



Financing for development negotiations – what should the EU bring to the table?

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European civil society scorecard for EU action

The transformative changes needed for a just, equitable and sustainable world with universal enjoyment of human rights require reliable and effective sources of financing. The European Union (EU) is a key actor in financing for development. It is home to many transnational companies and has a globally significant financial sector. It is the biggest provider of Official Development Assistance (ODA), and a major exporter and importer from the global south.

The coming year will be crucial for international negotiations to match shared global ambitions with binding commitments on financing for development. Discussions will create a new global sustainable development framework including post-2015 development goals, the post-Rio sustainability goals, and climate change financing. The European Commission (EC) has recently released a communication on post-2015 financing, but recognizes that this "does not propose new actions or commitments for the EU." However, the EU's credibility and reliability as a global actor will be determined by what it will bring to the table and the specific new commitments it is willing to make and deliver. This paper proposes 12 specific actions that would make concrete, vital changes, but are also realistic. These 12 actions serve as an initial test of the EU's ambition and credibility in these global negotiations, and we urge the EU to go beyond restating old commitments and adopt the proactive, positive and powerful measures below.

Take action in the EU – put our own house in order

1. Deliver public government registries of the real beneficial owners of companies, trusts and other corporate structures through the ongoing revision of the Anti-Money Laundering Directive.
2. Make the country-by-country reporting already adopted for the banking industry mandatory for transnational companies in all sectors.
3. Ensure full and effective participation of developing countries in the design and implementation of multilateral automatic information exchange between tax authorities.

Stop undermining the policy space partner countries need to lead their own development

4. Refrain from pushing trade and investment agreements and international taxation standards that are detrimental to developing countries' economic and development interests and to their own regional integration processes.
5. Endorse, implement and strengthen the UN principles on lending and borrowing, particularly by including private lending.
6. Ensure public and private finance to developing countries support national priorities and democratic ownership and sustainable state-society relations, in keeping with commitments made at Busan.

Increase and improve external public financing

7. Agree allocation of funds from innovative sources to sustainable development and international climate finance, for example by redirecting subsidies away from fossil fuels and from carbon pricing of maritime and aviation transport, and set aside 50% of revenues from the 11 country European financial transaction tax.
8. Meet the longstanding commitment to devote 0.7% of GNI to ODA in a transparent and accountable way and eliminate inflated aid.
9. Ensure the promised new and additional funds for climate finance are over and above aid commitments, and are effectively monitored and transparently reported.
10. Thorough evaluations of development and poverty reduction impact should be conducted, including whether the money could be better used elsewhere, before further promoting the diversion of scarce ODA to blend with loans that mainly benefit European companies.

Help prevent future finance and debt crises

11. Support and strengthen UN efforts to introduce fair and transparent debt work-out mechanisms.
12. Improve the regulation and supervision of the financial sector, and support developing countries' involvement in reforms.

Take action in the EU – put our own house in order

Ensuring that all EU policies integrate the EU's development objectives is the most sustainable and efficient way the EU can contribute to global goals. A lack of policy coherence for development not only violates EU treaty obligations,ⁱ but also has devastating effects on the poorest and most marginalized people in the world.

Developing countries' efforts to finance their own development are often undermined by illicit outward flows of finance, largely through tax havens, many of which are EU states or overseas territories. The best independent estimates conservatively suggest that over \$850 billion flow out of developing countries each year illicitlyⁱⁱ, mostly through tax dodging, costing at least \$100 billion in lost tax revenues.ⁱⁱⁱ As the EC has recognized in its communication, "loss of tax revenue is only one part of the negative impact of such flows, as they also discourage legitimate investments and undermine the wider social contract."

This is possible because the global financial system allows secrecy to flourish, particularly in tax havens, through which an estimated half of global trade flows,^{iv} and through which almost 1 in every 2 dollars of large corporate investment in developing countries is now being routed.^v While the collective call of EU heads of States for "effective steps to fight tax evasion and tax fraud" ^{vi} is promising, action has not kept up with rhetoric.

We know what needs to be done to end damaging financial secrecy and tackle tax havens. First, companies' accounts must become fully transparent. The EU should put in place measures to help ensure a fair tax contribution from transnational companies and make the country-by-country reporting soon required for the banking industry^{vii} mandatory for transnational companies in all sectors. Second, all stakeholders, including developing countries and civil society groups, need to know who are the real "beneficial owners" of companies and trusts and other corporate vehicles, and this information must be available through centralised public registries.

Third, tax authorities, including in developing countries need to have the information to track and tackle offenders. A multilateral automatic exchange of tax information regime that is only agreed between EU Member States and other developed countries is not sufficient. The EU must support a global regime which ensures the full and effective participation of developing countries in its design and responds to their needs, for example by allowing access to information without requiring full immediate reciprocity. Finally, fully involving developing countries in the design of global rules will be vitally important to making those rules fair and effective. For example, the EU should support and participate in the development of global standards of tax cooperation in the UN, rather than seeing the OECD as the only relevant forum.

Important tests of EU credibility are:

1. Deliver public government registries of the real beneficial owners of companies, trusts and other corporate structures through the ongoing revision of the Anti-Money Laundering Directive.
2. Make the country-by-country reporting already adopted for the banking industry mandatory for transnational companies in all sectors.
3. Ensure full and effective participation of developing countries in the design and implementation of multilateral automatic information exchange between tax authorities.

Stop undermining the policy space partner countries need to lead their own development

There is strong global agreement that successful development requires ownership and leadership from developing countries, but too often their ability to lead is undermined by the actions of powerful institutions such as the World Bank, IMF and OECD or by the EU itself. The EU has a direct and historical responsibility in its dealings with partner countries, particularly on tax, trade and investment, not to undermine the policy space of these countries to take decisions that are suitable for their own national context, respond to the demands of their populations, and fulfill their human rights obligations and other international commitments.

Double Taxation Agreements (DTAs), which are supposed to prevent double taxation, often ensure double 'non-taxation' of certain revenues and assets, leading to loss of tax revenue for developing countries.^{viii} Trade agreements, transfer pricing rules and investment protection treaties can also undermine the ability of developing countries to develop tax regimes that suit their national circumstances.^{ix} For example, the principles being pushed by the EU in EPA negotiations may undermine countries' abilities to nurture industrial development and may lead to loss of revenues in developing countries due to trade liberalization. Through its significant share in the decision-making structures of international institutions, the EU also has a responsibility for the policies of IFIs and of the OECD, particularly to prevent the active promotion of regressive tax systems in developing countries.^x

Depending on the quality of their investments, European companies also have an impact on the policy environment, economic space and development objectives in the countries where they operate. We welcome the recognition in the EC communication of "the need for all actors to apply responsible lending and borrowing principles to ensure debt sustainability." However, action, rather than rhetoric is needed: the EU should lead on promoting responsible financing standards^{xi} which go beyond a 'do no harm' approach to one that ensures that lending and investments actively deliver positive sustainable development outcomes. The UN has picked up this agenda, and UNCTAD has set out its own Principles for sovereign lending and borrowing,^{xii} which the EU and member states should endorse, implement and strengthen, particularly to include private actors.

Finally, the modalities and delivery mechanisms of aid, and the conditions attached to it, affect not only the results achieved, but may also undermine the ownership and leadership of developing countries. As a major block of donors, the EU should act to complete the unfinished business of the Paris Declaration and the Accra Agenda and put the Busan principles of development cooperation effectiveness into practice. These should apply not only to public flows but the EU should also ensure that private flows abide by these principles.

Important tests of the EU's credibility are:

4. Refrain from pushing trade and investment agreements and international taxation standards that are detrimental to developing countries' economic and development interests and to their own regional integration processes.
5. Endorse, implement and strengthen the UN principles on lending and borrowing, particularly by including private lending.
6. Ensure public and private finance to developing countries support national priorities and democratic ownership and sustainable state-society relations, in keeping with commitments made at Busan.

Increase and improve external public financing

Despite progress towards the Millennium Development Goals, the UN estimates the “additional investment needs of developing countries for sustainable development, including for climate change mitigation and adaptation, and for ensuring access to clean energy for all, sustainable food production and forest resource management, at about \$1 trillion per year in the coming decades.”^{xiii}

The climate crisis in particular represents a huge cost to developing countries.

The \$100bn per year of climate finance promised by developed countries by 2020, even if disbursed, is likely to cover only half the public finance that is needed^{xiv}, and a closer look at Fast Start Finance figures shows that very little was actually additional to existing aid commitments.^{xv} Therefore it is crucial that climate financing commitments are respected and strengthened, and that donors do not divert already stagnating aid budgets: international climate finance should be new and additional, with transparent reporting and verification. Much of this additional financing will need to be publicly provided, notably to meet developing countries’ adaptation needs. Overall, there is a crucial need for increasing public finance to face growing challenges, such as climate, health, ecosystems and biodiversity^{xvi}protection^[ii].

It is clear that new sources of public financing are urgently needed. The EU must be an advocate of a variety of additional sources for sustainable development and international climate finance. New financing mechanisms are already on the table that are predictable and sustainable, including taxes which have the potential to raise significant additional resources. For example, a financial transaction tax (FTT) among 11 EU countries could soon raise an additional €34 billion a year, to support international development, climate and domestic social sector goals. Carbon pricing of greenhouse gas emissions from global aviation and maritime transportation is also a promising revenues stream, in addition to helping reduce climate and environmental damage. The allocation of finance from these sources to sustainable development and climate finance is crucial, and this can be monitored through transparent, robust tracking measures and harmonized reporting of international climate finance at the EU and UNFCCC level.

Official development assistance should be scaled up to meet the 0.7% commitment of GNI. A debate on the current definition of ODA is inappropriate until donors have met their historic commitments on aid - changing the rules is not the way to meet spending targets. Instead, donors should reduce the amount of inflated aid^{xvii} and focus on genuine transfers to developing countries to spend on their own development. How we spend aid also matters – public finance is the flow that people can most easily engage with, track and influence. Aid spending should be ‘on budget’, predictable and transparent to ensure accountability of governments to their population and increase the development impact of aid. In conflict affected and fragile states where transparency, accountability and state legitimacy are often weak, it is also critical to reflect on the political economy of financing mechanisms, including which actors are reinforced, which dynamics are fuelled or whether development assistance is genuinely supporting the building of sound and resilient state-society relations.

Aid should remain focused on the poorest people and while this means working in the poorest countries it will also mean working in those countries where most of the world’s poor live. In the context of the EU differentiation proposal^{xviii}, decisions about phasing out aid should be made in consultation with partner countries, and income status should not be the only criteria; sustainable development, poverty and inequality indicators are also important.

Proposals to use scarce ODA to ‘leverage’ private investment by blending it with loans to private enterprises risk diverting valuable money from investment in essential public services and safeguarding global public goods, including biodiversity. In addition, research shows that its effects are often hard to verify, modalities lack transparency and accountability, and when this is done through international or European Development Finance Institutions, the majority of support goes to developed world companies, and to sectors and countries where private finance is already available, not the poorest countries or regions.^{xix}

Before promoting public-private blending facilities further, the EU should thoroughly evaluate, in dialogue with developing countries and populations, the impact of existing mechanisms with regards to sustainable development and poverty reduction outcomes, debt sustainability, decent work creation, social and environmental externalities and should assess the transparency and accountability of these mechanisms against internationally agreed ODA standards. They should also ensure that opportunity costs – referring to the lost opportunity to do something else with the money - have been carefully examined. Partner countries should take part in their governance and the decisions on their general framing and orientations.

Important tests of EU credibility are:

7. Agree allocation of funds from innovative sources to sustainable development and international climate finance, for example by redirecting subsidies away from fossil fuels and from carbon pricing of maritime and aviation transport, and set aside 50% of revenues from the 11 country European financial transaction tax.
8. Meet the longstanding commitment to devote 0.7% of GNI to ODA in a transparent and accountable way and eliminate inflated aid.
9. Ensure the promised new and additional funds for climate finance are over and above aid commitments, and are effectively monitored and transparently reported.
10. Thorough evaluations of development and poverty reduction impact should be conducted, including whether the money could be better used elsewhere, before further promoting the diversion of scarce ODA to blend with loans that mainly benefit European companies.

Help prevent future finance and debt crises

The poorest people and the poorest developing countries are always worst affected by crises. The current financial crisis, largely caused by developed countries' deregulation of finance, is no exception.^{xx} Taking steps at international level to reform global financial rules and to regulate capital flows is important, but must include developing countries. Existing forums such as the Financial Stability Board exclude most developing countries from decision-making.^{xxi} European banks have global reach, and crises in European banks can have huge spillover effects in developing countries. The EU therefore needs to implement far better and more effective regulation of its own financial sector, for example by ensuring that upcoming EU bank reform rules separate retail and investment banking activities.

The financial crisis has caused sovereign debt crises around the world, including in the EU, which has witnessed the huge impact of sovereign debt distress on a country as well as on the overall macro-economic environment. External debt remains a massive drain on developing countries public budgets: debt service on external debt for all developing countries was \$621 billion in 2011.^{xxii} Much of this debt remains of questionable legitimacy. Outstanding EU loans to developing countries must be checked for their compliance with responsible financing principles and thus their legitimacy, following the precedent set by the Norwegian debt audit.^{xxiii} Illegitimate debt must be cancelled.

With the HIPC initiative expiring, situations of over-indebtedness, debt distress or outright debt crises are impossible to manage unless the international financial architecture is updated and new debt work-out mechanisms are put in place. As the EC has recognized, there is an urgent need to "strengthen the international financial architecture for debt sustainability and absorbing shocks." The UN has recently started a process to discuss this critical issue. Fair and transparent debt work out mechanisms would require a neutral body for decision-making on debt restructuring, that is mandated to make binding decisions for all debt, taking into account the needs of developing countries to fulfill their human rights obligations when assessing debt and debt service sustainability, and giving all stakeholders the right to be heard.

The final important tests of EU credibility are:

11. Support and strengthen UN efforts to introduce fair and transparent debt work-out mechanisms.
12. Improve the regulation and supervision of the financial sector, and support developing countries' involvement in reforms.

Conclusion

The financial crisis was created by the rich world, yet poor countries have had to cut vital spending to bail themselves out. The climate crisis was caused by rich countries; though emerging economies are becoming large emitters, the historic responsibility lies squarely with developed countries. While developing countries have shown they can become the main driver of their own development, the EU can support them and be a credible partner in efforts to make all financing work for sustainable development, but only if it also takes action. This paper has set out initial concrete steps that the EU should take, on which we will judge the EU's commitments in the coming months, including the Council's conclusions on the communication on post 2015 financing. By passing these tests, the EU can begin to prove that it can be a constructive and credible partner in global efforts to increase and improve the finance needed to support sustainable development for the good of us all.

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