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## DAC Working Party on Development Finance Statistics

### AN ALTERNATIVE/EXPANDED INSTITUTIONAL APPROACH FOR ODA ELIGIBILITY OF PRIVATE SECTOR INSTRUMENTS

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# **AN ALTERNATIVE/EXPANDED INSTITUTIONAL APPROACH FOR ODA ELIGIBILITY OF PRIVATE SECTOR INSTRUMENTS**

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## **Introduction**

This proposal presents an expanded institutional approach. It is intended to contribute to the on-going discussions on this matter in WP-STAT. During the previous WP-STAT meetings two methods on reporting for DFIs have been discussed; the institutional method and the instrumental method.

DFIs play a crucial role in mobilising the private sector for development and this role will continue to increase in importance. ODA reporting should incentivise DAC members to make effective use of their DFIs. At the same time the system needs to remain transparent and credible. The institutional method has its point of departure in the pursuit of measuring the actual donor budget effort in using private sector instruments.

Institutions are at different levels of maturity and the desire to upscale these institutions in line with the growing importance of mobilising private finance for development should not be disincentivised by the ODA system. With this in mind, members should have the option of whether to put their institutions forward for ODA-eligibility or not, dependent upon if this is appropriate for their development approach. This would be consistent with current treatment of the Annex II list.

## **Summary**

The institutional method measures the donor capitalization of the DFI in ODA. The revenues drawn back from the DFI to the donor is accordingly counted as a negative ODA flow. In order to transparently report on the outflows in CRS, the outflows are reported in OOF.

## ***Definition***

DFIs are entities set up by donor governments to operate in developing countries with the promotion of economic development and welfare through private sector engagement as the primary objective. DFIs are not agencies that carry out export credit or promotion activities.

## ***This method has the following strengths:***

- a) Measuring actual donor budget effort
- b) Incentivizing upscaling of DFIs
- c) Instrument neutrality that fosters innovation and creativity
- d) Provides opportunity for innovative and bold financing without devastating fluctuations and impacts ODA-levels and thereby minimizes budgeting issues

- e) Allows augmentation of the DFI's activities without devastating fluctuations and impacts ODA-levels and thereby minimizes budgeting issues
- g) Results in equal treatment and comparability of multilateral and bilateral finance institutions
- h) More accurate ODA reporting for DFIs that are only partially owned by the DAC-members.

Quality controls of the DFIs are integrated in the method in the form of evaluation and Peer Reviews of the DFIs.

In order to capture DFIs with different financing setups and portfolios, an ODA-coefficient is determined in the evaluation process of the DFIs.

### **Evaluation of Institutions ODA-eligibility and Peer Reviews**

When a DFI applies for ODA-eligibility, the DAC will establish an ODA coefficient. An evaluation of the DFIs ODA-eligibility should be performed by the DAC.

The DFIs ODA-eligibility can thereafter be regularly controlled in Peer Reviews. The secretariat will control the ODA-eligibility on the outflows of the DFIs during the Peer Reviews, as well as the evaluation points mentioned below.

If a change in ODA-coefficient is recommended in the Peer Review, the amended ODA-coefficient should apply to the coming year.

#### ***The evaluation and peer review of the DFIs should be based on the following criteria:***

- The primary purpose test: Promotion of economic development and welfare of developing countries.  
Only the proportion of activities that meet the primary purpose test can be scored as ODA. This enables agencies that also undertake non-developmental activities to opt in to this option, so long as development resources can be clearly identified and the above criteria are met in relation to the development work.
- The bilateral agency operates in ODA eligible countries.
- The agency has a stated development goal, with activities in line with this mandate and the agency demonstrates evidence of development impact.
- The agency is sufficiently autonomous in its decision making, with independent bank accounts and fund management.
- All profits should be reinvested back into development activities. If capital or profits are taken out of the institution and back into the donor government, this would count as a negative ODA flow.

- ODA is untied.
- The DFI has an efficient balance sheet and cash management i.e. unreasonable amounts of cash are not held on the balance sheets of these agencies.
- Operations meet appropriate safeguards such as having appropriate evaluation and reporting structures or corporate governance standards.
- Activities are transparently reported in in the CRS as OOF
- Additionality requirements are clearly stated in the DFI's mandate and processes are in place to review the additionality of investment proposals before approval.

## **ODA-coefficient in order to capture the multitude of setups of the DFIs**

The DFIs have varying setups, structures, financing as well as different activity setups.

### ***Main issues that are solved by using an ODA-coefficient:***

The DFIs are setup in a multitude of ways, some of the DFIs have 100% ODA-eligible activities in ODA-countries and some have some non-ODA-eligible activities. In order to include the multitude of DFIs and their respective structures and focus, we propose that the DAC Secretariat be tasked with calculating an ODA coefficient to determine ODA eligibility of each DFI based on the mandate of the DFI. This would correspond to the method in which multilateral organizations that are not entirely ODA eligible, but are included in Annex 2, are being treated.

Key components of the coefficient should be:

- The mandate of the DFI, specifically the development objective and geographic scope (ODA eligible countries) and the character of capitalization of the institution.

The onward activities of the DFIs are consequently excluded from ODA and reported as OOF/TOSD in CRS.

This method has the following benefits:

- A) Adequate treatment of DFIs with mixed official and private financing
- B) Integration of DFIs with different sorts of activities, ODA and non-ODA

## **Safeguards**

### ***1. Additionality test***

The additionality of the activities is related to the risk of DFIs being market disturbing where the market has enough investors and capital. Additionality of the activities should be a primary requirement, as the DFIs principal goal should be to give a surge to the local markets in the ODA-countries and not to compete on the local markets. Crowding out the

existing investors and market distortion should be avoided. An additionality requirement should be clearly stated in the DFIs' mandate and regularly controlled in the Peer Reviews.

## ***2. Transparency and accountability***

In order to maximize the transparency of the DFI's activities, the outflows are reported in CRS as OOF.

Donor effort should be the basic pillar; this should also be the case for mature DFIs. Where there is no donors effort, there should be no ODA.

## **Coherence with the treatment of financial instruments handled outside DFIs**

What may be eligible as ODA versus OOF/TOSD remains an important but separate discussion. The system for calculation of ODA when it comes to private sector instruments must measure donor effort, be transparent and withstand public scrutiny. Upholding the credibility of the system is important per se, but also in relation to key on-going international processes such as FfD.

## **Next steps**

DAC members are invited to provide comments on this paper with a view to arrive at an institutional approach proposal that can be agreed upon by all members.

An expert group open to all DAC members and potentially DFIs could help building a compromise proposal for the institutional approach.