THE DEVELOPMENT ASSISTANCE COMMITTEE:
ENABLING EFFECTIVE DEVELOPMENT

DAC SENIOR LEVEL MEETING
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Measurement of Development Finance Post-2015

- Emerging Concept of Total Official Support for Development
- Treatment of Market-Like Instruments
- Action Plan to Achieve a More Balanced Distribution of ODA

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CHAPTER 1: TOTAL OFFICIAL SUPPORT FOR DEVELOPMENT - AN EMERGING CONCEPT IN SUPPORT OF THE POST-2015 SUSTAINABLE DEVELOPMENT GOALS

Introduction

1. The DAC High Level Meeting (HLM) of December 2012 provided a comprehensive mandate for exploring new ways to measure development finance, acknowledging the need to adapt statistical concepts in light of the profound changes in the global financial and economic landscape. This work should ensure the continued relevance and credibility of key measurements of development finance. As appropriate, new measures might be introduced, such as Total Official Support for Development (TOSD), and existing ones – notably Official Development Assistance (ODA) – modernised.

2. The UN's Open Working Group for Sustainable Development Goals (OWGSDG) has now reached consensus on key features of the international development framework that will succeed the Millennium Development Goals. They propose a post-2015 Sustainable Development Agenda that is universal, leaves no one behind and is predicated on *"goals and targets [that] integrate economic, social and environmental aspects and recognise their interlinkages for achieving sustainable development in all its dimensions"*[1]. Sourcing and deploying adequate and sustainable resources to meet these goals will be critical for successfully implementing this ambitious agenda. International public finance – including ODA, but also official contributions beyond ODA – will be an important component of the resource mix. The proposed new TOSD measure, which is designed to better capture and recognise these resources, could play a vital role in helping developing countries and their development partners grasp the totality and nature of finance on offer – and enhance strategic planning, oversight, and international accountability in the post-2015 era.

3. The Report of the Intergovernmental Committee of Experts on Sustainable Development Financing emphasises the need for making use of "all financing flows in a holistic way", which includes domestic public, domestic private, international public and international private financial resources. TOSD has the potential of enabling further resource mobilisation by tapping all these types of flows.

4. The March 2014 DAC Senior Level Meeting (SLM) acknowledged the utility of taking into account broader official contributions to development, including various financial instruments not yet reported on in a systematic and consistent way across members. In terms of overall guiding principles, the SLM agreed that the TOSD would provide a more comprehensive measure of donor contributions addressing global challenges and enablers of development (*e.g.* climate change, peace and security) and valorise market-like financial instruments in a broader sense (this is independent from the discussion on counting the donor/budgetary effort associated with these types of instruments[2]), essential for maximising resource mobilisation efforts in view of the post-2015 sustainable development agenda. With regard to the latter, it recommended paying particular attention to differentiating between official flows and finance mobilised from the private sector thanks to official actions. Subsequent discussions in the DAC (July 2014) have emphasised that only official flows should be included in the TOSD measure and that relevant private flows could be reported as a separate aggregate for memorandum. The Expert Reference Group on Development Finance also recognised the importance of capturing all resources provided and leveraged outside of ODA in a transparent manner, but recommended limiting TOSD to measuring official flows/outlays in the provision of development finance.

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1 Introduction to the Proposal of the Open Working Group for Sustainable Development Goals, 19 July 2014.

2 See chapter 2, on the treatment of market-like instruments in the post-2015 statistical framework.

5. The October 2014 SLM is a crucial milestone on the path to fully delivering on the DAC's 2012 development finance mandate. The SLM will assess how broader official contributions in support of development can be quantified, valorised and made publicly available to enhance international accountability. The December 2014 HLM will be invited to endorse the narrative and the main features of the TOSD concept – without prejudice to the UN process of final negotiations on the Sustainable Development Goals (SDGs) and the outcomes of the 21st Conference of Parties of the UN Framework Convention on Climate Change (UNFCCC) and the third Financing for Development Conference. This paper lays out the building blocks and definitional elements of the concept for DAC members' consideration.

Developing the TOSD concept

Scope and narrative

The core TOSD narrative starts from the proposition that achieving the ambitious forthcoming Sustainable Development Agenda will call for mobilising finance on an unprecedented scale to tackle challenges – such as climate change, peace and security, contagious diseases and inequality — that transcend borders, threaten development progress and human well-being everywhere, and call for collective action by the global community.

A defining feature of TOSD is that – while it would ensure that relevant flows are supporting the economic development and welfare of developing countries – it would also acknowledge benefits for the providing country. The notion of "mutual benefit" would therefore be an acceptable feature of the measure. Accordingly, TOSD would mirror in important ways the features of globalisation, including technology, trade and investment flows, which have characterised growth and development worldwide over the past two decades and continue to do so in the future. At the same time, the measure would need to withstand critical public scrutiny: steps would be required to ensure that TOSD statistics are carefully validated as legitimate expenditures within the definition of the measure.

The universality of the measure would ensure its relevance for providers beyond the DAC.

6. The TOSD measure should be considered as a measure in its own right with its own narrative and definition. It should be conceived and presented as a complementary measure to ODA (rather than encompassing ODA). **TOSD is not an excuse to back away from existing ODA commitments.** The 0.7% ODA to GNI target will remain the cornerstone of international accountability.

7. The exact coverage of TOSD may need to be adjusted once the final SDGs have been established. In the meantime, the DAC can offer the international community a credible narrative of measuring and monitoring total official support for sustainable development to inform the upcoming policy discussions and recommendations focusing on the financing for development agenda.

8. With ODA measuring the donor effort, TOSD would cover the totality of official resources in support of sustainable development, regardless of the terms under which they have been granted.

9. TOSD should be a universal measure that could be useful to development finance extended by sovereign providers beyond the DAC. Its focus on sustainable development, with the underlying rationale of mutual benefit, could create incentives for other providers to subscribe or align to TOSD. This could

facilitate forging innovative alliances and co-financing arrangements in the post-2015 era, in line with the spirit of international partnership as prefigured by the OWGSDG in the proposed goal 17. Indeed, development co-operation has evolved significantly from a north–south relation towards an international partnership for sustainable development, which brings together all actors, including DAC members, developing countries, south–south providers, multilateral institutions and other international partnerships.

Building blocks – elements of definition

10. TOSD would have a "purpose-based" definition. **While promoting the ultimate objective of "economic development and welfare of developing countries", TOSD may have other equally important objectives and the providers may themselves benefit from the activities.** This is different from ODA, which is administered with the promotion of the economic development and welfare of developing countries as the **main** objective.

11. In practice, a purpose test that is softer than ODA would entail inclusion in TOSD of contributions to Global Public Goods (*e.g.* research and development of technologies to combat climate change) and Enablers of Development (*e.g.* peace and security expenditures). Moreover, the fact that some degree of self-interest would be permissible under the measure would also allow for a broader coverage of activities promoting trade and exports. As a consequence, **TOSD could potentially also include official export credits if it can be demonstrated that the funding addresses the objective of sustainable development**.[3]

12. In addition to the purpose test – "promoting the economic development and welfare of developing countries as an important objective" – and to avoid all international co-operation qualifying as TOSD, it will be necessary to accompany the general definition with more operational criteria. It is proposed that, for activities carried out in developing countries, TOSD eligibility would require **alignment with the development priorities of the recipient country**. Unlike ODA, the TOSD definition would not include a required level of concessionality – all official resources for sustainable development will be considered irrespectively of their terms and conditions.

13. Finally, TOSD would need to withstand critical scrutiny by the public – and therefore statistical reporting on the measure would need to be transparent, implying activity-level reporting on commitments and disbursements. With regard to market-like instruments, in particular when finance is extended to non-sovereign entities, it will be necessary to respect commercial confidentiality of information on terms and conditions of finance as well as profits and defaults which could however be reported at aggregate level.

Main features of the measure

14. **All financial instruments, including those generating reflows to provider countries, would qualify as TOSD**. As a first step toward a more comprehensive statistical framework, the WP-STAT, at its September 2014 meeting, agreed in principle to update the DAC classification by type of finance[4]. New statistical categories will be created in particular for mezzanine finance instruments, shares in collective investment vehicles and guarantees, all of which are expected to feature in TOSD. (See Table 1.)

15. The DAC's recommendation to **distinguish between official and private resources** (see paragraph 4) calls for greater clarity regarding which flows would be included in TOSD in practice when it

3 Note however that 85% of officially supported export credits reported to the OECD represent private export credits guaranteed or insured by official export credit agencies.

4 Cf. DCD/DAC/STAT(2014)13 for the detailed proposal to modernise and update the DAC classification by type of finance, approved in principle by the WP-STAT at its meeting on 16-17 September 2014.

comes to market-like instruments that aim to leverage additional private finance. While not pre-empting forthcoming decisions on how donor effort can be measured[5] for example in the case of guarantees, it could be conceived that the amounts mobilised by the guarantees – typically investments by the private sector – would be reported in a separate memo item to TOSD and that the relevant official sector contribution be valorised in TOSD, thus maintaining a clear **distinction between flows and contingent liabilities.** More generally, a modernised DAC statistical framework should provide better information on the blending of different sources of finance and how governments leverage official resources with private capital through risk-sharing schemes.

Table 1. Landscape of instruments of development finance

Broad category	Description and subcategories
GRANTS	**Grants** are transfers in cash or in kind for which no legal debt is incurred by the recipient. **Capital subscriptions** to multilateral agencies are for most purposes assimilated to grants in DAC statistics.
DEBT INSTRUMENTS	Debt instruments require the payment of principal and/or interest at some point(s) in the future. Debt instruments can take the form of **loans** and **debt securities** (*e.g.* bills, bonds, notes, negotiable certificates of deposit, commercial paper, debentures, asset-backed securities, money market instruments, and similar instruments normally traded in the financial markets).
MEZZANINE FINANCE INSTRUMENTS	Mezzanine finance, also called hybrid finance, refers to instruments relating to the layer of financing between a company's senior debt and equity, with features of both debt and equity. Mezzanine finance includes **subordinated loans, preferred equity and other hybrid instruments**.
EQUITY AND SHARES IN COLLECTIVE INVESTMENT VEHICLES	Equity and shares are particularly relevant for supporting private sector development. It provides recipient institutions (private companies or collective investment vehicles) with the capacity of increasing their assets. Investing in developing economies is often deemed too risky by the private sector unless public sector institutions invest risk capital. This category includes **common equity, shares in collective investment vehicles and reinvested earnings**.
DEBT RELIEF	Debt cancellations, debt conversions, debt rescheduling within or outside the framework of the Paris Club.
GUARANTEES AND OTHER UNFUNDED CONTINGENT LIABILITIES	Guarantees or insurance, by reducing the risk, facilitate borrowers' access to the financial market and/or enable them to borrow at more favourable terms.

16. TOSD would be measured on a **gross** basis to capture the total monetary value of finance made available in any given year (for example, loans would be recorded at face value). Data on a **net** basis would also be collected to present a comprehensive picture of development finance from the recipients' perspective. Thus TOSD would feed into data series on developing countries' resource receipts – Resource Inflows for Development – in the same way that country programmable aid would be included.

17. Under TOSD **all purposes/sectors or thematic areas** are equally valid and should be aligned with the framework that will be provided by the final SDGs and developing countries' individual development strategies.

18. In comparison with the current measurement framework, TOSD would, in the case of DAC members, include all ODA, elements of other official flows – OOF (a share of investment-related and possibly export-related expenditures) and additional flows beyond, *i.e.* financing for sustainable development not covered in DAC statistics at present. The relation between TOSD and modernised ODA

[5] There is an increasing consensus among members to modernise ODA to also include donors' budgetary effort involved in the use of market-like financial instruments. See chapter 2 below.

depends on the decisions that the DAC will take with regard to assessing concessionality and reporting on loans. If modernised ODA measures loans in terms of grant equivalents, TOSD and ODA will be two distinct statistical quantities. If reporting on loans continues on a cash-flow basis, modernised ODA will rather be a sub-set of TOSD. For interested providers beyond the DAC, TOSD would comprise concessional and non-concessional financial instruments provided for development.

Implications for key thematic areas and channels of delivery

Climate change

19. TOSD can be an enabler for promoting development that is environmentally sustainable, climate-resilient and based on low-carbon emissions. Better tracking can help to shift both public and private, domestic and international finance away from "brown" and into "green" investments; it can in this way help to scale-up "green" finance and integrate environmental considerations into all relevant investment decisions and government activities. The SDGs reaffirm the role of the UNFCCC leadership on climate change, and include recognition of the commitment under UNFCCC by developed country parties to jointly mobilise USD 100 billion per year by 2020 from a variety of sources. The form and scope of TOSD, as proposed here, could contribute to UNFCCC monitoring and measurement of climate finance. Climate change is a cross-cutting policy theme and the DAC statistical system for tracking policy objectives such climate change (adaptation and mitigation) is geared to support this. Many climate mitigation and adaptation projects funded by DAC members are already included in DAC statistics and work is underway to further improve the quality and coverage of this reporting. Going forward, the extension of the coverage of DAC statistics to capture financial instruments such as guarantees and insurance schemes would greatly facilitate the measurement and monitoring of broader provider support for climate change mitigation and adaptation in developing countries.

20. A new TOSD measure could include climate-related activities that, under current definitions, do not count as ODA as their main objectives may not be developmental but rather in line with the provision of global public goods. This includes activities beyond ODA and OOF such as support to innovative technologies such as Carbon Capture and Storage and supporting early-stage technological research and development (to catalyse future cost-reductions and enhance commercial viability). These activities are crucial for promoting efficient action on climate change in developing countries. Projects funded through export credits, for example in the area of renewable energy, could be equally beneficial for sustainable development. In this respect, a key question in discussing the outer boundary of TOSD relates to the treatment of export credits.

Peace and Security

21. Conflict, violence and political instability are holding back global development, including progress on the MDGs. The proposed 16th SDG strives to "*Promote peaceful and inclusive societies for sustainable development, provide access to justice for all and build effective, accountable and inclusive institutions at all levels"* and will help ensure that the post-2015 framework will channel investment in the right places and help address drivers of conflict, violence, and instability effectively. The DAC is currently looking into the need for updating the ODA-eligibility criteria in this area to reflect the current scope of peace and security assistance. The principles guiding this update are expected to be endorsed at the forthcoming HLM. Under a TOSD measure a broader range of expenditures related to peace and security would be permissible, including those relating to the provision of military equipment and services. In practice this would entail the inclusion of activities ranging from ODA-supported programmes to broader security sector reform and counter-terrorism activities in developing countries. In previous discussions on TOSD it has also been suggested that the totality of assessed contributions to UN peacekeeping operations should be included. In setting the outer boundary of TOSD in the field of peace and security, the provision

of lethal equipment and training for security forces would need to be clarified, taking into account the reputational risks involved.

Trade and exports

22. An elaborate set of international rules governs concessional financing provided by governments. The rules have evolved through co-operation among industrial countries, which are major creditors as well as major exporters of capital goods. The rules set boundaries on the terms and conditions on which these countries can offer official financing. The primary purpose of the rules is to ensure that governments provide financing in ways that minimise trade distortions and safeguard the quality of aid allocations, including value for money. The application of the existing OECD rules or not to TOSD would need a separate discussion once the outer boundary of TOSD has been set. With regard to the WTO Agreement on Subsidies and Countervailing Measures, there should be no particular issues concerning grants and loans. However, for other financial instruments an assessment of compliance would also require a separate discussion.

Multilateral channels of delivery

23. TOSD will valorise bilateral support for sustainable development but also resources channelled through the multilateral institutions. TOSD would capture providers' full contributions to norm-setting by multilateral agencies with the reasoning that their activities, while benefiting developed and developing countries alike, are essential for enabling sustainable development. In addition TOSD should also capture full contribution to multilateral agencies that undertake activities/programmes in the area of human rights and justice. Multilateral peacekeeping missions authorised by the UN Security Council have a clear developmental and humanitarian intent, have proven to enable development and should thus be included. More generally, the entire UN budget (of which currently only 18% is ODA-eligible) could be considered TOSD-eligible.

24. The general inclusion in TOSD of market-like finance – often raised from the capital markets under a guarantee from the provider government – raises the question of whether similar operations by the multilateral development banks and international financial institutions, guaranteed by the shareholders, should be attributed to the providers. Callable capital to these institutions could be treated in a similar way as other contingent liabilities.

Ways forward and request for guidance

25. The international community, including developing countries, recognises the importance of securing sustained financing levels for the ambitious post-2015 development agenda. DAC members have an important contribution to make by offering a transparent and comprehensive measure of resources and efforts being undertaken by the development co-operation community to finance sustainable development, a measure that is sufficiently concrete to help guide allocation decisions towards the SDGs, and sufficiently flexible to allow for its further tailoring in accordance with evolving requirements from the broader international community. A final decision on TOSD may need to be adjusted following the agreement of the SDGs, but the building blocks of the new measure as described above could already be agreed upon at the HLM at the end of the year.

26. **Taking account of the proposed narrative, the SLM is invited to provide recommendations on the scope and definitional elements of the measure which will allow it to be fine-tuned in time for HLM endorsement. SLM participants are invited to:**

- **agree on the proposed scope and narrative of TOSD, that:**
  - reflects a broader, more universal development agenda;
  - has the economic development and welfare of developing countries as a key objective;
  - includes contributions to global public goods when these are deemed relevant for development;
  - may include mutual benefits to the provider and the recipient of the funding;
  - originates from official sources;
  - includes both concessional and non-concessional financing; and
  - is calculated on gross terms.
- **suggest any additional elements that could potentially be considered in TOSD.**
- **provide clear recommendation as regards the outer boundaries of TOSD in particular in the areas of climate finance, peace and security, and trade and exports.**
- **consider renaming the concept to align it with the terminology used in the context of the financing for development narrative:** ***e.g. International Public Finance for Development.***

CHAPTER 2: TREATMENT OF MARKET-LIKE INSTRUMENTS IN THE STATISTICAL FRAMEWORK MEASURING AND MONITORING DEVELOPMENT FINANCE POST-2015

27. Market-like instruments (including equity and shares in collective investment vehicles, mezzanine finance instruments and guarantees) have gained more and more attention in development finance in recent years as they help to narrow the profound financing gap to fund sustainable development in two ways. First, they constitute an important form of financing in themselves, with features that cannot easily be mirrored by other instruments (e.g., ownership rights and responsibilities when investing in an equity stake). Second, they have the potential to crowd in additional private funds, both by mitigating the risk for and by demonstrating the financial viability of projects to private investors. Such instruments are employed in particular by development finance institutions (DFIs) mandated to invest in the private sector for development purposes – this explains why they are often referred to as **"private sector instruments"**. In principle, however, they can be used to finance both public and private sector entities.

28. There is broad agreement that the present ODA reporting does not sufficiently recognise and incentivise these instruments. In accordance with the 2012 DAC High Level Meeting (HLM) mandate, work has therefore been carried out over the last 18 months to map the development finance landscape and better understand the functioning of market-like instruments and their potential to leverage other resources. Statistical categories and methods have been developed for monitoring their use. Major steps forward were taken at the meeting of the Working Party on Development Finance Statistics (WP-STAT) on 16-17 September 2014 where members approved in principle a new taxonomy for financial instruments[6] alongside with an expansion of the DAC statistical collection to include the mobilisation effect of official development finance. (See Box 1.)

29. **There are different ways in which market-like instruments could be better reflected in ODA reporting, and the SLM is invited to give strategic guidance in the lead-up to the HLM.** Members have previously stated that recognition of the effort involved in the use of market-like instruments would create further incentives for their use. There seems therefore to be broad agreement that as a minimum, ODA modernisation should remove the disincentives embedded in the current reporting system. (Given that reporting is based on net disbursements, positive sales proceeds from any ODA equity investment score as negative ODA.) Two main approaches to addressing these issues are being explored: an assessment of donor effort instrument by instrument, or including in ODA governments' contributions to their national DFIs. (See Box 2.)

30. **In general, it would seem important to ensure that the overall statistical framework remains coherent.** Concrete proposals on the measurement of donor effort involved in the use of market-like instruments should therefore be synchronised with the conclusions of the ongoing discussion on assessing concessionality and the reporting on loans in ODA. A grant equivalent approach in ODA loans reporting could facilitate the development of methodologies for calculating the grant equivalents of equity, mezzanine instruments and guarantees. If ODA reporting remains on a cash-flow basis, it would seem more challenging to include non-flow instruments, at least on an instrument-by-instrument basis.

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6 See chapter 1, Table 1.

Adoption of a risk-adjusted approach for loans would also logically make it more relevant to valorise risk-taking in the reporting on other non-grant instruments which are designed to mitigate the risks that private investors are not willing to take.

Box 1. Measuring the mobilisation effect of official development finance

The question on how to use ODA in "smarter" ways to **mobilise additional resources** for development – and **how to measure and valorise** these resources – has been at the core of political discussions on development finance for several years. The question is most relevant also for the climate community that has committed to mobilise, by 2020, USD 100 billion for climate change mitigation and adaptation in developing countries. Monitoring climate finance and the fulfilment of this commitment has shown to be complex, due to unclear definitions and lack of internationally accepted methodologies for reporting on mobilisation.

To address these challenges, and in accordance with the HLM mandate, the WP-STAT has explored the scope for expanding the DAC statistical system to collect data on private sector resources mobilised through risk-mitigation and other instruments with a potential leveraging impact. Following a Survey on guarantees for development in 2013, a Survey on the mobilisation effect of official development finance in 2014 and consultations with members and DFI experts, a first **proposal for collecting data on amounts mobilised** was presented for consideration by the WP-STAT at its meeting on 16-17 September 2014.

Members welcomed progress in work on the mobilisation effect of official development finance and saw the proposal as an **initial concrete step towards a system for recording, at the activity level, the private funds raised for development by all official actions that have mobilisation as an explicit objective**. It focused on financial mechanisms for which the Surveys demonstrated that it was feasible to measure amounts mobilised in the short-term, namely:

- **Syndicated loans**. A syndicated loan is one provided by a group of lenders (called a syndicate) who work together to provide funds for a single borrower. The main objective is to spread the risk of a borrower default across multiple lenders, and thus encourage private investment.

- **Guarantees for development**. Guarantees facilitate the mobilisation of finance by transferring or mitigating risks that private investors would not be able or willing to take.

- **Shares in collective investment vehicles**. Highly rated investors (e.g., development finance institutions) increase the creditworthiness of the collective investment vehicle, and thus provide a positive signal to the market and attract private finance that may not have invested otherwise.

WP-STAT members approved the proposal in principle and the work plan to revise the Directives accordingly. Members encouraged the Secretariat to carry out further work to expand the coverage of the measurement to other financial instruments such as direct equity and mezzanine finance instruments.

31. Pending agreement on the treatment of loans, and given that members have specifically requested that ODA modernisation resolves the issue of disincentives, members are invited to consider a **two-phased approach** where, as a first step, the **"institutional approach"** be adopted for reporting on market-like finance to the private sector. It is technically relatively easy to implement, although it would require clarifying which institutions are considered as DFIs and whether only capital contributions, or capital contributions and reinvested earnings, would be reportable as ODA. As a second step, **"instrument-specific solutions**" would be developed further in alignment with the treatment of ODA loans, expected to be decided upon at the HLM in December 2014. Further discussions would be required on the question of whether some flexibility could be built in the reporting system as suggested by some members.

32. In any case, within the current framework, there would be scope to address the issue of disincentives by aligning the treatment of ODA equity investment with that of ODA loans, *i.e.* limiting the

measurement of net cash flows to the initial investment value.[7] The question that arises, however, is whether data on profits from sales of equity should be collected for transparency purposes; some members have also suggested that a good practice would be to ensure these profits are reinvested for development.

Box 2. Recent approaches to accounting for the donor effort of market-like finance

Recent discussions in the DAC, its Expert Reference Group and the WP-STAT have all stressed the need to account for market-like instruments in a consistent, instrument-neutral and easily justifiable manner in modernised DAC statistics. While members have made significant progress in their thinking on how to capture the totality of official flows and private flows mobilised by official efforts in the new measurement system complementing ODA, views are still divided on how best to estimate the donor effort involved, *i.e.* the ODA-eligible portion, in the deployment of such instruments.

Recent discussions for valuing and thus reflecting such instruments in ODA have focussed on direct private sector financing. As most – albeit not all – bilateral private sector financing is channelled through Development Finance Institutions (DFIs), some members suggest an **institutional approach**. Instead of trying to calculate the degree of concessionality for each activity, they propose changing the point of measurement from outflows to inflows for DFI operations, *i.e.* counting in ODA official capital contributions to DFIs and potentially also reinvested earnings. Members supporting this approach point to the relative simplicity and hence feasibility of reporting which would not require any instrument-specific concessionality test or calculation considered as too complex or arbitrary. They furthermore argue in favour of conceptually aligning the treatment of bilateral DFIs with the treatment of International Finance Institutions (IFIs) which operate under a comparable mandate and for which capital contributions are already counted in ODA under the current system. When following this proposal, complementary solutions would still have to be developed for accounting for market-like instruments that are provided by those other than DFIs.

Several other members favour an **instrument-specific approach** in which market-like instruments are reported on in the same manner as grants and sovereign loans, *i.e.* defining in which circumstances the instruments are ODA-eligible and counting either the relevant flows in a flow-based system or the estimated ODA grant equivalents in a grant equivalent system. Such an approach would be independent of the institutional set-up within donor countries and could incorporate market-like instruments extended to official and private sector entities alike. Members supporting this approach point to the possible application and adaptation of existing financial accounting practices to calculate the associated costs or grant equivalents, while acknowledging that some simplifying assumptions are required to keep reporting simple and feasible.

Some members also suggested an optional choice between the institutional and instrument-specific approach. This would however pose the question on how to ensure statistical comparability and consistency across the membership.

33. **The SLM is invited to agree that:**

- **as a minimum, Reporting Directives be revised to remove the disincentive for the provision of ODA equity investment by capping the reflows to the amount of the initial investment;**
- **in going forward, a two-phased approach be adopted for the treatment of market-like instruments in the DAC statistical framework, as suggested in paragraph 31, where:**
  - **an institutional approach is further detailed with a view to implementing it as soon as possible, and**
  - **technical options for instrument-specific treatment of market-like finance in ODA and TOSD are developed further, synchronised with the agreement on concessionality.**

[7] This would imply reporting the amount of the initial investment as a positive entry and the amount received from divestment as a negative entry but limited to a maximum of the initial investment value.

CHAPTER 3: ACHIEVING A BETTER DISTRIBUTION OF ODA – AN ACTION PLAN TO MEET THE UN COMMITMENT OF 0.15-0.20% OF GNI AS ODA TO LDCS

34. The changing development finance landscape has sparked an international debate on the most appropriate and strategic use of limited concessional resources. While recognising the increasing challenges of sustainable development which affect low and middle income countries alike, there is a growing agreement within the international community that a differentiated approach is needed to ensure a better balance in the global distribution of development finance, and the optimal use of the different types of funding.

35. In the mandate of the DAC High Level Meeting (HLM) of December 2012, it was stated that development finance reform would be carried out "*with a view to ensuring that ODA is directed to where it is most needed and where it can catalyse other flows and promote accountability*".

36. At its Senior Level Meeting (SLM) in March 2014, the DAC expressed support for the continued examination of ways to increase Official Development Assistance (ODA) to those countries where concessional financing is most needed. In May 2014, the DAC debated ways to incentivise a more "needs-sensitive" allocation of ODA, including the setting of operational targets for increasing aid to Least Developed Countries (LDCs).[8] While there was consensus among members that the current trend of decreasing ODA to LDCs should be reversed (see Figure 1), the Committee did not reach a consensus on how to incentivise progress towards the UN targets of allocating at least 0.15% to 0.20% of Gross National Income (GNI) as ODA to LDCs.[9] The DAC Chair in his conclusion encouraged members to reach the UN target on a collective basis. The Expert Reference Group on Development Finance also recognised that sufficient financing needs to be secured for countries where ODA continues to be a major source of external financing.[10]

37. The recent Report of the Intergovernmental Committee of Experts on Sustainable Development Financing emphasised that "*ODA […] will remain critical and should be focused where needs are greatest and the capacity to raise resources is weakest*". A better balance would help ensure adequate means of implementation of the post-2015 development framework as proposed by the Open Working Group for Sustainable Development Goals.

38. **The post-2015 sustainable development financing framework presents an opportunity for the DAC to take leadership and showcase its ambition to improve countries' access to external development finance, including concessional resources, leaving no country behind.**

39. The October 2014 SLM is requested to agree on how to ensure a better balance of development finance including how to accelerate implementation of the UN commitment of 0.15-0.20% of GNI as ODA to LDCs. The SLM deliberations are expected to inform the December 2014 HLM. The DAC discussions are crucial and timely as they are expected to feed into the preparation of the third Financing for Development conference.

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8 See DAC discussion paper, DCD/DAC(2014)20, on Targeting ODA towards countries in greatest need.

9 See Summary Record of 13 May 2014 DAC Meeting [DCD/DAC/M(2014)5/FINAL].

10 Read the Final Conclusions and Recommendations from the Expert Reference Group on Development Finance at: http://www.oecd.org/dac/stats/ERG%20Recommendations%202014%2008%2007%20Final.pdf

Figure 1. DAC ODA to LDCs / GNI

Well justified individual strategic allocations – but a more rounded collective approach is needed

40. Each DAC member has its own priorities, values and set of norms that underpin its development co-operation policy and its strategic allocation of official resources for development. These can be motivated by a focus on poverty alleviation, historical ties, geographical position, global peace and security considerations and climate change and other environmental concerns. More recently, members have also been attentive to enhancing the catalytic role of ODA in order to maximise resource mobilisation and its effectiveness.[11] Allocation decisions combine all these dimensions, reflecting the increased complexity of an inter-connected world. Donors will also engage in sectors and regions where they consider they have comparative advantages.

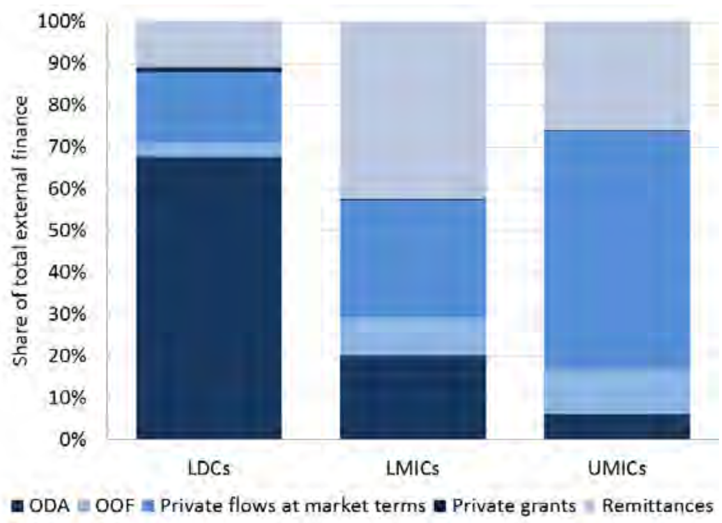
41. As a consequence, members have different approaches and objectives for deploying their ODA, including its geographical allocation. **As a community of donors, the DAC needs to reflect on the aggregate allocation pattern that results from these individual decisions, and see if they result in an optimal use of concessional financing.**

42. The new development finance landscape is a reality – there is a diversity of resources and instruments available today. While many countries, especially middle-income countries, have access to a more diverse range of sources of finance – domestic and international, public and private – ODA remains a crucial source of development finance for the LDCs.[12] In 2012, ODA represented 68% of total external finance for development in LDCs, whereas it represented 20% in Lower Middle Income Countries (LMICs) and 6% in Upper Middle Income Countries (UMICs) respectively. (See Figure 2.) These statistics are broadly representative of continuing resource trends to these country groupings – and attest to the crucial role played by ODA in many of the poorest developing countries.

[11] See chapter 2, on the treatment of market-like instruments in the post-2015 statistical framework.

[12] See for example DCD/DAC(2013)29 "The Where" of Development Finance: Towards Better Targeting Of Concessional Finance.

Figure 2. The composition of external finance in LDCs and other countries (2012)



43. While MICs have more financing options than LICs, **current resources are also not sufficient to address the wide range of challenges within MICs**. They are home to the majority of the world's poor, they face important inequality challenges and they are vulnerable to climate change and natural disasters. ODA is necessary to tackle these challenges and help countries build capacity and expertise for sustainable economic growth, including structural changes to create jobs and reduce inequality.

44. At the Fourth United Nations Conference on the Least Developed Countries in 2011, donors adopted a **Programme of Action for the Least Developed Countries for the decade 2011-2020**, and committed to "*assisting the least developed countries with an overarching goal of enabling half of them to meet the criteria for graduation through the eradication of poverty and the achievement of accelerated, sustained, inclusive and equitable growth and sustainable development*". Donors re-affirmed their existing commitment to provide 0.15-0.20% of their GNI as aid to LDCs by 2015, and acknowledged that "*donor countries should review their ODA commitments in 2015 and consider further enhancing the resources for least developed countries*".[13]

45. Looking at current collective DAC donor countries' performance against the UN ODA target of 0.15-0.20% of GNI to LDCs, the DAC as a whole still falls short of the target. Between 1998 and 2009, the share of ODA to LDCs increased steadily, putting the UN target within reach. However, in recent years this trend has been reversed. In 2012, total DAC ODA to LDCs amounted to USD 41 billion, representing

[13] More specifically, the commitment of the Istanbul Programme of Action states that "Donor countries will implement the following actions that they committed to at the Third United Nations Conference on the Least Developed Countries as soon as possible. (i) Donor countries providing more than 0.20 per cent of their GNP as ODA to least developed countries: continue to do so and maximize their efforts to further increase ODA to least developed countries; (ii) Other donor countries which have met the 0.15 per cent target: undertake to reach 0.20 per cent expeditiously; (iii) All other donor countries which have committed themselves to the 0.15 per cent target: reaffirm their commitment and undertake either to achieve the target by 2015 or to make their best efforts to accelerate their endeavours to reach the target; (iv) During the period of the Programme of Action, the other donor countries: exercise individual best efforts to increase ODA to least developed countries with the effect that collectively their assistance to least developed countries will significantly increase". Read the full report at http://unohrlls.org/UserFiles/File/A-CONF_219-7%20report%20of%20the%20conference.pdf

0.09% of total DAC GNI. An additional USD 29 billion would be required to reach the 0.15% UN target on a collective basis.[14]

DAC Action Plan to accelerate fulfilment of the 0.15-0.20% UN target to LDCs

46. As part of its modernisation of ODA and the development of a new measure for Total Official Support for Development (TOSD)[15], the DAC has a unique opportunity to showcase its ambition for achieving a better balance in the global allocation of official resources for development that takes into account the needs of the LDCs. **An agreement in the DAC to reverse the recent decline, and the development of an action plan for gradually increasing DAC ODA to LDCs up to 2020, could serve as a concrete contribution to the post-2015 financing framework, as well as contribute to the delivery of the Istanbul Declaration and the Programme of Action for the Least Developed Countries**.

47. The DAC action plan could also incorporate concrete measures to facilitate the crowding-in of private resources essential for sustainable economic growth for example through guarantees, including in the poorest countries. While more work is needed to facilitate further leveraging of non-ODA resources, particularly in the case of LDCs where the business case for the leveraging effect of ODA must be made, work on the valorisation of these instruments could be a key contribution. The proposed TOSD measure could also play an important role in capturing the totality and nature of financial instruments and allocations to ensure a better distribution of development finance going forward, as well as encouraging further resource mobilisation.

48. Finally, the DAC action plan could also include a review of the existing DAC Recommendation on the Terms and Conditions of Aid, which has special provisions for LDCs. These require an overall average grant element of at least 86% to each least developed country over a period of three years or at least 90% annually for the LDCs as group. While the exact target of the Recommendation would need to be reviewed to take into account the forthcoming DAC decision on the discount rate, there is also the more general question of the need for ensuring prudent practices in the provision of financing, mindful of countries' debt sustainability frameworks.

49. **The SLM is invited to agree that:**

- **the DAC should work to reverse the decline in ODA to LDCs;**
- **an action plan to reach the UN LDC target by 2020 be proposed to the HLM in December 2014; and**
- **progress in implementing this plan be reviewed annually at the SLM.**

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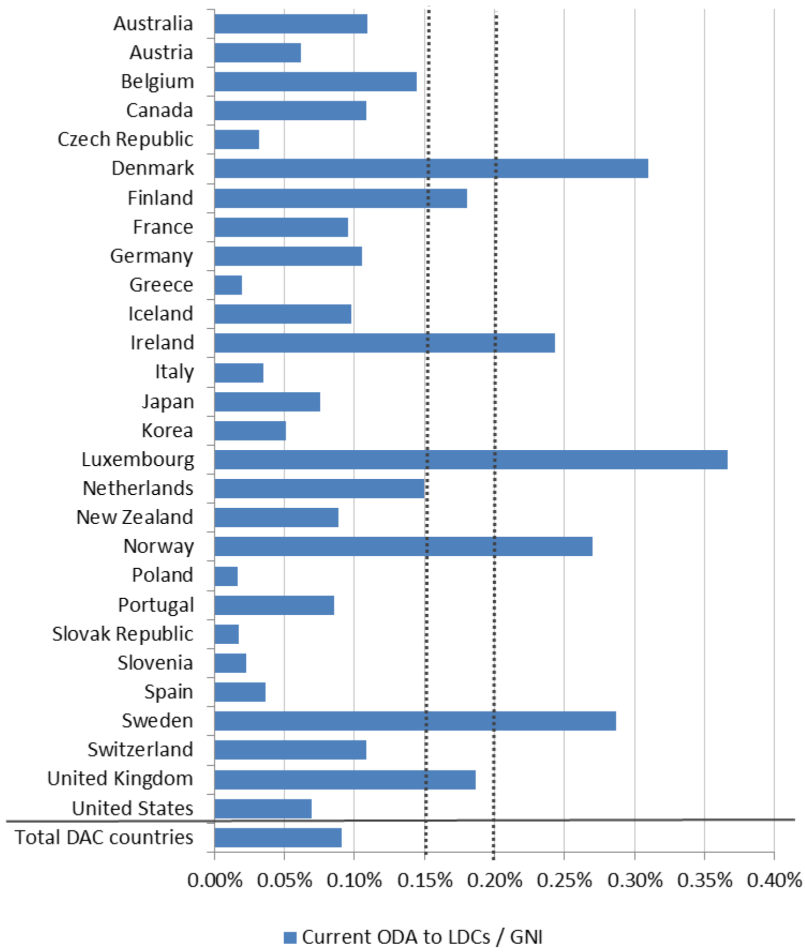
[14] This figure is based on the current methodology which takes into account both bilateral ODA and the portion of multilateral ODA to LDCs attributed to donors (the so-called "imputed multilateral ODA). If a portion of regional and global unallocated resources is assumed to benefit LDCs, the amount required to reach the target would be smaller.

[15] See chapter 1 on the proposed narrative and building blocks of the TOSD concept.

Annex: DAC members ODA/GNI to LDCs



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