DAC Working Party on Development Finance Statistics

Reporting of Direct Investment as ODA

Proposal from Spain

Informal meeting of the Working Party on Development Finance Statistics (WP-STAT), 28 February - 1 March 2017

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Proposal from Spain (for discussion):
Reporting of Direct Investment as ODA

Spain views: Reporting direct investment in ODA

It is not clear that all types of direct investments are ODA eligible in current DAC statistical reporting directives. References to direct investments are only made under the “OOF” chapter. It seems that this question is not clear for many members who have addressed this issue, and who have never reported direct investment as ODA.

Also the conclusions of the Task Team on PSI (Private Sector Instruments), lead us to define some safeguards for reporting PSI transactions as ODA. The Agenda 2030 raises the importance of the private sector in development, and implies an evolving role for private sector actors. In this context, concerns have grown about potential conflicts of development and commercial objectives, and increased instances of tying. It will be important for the DAC to further assess these concerns and clarify, how the private sector agenda relates to commitments on untying.

Task Team members also raised similar concerns in the margins of the discussions. As it was agreed in the summary of the Task Force, safeguards for PSI transactions should verify that DFIs operations are developmental, untied and additional. At the Institutional level, in the summary of the Task Team meeting 13-14 February, a Biennial assessment of DFIs in which these three aspects (development, tying status, additionality) will need to be revised, was also proposed.

For Spain, it is clear that in order to make possible this assessment we would need some tools that would allow the Assessment Committee (DAC – ECG), taking objective decisions based on evidence.

In the case of loans it has been proposed, to enhance the ex-ante notification system. Compliance of DAC members with the Untying Recommendation is weakest in the area of ex ante notifications. To encourage stronger compliance with this provision by more DAC members, it might be considered to which extent the information provided may be used to serve the purpose of competitive tendering, beyond being a reporting obligation to DAC members. Offers could be published on the untied aid bulletin board.

Similarly to PSI loans where ex-ante notification could be able to provide the Secretariat with information to assess the competitive character of a transaction, for mezzanine finance and direct investment we will need another tool or procedure to assess this competitive character.

In a competitive process the donor country has to prove that the operation supported is not tied. In the case of loans, the untying condition can be more easily satisfied. In the case of direct investment, the untying

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1 It is also among the proposals of the (DAC – ECG) Task Team on competition safeguards:
Make contractual export contingent untied PSI (ODA or not) subject to succinct ex-ante notification, in the DAC or ECG: project name, country, sector, volume (scale), tenor, greenfield vs brownfield, entity involved (type).
- Procurement regime (if not international Competitive Bidding, state regime and justification).
- Details of the agency responsible for procurement and from with further information or details (e.g. bidding periods, procurement regimes, bidding documentation) can be requested.
condition is more difficult to justify. As per the PSI Task Force conclusions, DFI’s portfolios should be untied to be reported as ODA. Therefore, we need tools for verification.

In order to systematize the analysis of direct investment portfolios, the following diagram is helpful. The diagram categorizes the investment based on the typology of the investment and the nationality of the company.

Thus, the typology of direct investment in companies can be sum up here:

<table>
<thead>
<tr>
<th></th>
<th>Unspecified Investment</th>
<th>Specified Investment</th>
</tr>
</thead>
<tbody>
<tr>
<td>National Company</td>
<td>It is not reportable neither as ODA nor OOF</td>
<td>Reportable only as OOF (See 1 and 2)</td>
</tr>
<tr>
<td>Foreign Company</td>
<td>Still to be discussed in WP-STAT</td>
<td>Could be ODA (to be discussed at WP-STAT)</td>
</tr>
</tbody>
</table>

1. Paragraph 24, vi (Page 11) from the reporting directives [DCD/DAC(2016)3/FINAL]: “Funds in support of private investment (loans and grants by the official sector to a private company in the donor country to help finance a specified investment in a developing country). Support to a general investment programme of an enterprise is not reportable, even though it may indirectly encourage investment in developing countries.”

2. In the same directives, Line II (on OOF) A.2.2 (page 59) Investment-related transactions with residents – support to national private investors (code 287) Covers loans (columns 1122 and 1152) and subsidies (columns 1121 and 1151) to national private investors, i.e. loans and grants by the official sector to a private company in the donor country to help finance a specified investment in a developing country. Support to the general investment programme of an enterprise should not be included, even though it may indirectly encourage investment in developing countries.

The first issue to solve here is to determine the nationality of the company. In order to do so, several criteria should be taken into account. A preliminary list can be:

- Who exerts the control of the company
- How the share capital of the company is distributed (national / foreign)
- Where is the company registered
- How is the company registered (with respect to its parent: Is it a representative office, a branch, an establishment, a subsidiary?)

The assessment to determine the nationality of a company in many cases is not immediate and we believe that in most cases it can be solved with a form/survey (containing at least the four requisites abovementioned) filled by the company receiving the capital as a prerequisite prior to the capital investment. We understand that the donor country making the investment and reporting it as ODA, should have the information required in the form/survey.

We propose that the DAC Secretariat requires the information contained in these surveys to the donor DFI in order to assess ODA eligibility and also to prepare the Biennial Assessment at the institutional level (development, untied, additional).

The second question to solve is linked to the character of the investment: whether it is specified or unspecified. When an investment is made in a foreign company, is specified and has a development character it could be in principle reported as ODA.

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2 We suggest that the Secretariat provides references to existing international agreements (such as for instance OECD/DAF rules on ownership)
The case is less clear when an investment is done in a foreign company for an unspecified investment. Our view with regards to reporting as ODA an unspecified investment is that some requirements need to be fulfilled such as:

- Guaranteeing that the unspecified investment is not used to cover balance sheet losses of the company and it is not used for refinancing other debts.
- Guaranteeing that the company financed has real productive activity
- Including some competitive mechanisms to guarantee that, in case the unspecified investment is used to finance imports from another country (donor country or not), this is not causing a competitive issue. Moreover, imports should be demand driven.
- Additional criteria could be developed, inspired by the EU regulation on regional Aid (“Minimis regulation 2013”) COMMISSION REGULATION (EU) No 1407/2013.
  - We can consider that a public participation on the capital of an enterprise granted over a period of time not exceeding a certain fixed amount and which complies with ODA definition, can be ODA eligible.
    - It is appropriate to maintain the ceiling of EUR 200.000 as the amount of public participation that a single undertaking may receive over any period of three years. That ceiling remains necessary to ensure that (any measure failing under this Regulation) can be deemed not to have any effect on trade and not to distort or threaten to distort competition.
  - For public participations exceeding EUR 200.000, a notification procedure to the DAC Secretariat and potentially to other Committees, should be established in order to ensure that the investment has a developmental purpose and does not have any effect on trade and does not distort or threaten to distort competition.

**Conclusion:**

We propose that the DAC Secretariat requires the information contained in the surveys presented above (to determine the nationality of a company and character of the investment) to the donor DFI in order to assess ODA eligibility and also to prepare the Biennial Assessment at the institutional level (development, untied, additional).

These issues are difficult to agree on in a generic manner and a priory. We therefore propose to expand the ex-ante notification requirement with the possibility of requesting a face to face consultation in the Committee to (i) obtain additional information and (ii) ask for the view of the committee on how to report the investment i.e. as ODA, OOF or neither. This procedure is part of the 2001 DAC Recommendation Untying. Moreover, it was used most effectively to get operational clarity among Members about the concept of commercial viability of the 1992 "Helsinki Disciplines on tied aid.

We believe that an in-depth discussion in the WP-STAT, ECG and the DAC is needed in order to decide whether and under which conditions could mezzanine finance instruments and direct investment be ODA eligible.