

Development Co-operation Directorate
Development Assistance Committee

DAC Working Party on Development Finance Statistics

CHRONOLOGY OF DAC DISCUSSIONS ON CONCESSIONALITY IN CHARACTER

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This note presents a chronology of DAC discussions on concessionality since the WP-STAT Task team on concessionality and WP-STAT plenary meetings on 14 September 2012 and 16 October 2012. It informs WP-STAT members of the DAC proposal on concessionality approved on 8 April 2013 and the actions to be taken by the Secretariat to implement this agreement.

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1. This note presents a chronology of DAC discussions on concessionality since the WP-STAT Task team on concessionality and WP-STAT plenary meetings on 14 September 2012 and 16 October 2012.¹ It informs WP-STAT members of the DAC proposal on concessionality approved on 8 April 2013 and the actions to be taken by the Secretariat to implement this agreement.

Discussions in the DAC in October-November 2012

2. Following the WP-STAT meeting on 16 October 2012, the Secretariat summarised members' positions on concessionality in character [DCD/DAC(2012)50] for the **DAC meeting on 30 October 2012**². The WP-STAT Chair attended and briefed this meeting, which considered how to present the issue to the DAC High Level Meeting (HLM).

3. At the **DAC meeting on 12 November 2012**³, the DAC Chair proposed a compromise – DDR-25% as a benchmark for ODA loans, and the creation of a separate category of “preferential development loans” – on which he subsequently sought written comments. On 3 December 2012, he issued [DAC/CHAIR\(2012\)5](#), encouraging members to support this proposal, and laying out five broad principles that a compromise should meet. He also discussed some members' suggested “transparency option”.

HLM principles and decisions

4. **The DAC HLM** considered concessionality at a **breakfast discussion on 5 December 2012**.⁴ Participants did not agree on how to define “concessionality in character”, or to adopt the DDR-25 option, but they broadly accepted the Chair's five principles, and agreed on the need for transparency and equal treatment of every DAC member. They also committed to defining the term “concessional in character” by 2015 in a way that reflected modern financing conditions.⁵ The HLM directed the Secretariat to prepare for members' consideration and approval a note describing the criteria it was applying in assessing loan concessionality, including the degree of subsidy needed.

1. A list of WP-STAT documents relating to concessionality issued between June and October 2012 is given in Annex 1.

2. See DCD/DAC/M(2012)9/PROV, paragraphs 21-22.

3. See DCD/DAC/M(2012)10/PROV, paragraphs 15-19.

4. See DCD/DAC/M(2012)11/PROV, Annex.

5. See HLM communiqué, paragraphs 18-19. The HLM principles and decisions are also part of the proposal on concessionality approved by the DAC – see Box, 2nd and 3rd paragraphs.

Discussions in the DAC in February-March 2013

5. The DAC considered this Secretariat note [DCD/DAC(2013)2] at its **meeting of 20 February 2013**.⁶ The note stated (paragraphs 28-30) that, pending a clear definition of concessionality in character, the Secretariat would continue to advise members that loans made from market-raised funds should only be reported as concessional if they have an element of official sector subsidy. It presented three options for dealing with a situation where some members did not provide the necessary information to distinguish between subsidised and unsubsidised loans. The meeting also received a report from Ms. Ana Fernandes, DAC Vice-Chair and WP-STAT Facilitator, on her consultations with members, and a letter from France and Germany⁷ giving detailed reasons for counting specific development loans as ODA. The meeting asked the DAC Bureau to draft for members' consideration a proposal for resolving the issue, drawing on the "transparency" and "assessment" options in the referenced document.

6. The Bureau's proposal⁸ was discussed **at the DAC meeting on 14 March 2013**.⁹ The proposal envisaged France, Germany and the EU providing rationales for their reporting.

DAC approval of the proposal on concessionality

7. A revised proposal¹⁰ was approved by the DAC through the written procedure on 8 April 2013 (see Box), and the EU, France and Germany provided their rationales (see Annex 3), which were circulated for members to note under a written procedure¹¹ by 26 April 2013.

8. On 2 May the DAC Chair informed the Committee that the rationales had been noted, so that a transitional compromise was in place for the period until 2015. He added that the DAC urgently needed to start working on the broader development finance issues, including the definition of concessionality in character, to arrive at a solution for the period after 2015 on the basis of a thorough discussion.

Action items for the Secretariat and the WP-STAT

9. Under the approved proposal the Secretariat will:
- i. Prepare an annex for inclusion in annual releases of new ODA data, stating there are different views on concessionality in character, presenting the rationales of the three members as well as the current practice of other members (paragraph 8 of the proposal);
 - ii. Compile an annual report on monitoring and assessing the reporting of loans by all members (paragraph 12) that would contribute to discussions regarding concessionality (paragraph 13); and
 - iii. Apply the decisions outlined in the proposal, adjusting the information on final 2011 ODA figures and preliminary 2012 ODA figures accordingly.

6. See DCD/DAC/M(2013)2/PROV, paragraphs 2-9.

7. Letter circulated to DAC Delegates on 19 February 2013.

8. Email from Erik Solheim to DAC Delegates dated 13 March 2013.

9. See DCD/DAC/M(2013)4/PROV, paragraphs 5-14.

10. Email from Erik Solheim to DAC Delegates dated 29 March 2013.

11. Email from Erik Solheim to DCA Delegates dated 18 April 2013.

10. The Secretariat has started implementing these decisions. Following suggestions from members regarding the annual report, it will also contact members that have reported ODA loans for 2011 to obtain additional information needed for the assessment of loans. The report on ODA loans in 2011 will be prepared for consideration and approval by the DAC in September 2013. The reports on ODA loans in 2012, 2013 and 2014 will be prepared upon reception of final data for these years and can be therefore be expected in December 2013, 2014 and 2015 respectively.

11. Further discussion on the concept of concessionality will take place as part of the broader debate on development finance (paragraph 2 of the proposal). This will undoubtedly involve additional technical work by the WP-STAT. The DAC Facilitator will outline the expected WP-STAT contribution to discussions on concessionality at the meeting of the Working Party on 12 June 2013.

Box 1. Proposal On Concessionality approved by the DAC on 8 April 2013

The DAC has discussed for some time the interpretation of concessionality in character in the ODA statistics. Due to the fact that there were different views among members, the DAC decided to discuss this topic and the different options presented by the Secretariat and by the Chair of the DAC at the High Level Meeting (HLM) in London in December 2012.

At the HLM, the DAC agreed on several principles regarding concessionality in character. These are that ODA reporting should: i) Withstand a critical assessment from the public; ii) Avoid creating major fluctuations in overall ODA levels; iii) Be generally consistent with the way concessionality is defined in multilateral development finance; iv) Maintain the definition of ODA, and only attempt to clarify the interpretation of loans that qualify as ODA; and v) Prevent notions that ODA loan schemes follow a commercial logic: this includes the principle that financial reflows should be reinvested as development resources.

The HLM also decided: i) on transparency regarding the terms of individual ODA loans; ii) to ensure equal treatment of all DAC members; iii) to establish, as soon as possible, and at the latest by 2015, a clear, quantitative definition of "concessional in character", in line with prevailing financial market conditions; and iv) to recognise development loans extended at preferential rates- whether "concessional in character" under a future post-2015 definition or not - as making an important contribution to development.

On 20 February 2013, the DAC decided to mandate its bureau to present a proposal to the Committee, in line with the HLM principles and decisions and in line with the current ODA-eligibility requirements. This proposal would merge transparency with the need for a more clear assessment of loans and ensure that all DAC members are treated equally.

Proposal

The DAC, pursuing the HLM principles and decisions and recognising the need for a long- term discussion and a short-term solution on concessionality in character, will take the following steps.

1. The DAC will work to contribute to the development finance global debate.
2. In order to pursue the decision of the HLM to establish, as soon as possible, and at the latest by 2015, a clear, quantitative definition of concessional in character, in line with prevailing financial market conditions, the DAC will start a debate on the definition of concessionality in character, as part of the broader debate on development finance.
3. The rationale presented by EU, France and Germany, referred to in paragraph 5 below, is a welcome contribution for this discussion.
4. Other members are also encouraged to share in the DAC their own views regarding the future definition of concessionality in character.
5. The DAC notes the willingness of the three members, whose loans were subject to references for the 2011 ODA statistics, to continue to provide information on those loans according to the DAC Statistical Reporting Directives (i.e., terms and conditions of individual loans, including interest rates, maturity and grace periods). Together with this information, the three members will have to present respectively a rationale, that encompasses their own views of concessionality in character, and that is sufficiently clear and objective. The rationales will refer to the HLM principles and decisions and they will state clearly that loans are not given on a profit basis.
6. The DAC will discuss the rationales with a forward looking perspective and will take note of them, recognising that there are different views on concessionality in character.

7. If the DAC notes the rationales, the DAC will consider that a notification done in *bona fide* according to the rationales is a reporting practice that can be accepted.
8. To ensure transparency the DAC will present an annex to annual releases of new ODA data, online or on paper, stating that there are different views on concessionality in character. For the purpose of information, the annex will present the rationales of the three members, as well as the current practice of other DAC members.
9. The DAC will only apply this solution to ODA data from 2011 to 2014. There will be no retroactive changes to loans extended before 2011.
10. In order to ensure equal treatment, the DAC will take note of the rationale presented by the EU, concerning the European Investment Bank (EIB) loans since 2008.
11. This process will not imply changes in the current or past reporting practice of other DAC Members.
12. The Secretariat fulfils a fundamental role of advising members and will present an annual report on monitoring and assessing the reporting of loans by all members. This report will assess loans, starting with 2011 figures, against a) the ODA directives b) the practice of ODA reporting and c) the High Level Meeting principles and decisions. The report should indicate if any changes of practice have occurred that need to be discussed by the DAC. The Report will be for discussion and approval by the DAC in full consideration of the HLM principles and decisions.
13. The report will also contribute to the DAC discussions regarding the need to find a solution for the concept of concessionality and it will mention the steps that have been undertaken to find that solution.
14. The approach outlined in this document is understood exclusively as a transitory solution, and should not pre-empt any decisions to be taken in the context of deliberations on post-2015 development finance.
15. The DAC instructs the Secretariat to apply decisions outlined as above and adjust the information on final 2011 ODA figures and preliminary 2012 ODA figures accordingly.
16. Procedure:
 - a) The DAC is invited to agree on the process outlined in paragraph 1 to 15 by written procedure by the 8 April 2013 cob.
 - b) The EU, France and Germany are invited to revisit their rationales and to complement information already provided to be in line with paragraph 5 by 15 April 2013; subsequently they will be submitted to the DAC for written procedure.

ANNEX 1. WP-STAT process and consultations on concessionality in character

Process of consultations / Document titles	Document references
1. WP-STAT Survey of approaches to determining concessionality of loans	
Seeking members' policies and views on clarifying the definition of concessionality in DAC statistics	Email STAT(2012)46
2. WP-STAT Task team on concessionality on 14 September 2012	
Extracts from reporting directives bearing on concessionality	DCD/DAC/STAT(2012)16
Results of the Survey of approaches to determining concessionality of loans	DCD/DAC/STAT(2012)17 and DCD/DAC/STAT(2012)17/ADD1
Explanation of concepts used in concessionality and grant element calculations	DCD/DAC/STAT(2012)18
Task team on concessionality meeting: Chair's summary	DCD/DAC/STAT/M(2012)3
3. WP-STAT plenary on 16 October	
Benchmarking concessionality in character: Draft issues paper	DCD/DAC/STAT(2012)20/DRAFT
Concessionality in character: Sensitivity analysis using differentiated discount rates	DCD/DAC/STAT(2012)21
Proposal for clarification of concessional in character: Note by Canada, France, Germany and Spain	DCD/DAC/STAT(2012)22

**ANNEX 2. Process and consultations on concessionality in character in the DAC
(October 2012 – April 2013)**

Process of consultations / Document titles	Document references
1. DAC meeting on 30 October 2012	
Summary of members' positions on "concessionality in character"	DCD/DAC(2012)50
Draft summary record of the 953 rd DAC meeting	DCD/DAC/M(2012)9/PROV, paragraphs 21-22
2. DAC meeting on 12 November 2012	
Draft summary record of the 954 th DAC meeting	DCD/DAC/M(2012)10/PROV, paragraphs 15-19
3. Mr Atwood's proposal for a compromise	
The ODA definition: interpretation of "concessional in character" – A proposal for a compromise	DAC/CHAIR(2012)5
4. DAC High-level meeting on 5 December 2012	
Summary of the HLM breakfast discussion on the concessionality of ODA loans	DCD/DAC/M(2012)11/PROV, Annex
5. DAC meeting on 20 February 2013	
Loan concessionality in DAC statistics	DCD/DAC(2013)2
Draft summary record of the 959 th DAC meeting	DCD/DAC/M(2013)2/PROV, paragraphs 2-9
6. DAC meeting on 14 March 2013	
Draft summary record of the 961 st DAC meeting	DCD/DAC/M(2013)4/PROV, paragraphs 5-14
7. DAC Bureau's proposal for a compromise	
Proposal on concessionality	DAC/CHAIR(2013)2

Annex I

Proposal on concessionality**Rationale of the EU's development loans**

EIB loans comply with the ODA-eligibility requirements set out in the DAC Statistical Reporting Directives which are applicable to all DAC Members equally. In addition, they are in line with the principles agreed at the HLM in December 2012 and notably with the five criteria mentioned in paragraph 18 of the HLM Communiqué:

Regarding development purpose and additionality: The EIB fosters sustainable development outside the EU under the ACP-EU Cotonou Agreement for ACP countries and on the basis of an explicit mandate by the Council of the EU and the European Parliament (the so-called External Lending Mandate) for the other external regions.

The EU via the EIB provides external financing in areas where long-term capital is lacking either because markets are not active or because they are not yet functioning sufficiently well. Documentation of the additionality of the EIB loans is part of the internal project appraisal. Maturities might reach up to 20 or 25 years, for example in the case of infrastructure projects where they are essential to make these projects viable.

Regarding the donor effort: Given that recipient countries outside the EU are not EIB shareholders, lending to these countries generally involves a higher degree of risk in EIB operations. This is the reason why the EU budget provides a sovereign risk guarantee (for public sector coverage of commercial and political risk, for private sector full coverage of political risk). The EU guarantee involves a **direct budgetary effort**, since its costs are borne by the EU budget. It enables the EIB to lend to developing countries on terms it would otherwise not be able to offer in terms of maturities, grace period, interest rate and other contractual obligations. This amounts to the sovereign/political risk being borne entirely by the EU. Some of the loans also benefit from direct grants and technical assistance.

Regarding not-for-profit: The EIB operates on a **non-profit basis** (ref. 309 TEU) as a policy-driven public Bank owned by the EU Member States. The EIB's lending operations outside the EU are not conducted with a commercial or profit purpose. In line with the EIB policies, interest rates on loans are set in such a way that the income therefrom enables the Bank to meet its obligations, to cover its expenses and risks, and to operate on a sustainable basis. The loans provided by the EIB are priced in such a way that these statutory provisions are satisfied.

French rationale on ODA loans

All French loans declared as ODA are concessional in character and they fully respect the principles agreed at the HLM:

- 1- All loans granted by the French Development Agency bring a major contribution to development objectives.**

All loans granted by AFD and declared as ODA are part of the French development strategy.

These loans offer to the beneficiaries (i) a source of financing when alternatives are not always available (in particular in the case of non-sovereign financing) and (ii) much better financial conditions (interest rate, duration, grace period, credit risk tolerance) compared to those prevailing on local markets.

- 2- ODA loans are offered at preferential interest rates including a donor effort, and are not designed to make profit.**

AFD ODA loans are not designed along a profit-oriented banking model. They systematically include a French Government subsidy, either explicitly through a grant to lower the interest rate, or implicitly, because the interest rates offered to the beneficiaries do not reflect the full costs of the loans, and are therefore much lower for the beneficiaries. In particular:

- The pricing of the loans does not include any return on AFD equity: the equity, required for the loans' commitments is brought by the French Government;
- The pricing of both sovereign and non-sovereign loans declared as ODA is established without any profit margin. In addition, the cost of credit risk is not included in the rate offered to partner Government: it is borne by the French Government.

- 3- Net earnings contribute to reinvesting in development activities.**

AFD end-of-the-year net earnings are mostly the result of activities not declared as ODA (activities in French overseas territories and activities linked to Proparco, AFD private sector development subsidiary). Net earnings are used in particular to increase AFD equity and therefore contribute to increase its abilities to supply development loans.

Argumentaire pour les prêts français

Tous les prêts déclarés en APD par la France sont concessionnels en caractère et respectent les principes décidés à la HLM :

4- Tous les prêts de l'Agence française de développement apportent une contribution majeure au développement.

Tous les prêts consentis par l'AFD et déclarés en APD s'inscrivent dans le cadre de la stratégie d'aide au développement française.

Par ailleurs, ces prêts offrent (i) une source de financement alors que des alternatives n'existent pas toujours (notamment pour les prêts non-souverains) et (ii) des conditions financières (taux, durée, différé, risque) nettement plus favorables que celles auxquelles il aurait accès sur les marchés locaux.

5- Les prêts sont consentis à des taux préférentiels qui intègrent un effort du donateur et ne sont pas conçus pour engendrer des bénéfices.

Les prêts ne sont pas conçus sur la base d'un modèle lucratif bancaire. Ils contiennent systématiquement un effort de l'État français, soit de façon explicite, sous la forme de bonification de taux d'intérêt, soit de façon implicite car les taux d'intérêt des prêts de l'AFD ne reflètent pas les coûts totaux de ces prêts et sont ainsi nettement abaissés pour les bénéficiaires. En particulier :

- les fonds propres nécessaires à l'activité de crédit de l'AFD, apportés par l'État français, ne sont pas rémunérés dans la construction du barème des taux d'intérêt ;
- la tarification qui s'applique aux prêts à la fois souverains et non souverains déclarés en APD est établie sans marge bénéficiaire. Par ailleurs, le coût du risque n'est pas facturé à l'Etat récipiendaire : il est pris en charge par l'État français.

6- Le résultat comptable contribue à réinvestir dans des activités de développement.

Le résultat comptable qui apparaît à la fin d'un exercice pour l'AFD s'explique principalement par ses activités non déclarées en APD (activités dans les départements et territoires d'outre-mer français et activités liées à la filiale Proparco de développement du secteur privé). Ce résultat est notamment utilisé pour renforcer les fonds propres de l'AFD et ainsi lui permettre de développer son offre de prêts pour le développement.



Federal Ministry for Economic Cooperation and Development, Germany

15 April 2013

Rationale of German Development Loans

German development loans are concessional in character and ODA-eligible, because they are in line with the HLM principles and comply with the ODA reporting directives:

1. The loans incorporate an **effort by the German government** either by means of an explicit subsidy element (grant) or an implicit one in form of a guarantee. In the latter case the German government guarantees for the default of loans. This guarantee can be statutory or transaction specific and lowers the funding costs and the risk margins for the executing development bank (KfW). The full costs of subsidies and guarantees are defrayed by the German government. Thus, the interest rate does not reflect the full costs of the loan, which are lowered considerably for partner countries. Subsidies and guarantees are part of the annual federal budget which is approved by parliament.
2. The loans are attested **development relevant**. Each loan is mandated by the Government according to German development cooperation rules and strategies. The loans are part of the official government negotiations with partner countries and they provide **benefits to the recipients** being extended at softer terms and longer maturities and grace periods than other sources of financing. They provide additional financing for MICs, so liberating ODA- funds for LDCs, in sectors in which financing through credits is developmentally sound.
3. The loans **do not earn any profits** for Germany as the beneficial owner of KfW development bank. Its interest rates depend on maturity, grace period, currency and initial risk of the partner country. Any reduction in the interest rate through a Federal guarantee or a direct subsidy (grant) as well as better refinancing rates of the development bank are passed on to the borrowing partner country in full. The German development bank does not distribute any earnings to its shareholders. Instead all revenues are reinvested for development purposes.