ODA modernisation

an update following the October 2017 HLM

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briefing
Background

In September, Development Initiatives (DI) published a background paper outlining the various components of ODA modernisation. Since then, more details have been published by the OECD Development Assistance Committee (DAC) on some aspects of ODA modernisation. The October high-level meeting (HLM) of the DAC has also addressed some of these issues. The results of the discussions at the HLM are outlined in their official communiqué.

This document provides an update to our earlier background paper. It focuses on developments in five areas:

1. Private-sector instruments (PSIs)
2. Blended finance principles
3. The reporting of in-donor refugee costs (IDRCs)
4. The publication of the ODA casebook on conflict, peace and security activities
5. The possibility of reinstating countries to the ODA-eligible list.
Private-sector instruments

The DAC moves forward with reporting, despite lack of clear agreed rules

The October HLM was intended to provide an agreement on the rules around counting additional forms of investment in the private sector within ODA. OECD DAC members already invest in the private sector of developing countries, typically through development finance institutions (DFIs) – organisations set up by the donors specifically to make and manage such investments. However, much of this support to the private sector was not eligible to be counted as ODA. In order to incentivise greater support for the private sector in developing countries, the DAC agreed in 2016 that, in future, more investments in private-sector development would be allowed to be counted as ODA. These became known as private-sector instruments (PSIs).

In draft proposals (summarised in our previous paper) the DAC had proposed two ways in which donors could count their support to the private sector as ODA – known as the institutional approach and the instrument approach. Donors could count either capital funds passed to a DFI as ODA (the institutional approach) or they could count the grant element percentage of the investments made by the DFI in developing countries as ODA (the instrument approach).

At the October HLM, the DAC was unable to secure agreement on the proposed PSI rules. Disagreement centred on the level of reference rate that should be used to calculate the grant element of PSIs. There was also disagreement on whether PSIs counted as ODA should be subject to a threshold (i.e. a minimum level of grant element, below which a PSI investment would not count as ODA). The communiqué following the October HLM contained the statement: “We note that at this stage we were not able to conclude in the spirit of consensus our negotiation.”

However, it appears that the DAC members will be permitted to continue reporting PSIs as ODA – despite the fact that specific reporting rules have not been agreed. The communiqué continues:

“Pending an agreement on the Implementation details of all the PSI principles, the donor effort may be measured either at the point of transfer of funds to a vehicle providing PSI to developing countries or for each PSI transaction between the vehicle and the private enterprise or institution in the partner country. We clarify that this relates to PSI that are development-oriented.”

At time of writing there is no clear guidance as to how, given the lack of agreement on the reporting rules, donors will report PSIs as ODA. This situation leaves us with a number of unanswered questions:

- In the absence of agreement on the calculation of grant element, will donors wishing to use the instrument method report their PSI ODA on a cashflow basis – new investments from DFIs minus proceeds from the sale of investments? This
will make ODA on PSI loans inconsistent with ODA on sovereign loans as these, in future, will be counted in ODA using a grant-element basis.

- Will guarantees be allowable as ODA? One possibility is for donors to be allowed to count the full face value of guarantees that are called in – in the event of a borrower defaulting on a loan covered by a guarantee. However, this approach to guarantees has been previously rejected on the grounds that it, in effect, rewarded bad investment decisions.

- Will donors be allowed to count recapitalisation of their DFIs as ODA even if those DFIs have not had their developmental impact assessed by the DAC (the process set out in the draft proposals)? In 2015 the UK and Belgium started to count funding to their DFIs as ODA in anticipation of the rule changes. The assumption (in the absence of information to the contrary) is that these ODA items previously reported will be allowed to remain in the data, and this approach may be continued for future reporting.

Commentators, including DI, have raised questions about the possible impacts on the transparency, consistency and quality of ODA reported under the approach the DAC has set out. The next steps the DAC will take to establish reporting systems on PSI are unclear. It is currently not possible to assess the impacts of the reporting of PSIs on global ODA levels or the ODA of individual donors.

**Blended finance principles**

*The international community may need to help shape future implementation and monitoring*

At the HLM, the DAC adopted a new set of principles that provide high-level policy guidance on the use of blended finance for development. These were prepared by the OECD with the inputs of a multi-stakeholder Senior Advisory Group.

There are five principles, each one comprising three or four sub-principles:

- Anchor blended finance use to a development rationale:
  - use development finance in blended finance as a driver to maximise development outcomes and impact
  - define development objectives and expected results as the basis for deploying development finance
  - demonstrate a commitment to high quality.

- Design blended finance to increase the mobilisation of commercial finance:
  - ensure additionality for crowding in commercial finance
  - seek leverage based on context and conditions
  - deploy blended finance to address market failures, while minimising the use of concessionality
  - focus on commercial sustainability.

- Tailor blended finance to local context:
  - support local development priorities
ensure consistency of blended finance with the aim of local financial market development
- use blended finance alongside efforts to promote a sound enabling environment.

- Focus on effective partnering for blended finance:
  - enable each party to engage on the basis of their mandate and obligation, while respecting the other’s mandate
  - allocate risks in a targeted, balanced and sustainable manner
  - aim for scalability.

- Monitor blended finance for transparency and results:
  - agree on performance and result metrics from the start
  - track financial flows, commercial performance and development results
  - dedicate appropriate resources for monitoring and evaluation
  - ensure public transparency and accountability on blended finance operations.

The development of policy principles for blending by the DAC as a group is fairly significant, as most DAC donors have not published blended finance policies or strategies to date. The DAC also notes that guidance will be developed to help donors in their implementation of the principles, which presently lack detail; it is not yet clear exactly how this guidance will be developed, or how stakeholders may be able to contribute to its development.

The principles have been adopted in parallel with the DAC’s agreement to allow donors to use ODA for PSIs. Many of the instruments used to fund PSIs will be captured by the blended finance definition used by the DAC. The DAC did not, however, commit to systematic monitoring of blended finance at an institutional level, or make a direct link between reporting of PSI and the principles. They did commit to advance their work on blended finance “with other fora and organisations such as the United Nations, Multilateral Development Banks, G7 and G20.”

**In-donor refugee costs**

New guidance to support consistency in donor reporting

The HLM approved revised guidelines for reporting in-donor refugee costs (IDRCs) – these guidelines were prepared by the Temporary Working Group on Refugees and Migration following extensive consultation with DAC members. The previous reporting directives were comparatively brief and lacking in detail. As a result, different donors adopted inconsistent approaches to the reporting of IDRCs in ODA. This issue had become high profile in advance of the HLM, as public attention has turned to the increase in IDRCs as a proportion of ODA in recent years.
The new guidelines seek to improve consistency and transparency in the reporting of IDRCs, focusing on a number of key areas:

- the definition of refugees
- the 12-month period of time for which spending on refugees is allowed to be counted as ODA
- the eligibility of specific cost items for inclusion in ODA
- safeguards around donors’ methodologies, including additional reporting requirements.

The definition of refugees

The new guidelines define a number of categories of refugee – recognised refugee; beneficiary of international protection; a person granted temporary or subsidiary protection; and asylum seekers – which are eligible for IDRCs to be reported as ODA. Crucially, two categories – ‘rejected asylum seekers’ and ‘in-transit refugees’ – are singled out as not falling under the definition of ‘refugee’ for the purposes of ODA reporting. This is notable as, currently, many donors include spending on rejected asylum seekers in their IDRCs reported as ODA.
The 12-month period

Donors have always been able to count IDRCs spent on refugees for a 12-month period. Most donors count this 12-month period as beginning when a refugee arrives or applies for asylum. However, three donors – Canada, Germany, and the US – count this 12-month period as commencing at the point when a decision has been made on a refugee’s asylum status. The new guidelines state that: “The 12-month rule applies from the date of the application for asylum, or, alternatively, the date of entry into a country”. This means that Canada, Germany, and the US will need to alter the way in which they report IDRCs.

Specific cost items

The new guidelines identify a number of specific types of spending that can be reported as IDCRs for ODA purposes, including such items as food, shelter, education, healthcare and language training, but also “voluntary repatriation of refugees to a developing country during first twelve months”, “transport to, and within, the host country in the case of resettlement programmes”, the “rescue of refugees at sea (when it is the main purpose of the operation)” and overheads attached to supporting refugees.

Also, some categories of IDRC are to be explicitly excluded from ODA:

- Promotion of the integration of refugees into the economy of the donor country through tertiary education, vocational training, skills development, job programmes, wage subsidies, etc.
- Construction costs of refugee accommodation.
- Processing of asylum applications.
- Policing and border patrol, including air and coast guard patrols, whose main purpose is the control of borders rather than the rescue of refugees.
- Security screening.
- Counter-trafficking operations and costs for detention.
- Costs incurred for asylum-seekers undergoing ‘fast-track’ procedures in detention centres or any facility in which the right to freedom of movement is denied.
- Voluntary repatriation of refugees to a developing country after first twelve months.
- Costs for return of rejected asylum-seekers.
- Resettlement of refugees to another donor country.
- Forcible measures to repatriate refugees.

It is not yet possible to ascertain what impact this clarification of the types of allowable spending will have on donors’ IDRC reporting. The current data on IDRCs is reported as an aggregate figure and gives no indication as to whether any donors are reporting categories of spending that are excluded under the new guidelines, or not reporting expenditure that is allowable.
Methodologies: new safeguards for consistency

Finally, the new guidelines set a number of principles for donors to follow that are intended to ensure maximum consistency across their reporting of IDRCs:

- Donors should share the model used to assess costs with the DAC secretariat.
- Only direct costs should be reported – donors should not use imputations.
- Reporting should ideally be based on costs for individual refugees – only if national reporting systems do not support this should donors use methodologies that rely on estimating the ODA-eligible share of annual expenditures.
- Donors should improve transparency by providing disaggregated data on the type of spending and the category of refugees receiving that spending.

Peace and security

Greater clarity needed on what security activities are ‘developmental’

Just prior to the October HLM, the DAC published its new ODA casebook on conflict, peace and security activities. The casebook provides case studies to demonstrate how the rules agreed on peace and security at the 2016 DAC HLM can be applied in practice. This provides a resource for donors and implementing agencies that will contribute to greater consistency and comparability in donor reporting. For example, it provides clear examples of the types of training for partner-country military that can be reported as ODA, as per the lists outlined in the reporting directives.

This is a clear step towards strengthened and standardised reporting on peace and security. However, as DI has outlined in more detail elsewhere, there is a need for greater clarity: some rules are still open to interpretation. As a result, there is a risk that the agreed rules may result in some donors diverting resources away from activities with a greater development and poverty-reduction focus in favour of activities that align to national security and political priorities. Examples of areas that need clarification include:

- Some cases are deemed ODA eligible on the basis that the ‘purpose is civilian’ or the project provides a ‘development service’. Parameters determining the types of activities and anticipated civilian/development-related outcomes that fall within these categories should be set.
- Terms used in the reporting rules (such as ‘non-lethal weapons’ and ‘routine police activities’ in regard to supporting partner-country police) would benefit from further detail and definition. This would ensure that, for example, training and use of non-lethal pain-inducing weapons (such as tear gas) and law enforcement activities that cause physical or mental harm to citizens are excluded from ODA. It is generally assumed that ODA cannot be used for such activities, although this is open to interpretation by donors. Clear guidelines on this are urgently needed in the current definition of ODA.
The rules say that training in intelligence gathering on political activities cannot be counted as ODA, but that some data collection for development purposes or preventative or investigatory activities seeking to uphold the rule of law or counter transnational crime can be counted. More explanation is required to clarify the types of intelligence activities that are considered ‘development focused’, and can be reported as ODA.

**Reinstatement of countries that have graduated from ODA-eligible status**

**Changing the approach to countries that are no longer eligible for ODA, but which suffer a natural disaster or economic shock**

To be counted as ODA, developmental or humanitarian spending must be for the benefit of countries or territories that are on the DAC’s list of ODA recipients. If a country or territory achieves high-income status for three consecutive years, it is removed from this list.

The recent hurricanes in the Caribbean caused a great deal of damage in a number of places that were formerly ODA recipients, but have been removed from the list of ODA-eligible countries due to their level of per capita income. This led to calls for some of the affected territories (such as the British Virgin Islands) to be temporarily reinstated to the list of ODA-eligible countries, so that funding for post-hurricane reconstruction could be counted as ODA.

The HLM decided against reinstating any specific countries or territories to the list at this stage. However, the potential was recognised for a country to drop back below high-income status in the face of a natural disaster or economic shock. The HLM communiqué admitted that: “there are currently no rules, nor precedents under the current methodology, for reinstating on the DAC List a country or territory that has graduated and later suffers a persistent drop in its per capita income below the World Bank high-income threshold.”

The HLM therefore agreed to move to address this situation through two initiatives:

- The DAC secretariat will develop evidence-based proposals for the reinstatement of countries or territories in the event of them falling back below the high-income threshold.
- The DAC will also establish a process to examine short-term financing mechanisms available to respond to catastrophic humanitarian crises in recently graduated high-income countries.
Endnotes

4 See note 1
6 Cordelia Lonsdale, 6 November 2017. ‘New Principles for DAC Donors on blended finance’. Available at http://devinit.org/post/new-principles-dac-donors-blended-finance-commit-increasing-transparency-accountability-development-impacts/. A preface in a separate OECD document defines blended finance as “the strategic use of development finance for the mobilisation of additional finance towards the SDGs in developing countries”, with ‘additional finance’ referring primarily to commercial finance (there is not yet a single accepted definition of blended finance in international development policy dialogue and we understand different DAC members have been using the term differently). The OECD’s definition is fairly broad.
9 OECD 2016, Converged statistical reporting directives for the creditor reporting system (CRS) and the annual DAC questionnaire (paragraphs 95–119). Available at: http://www.oecd.org/dac/financing-sustainable-development/development-finance-standards/
10 Sarah Dalrymple, 9 November 2017. ‘Revised ODA casebook on conflict, peace and security: A useful resource but falls short of providing practical guidance on what activities can and cannot be counted as aid’. Available at: http://devinit.org/post/the-revised-oda-casebook/
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