, the UK played a full role in negotiations leading to agreement at the Busan High Level Forum on Aid Effectiveness to form a new Global Partnership for Effective Development Cooperation. This sets the stage for a new development architecture reflecting a broader and more inclusive partnership for development than ever before.

5.2.2. *Reforming Multilateral Institutions*

The 2011 Accountability Report provided a detailed account of the status of these reforms and only recent evolutions are presented herein. As mentioned above, the proposed continued reliance on existing structures underscores the importance of completing the reforms of multilateral institutions.

A number of recent studies by EU Member States help identify areas of improvements for multilateral organisations. While primarily focused on efficiency and aid delivery, these studies have a bearing on governance of these organisations from the standpoint of responsibilities of their boards and how they operate. Partly because of the differing objectives and methodology, there is no common platform used by EU Member States to undertake such studies. The **UK's** 2011 Multilateral Aid Review[168] (MAR) provided a comprehensive overview of the strengths and weaknesses of the multilateral organisations that DFID works with. The MAR confirmed that the multilateral system is a critical complement to what any government can do alone. It also found evidence of significant weaknesses. DFID has thus drawn on its value for money assessment to decide on funding through multilateral organisations, communicated its key reform priorities to each multilateral organisation and engaged closely both with the institutions themselves and their boards, and with other stakeholders to promote reform. Other EU Member States are also involved in assessments of multilateral organisations, notably through the Multilateral Organisation Performance Assessment Network (MOPAN).[169] Similarly, **Sweden** has made assessments of multilateral organisations[170], which are an important part of the implementation of its strategy for multilateral development cooperation. Lastly, in 2011 **Denmark** initiated its first full-scale annual multilateral review aimed at strengthening the strategic approach and coherence in its engagement in multilateral organisations system-wide.

5.2.2.1. IMF, World Bank and other international fora

The issue of improved African representation and voice, such as the African Union, in international fora, such as the G20, **remains very important to the EU**.

The EU sees the implementation of the World Bank voice and participation reforms agreed in April 2010 as a priority. In accordance with the second phase of voice reforms of March 2011, the voting power of developing countries and transition economies in the International Bank for Reconstruction and Development (IBRD) increased by 3.1 percentage points to a total of 47.2%. Under the new reforms, the Bank is required to review its shareholding every five years, starting in 2015. Also in April 2011 the Executive Director Board approved a new process for selecting the World Bank President and then, for the IMF Managing Director. The process has been improved by adopting the recommendations of the Executive Directors' Working Group which was created in response to the Development Committee Communiqués of 2010 calling for open, merit-based and transparent selection of the World Bank President.

[168] http://www.dfid.gov.uk/Documents/publications1/mar/multilateral_aid_review.pdf
[169] http://www.mopanonline.org/ Austria, Belgium, Denmark, Ireland, Finland, France, Netherlands, Norway, Spain, Sweden and UK are members of MOPAN.
[170] http://www.sweden.gov.se/sb/d/11747/a/122004

The IMF quota reform[171] agreed in 2010 will, once approved, shift more than 6% of quota to dynamic emerging market countries and from over-represented to under-represented countries; significantly re-distribute quotas and preserve the voting share of the poorest countries. Once implemented, the voting shares of US and EU members will fall below 50%. The EU intends to fully implement the 2010 quota and governance reform of the IMF by the agreed deadline of the 2012 Annual Meetings. A significant number of EU Member States have already concluded national ratification procedures in that direction. The process is on-going in the remaining Member States and is projected to be completed by most Member States during 2012. Moreover, by consenting to two fewer seats for advanced European economies once the 2010 quota reform becomes effective, EU members will play their part in giving emerging markets and developing countries more visibility in the IMF Executive Board. Furthermore, the move to an all-elected Board will create a level-playing field for all IMF members. The Commission is continuously working to deepen and broaden the coordination between EU Member States, in order to strengthen Europe's voice in the IFIs.

As regards Commission - IFI strategic relations in the area of development~~,~~ a Taskforce has been established for an Enhanced Dialogue with International Organisations, focusing on the IFIs. The taskforce aims to develop a platform for a more structured dialogue with the IFIs (IMF, World Bank Group, Asian Development Bank, African Development Bank, Inter-American Development Bank) at senior management level, to identify joint actions and intervention frameworks in areas of mutual interest, and to formulate, co-ordinate and promote Commission and EU positions on development issues in the IFIs. Since the creation of the task force, dialogue and cooperation with the IMF (vulnerability/resilience in LICs, budget support and public financial management, capacity building) and the World Bank Group (private sector development, fragility and conflict situations, budget support) have been enhanced, with far more frequent meetings with the Bretton Woods institutions at senior management and political level.

5.2.2.2. Other initiatives

The following notable initiatives were launched recently:

- The close cooperation between the EU, and the EIB and EBRD, particularly in the Neighbourhood region and (for EIB) ACP region was strengthened in 2011 and a new Tripartite MoU between the EC, EIB and EBRD on cooperation outside the European Union was signed in March 2011.

- There is also a Commission proposal[172] to the European Parliament and the Council to extend EBRD's mandate to the Middle East and North Africa region.

[171] An IMF paper analysing quota reforms was issued in 2011: "Global Economic Governance: IMF Quota Reform". http://www.imf.org/external/pubs/ft/wp/2011/wp11208.pdf

[172] http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2011:0905:FIN:EN:PDF

ANNEXES

See Vol.2.