G-24 Technical Group Meeting

2-3 March, 2015

Beirut, Lebanon

SUMMARY REPORT

The Spring 2015 Technical Group Meeting was held in Beirut on March 2-3, hosted by the current G-24 Chair, Lebanon. Members discussed priority issues for the Group at this juncture, including financing for development, the role and reform of multilateral finance, international tax cooperation, and sovereign debt restructuring. Participants benefitted from the perspectives of expert speakers as well as country discussants, whose inputs served to underpin substantive deliberations and lesson sharing. The points of consensus and priorities that emerged from discussions will provide a strong foundation for the upcoming Ministerial meeting in April in Washington, D.C., and will also enable the Group to engage productively in current global debates. Key lessons and takeaways from each session are outlined below.

Session 1: Financing for Development Agenda – Implications for the G-24

The opening session of the meeting focused on financing for development (FfD) and the perspectives of G-24 members. This topic has practical significance for the Group at this moment, in light of the global deliberations underway in the lead up to the Third International Conference on Financing for Development in July in Ethiopia and the articulation of the sustainable development goals (SDGs) to be agreed upon in at the United Nations General Assembly in September under the umbrella of the post-2015 development agenda. The lead speaker in this session was Alex Trepelkov, Director of the Financing for Development Office at the UN Department of Economic and Social Affairs, and he provided an overview of the preparations, consultations, and anticipated outcomes for the upcoming Addis Ababa FfD conference.

A consultation process has been underway in the UN since last year, involving numerous stakeholders across governments, civil society, international institutions, and the private sector. A draft document to form the basis of consensus in Addis is currently being prepared by the Co-Facilitators of the UN-led Preparatory Process[1], and will be ready by the end of March. The foundation of the consensus document will be a cohesive framework for sustainable development, addressing its economic, social, and environmental dimensions, and supported by policy commitments and concrete deliverables. This document will build on the Monterrey Consensus – which recognized the importance of different financing sources – but will include important distinctions, reflecting the evolution of the global financing landscape in the last decade. Mr. Trepelkov outlined the status of discussion across the various pillars:

- A strong domestic public finance pillar is essential for the provision of basic social needs as well as sustainable infrastructure, both of which lie at the core of growth and development aspirations. Across all countries and regions, improved domestic resource mobilization will be a central element of the FfD agenda, and will require concerted reforms and augmented capacity. There are ongoing discussions regarding proposed target revenue-to-GDP ratios for low- and middle-income countries, as well as a proposed "new social contract" on minimum social spending, although these still need

[1] H.E. George Talbot, Permanent Representative to the UN for Guayana and H.E. Geir Pederson, Permanent Representative to the UN for Norway.

further elaboration. It is also clear that domestic efforts must be accompanied by international support for capacity building as well as significant efforts towards tax cooperation and addressing tax evasion and tax avoidance through profit shifting, which contributes to erosion of the tax base.

- Private finance is a key driver of increased productivity and job creation, and will be crucial in meeting development aspirations, given the scale of potential pools of resources. However, the challenge of channeling domestic and international private finance towards investment opportunities in developing countries, particularly in infrastructure, SMEs, and public goods, will require addressing the enabling environment and improving risk intermediation. Multilateral development banks (MDBs) can play a central role in this regard.
- International public finance is essential for ending poverty and providing basic social needs, especially in the least developed countries (LDCs). For this reason, official development assistance (ODA) will remain crucial for these countries, and there is growing agreement to allocate 50% of ODA to LDCs. ODA also needs to play a greater catalytic role, particularly for leveraging private financing and for supporting efforts for climate resilience and environmental sustainability. It will be necessary, therefore, to address the issue of delivery of commitments, targeting of resources, and effectiveness. Strengthening multilateral finance will also be required.
- Trade and debt sustainability will also constitute important channels for facilitating the flows of FfD. Additionally, and differently from the Monterrey consensus, science, technology, and innovation have been recognized as important components of development financing with strong multiplier benefits. However, innovative capacity and access to technology is markedly uneven between developing countries and will need to be improved via domestic and international efforts. Finally, systemic issues continue to impact the financing architecture, and it will be necessary to strengthen safety nets, improve stability, and undertake governance reforms in the international financial institutions.

In addition to the commitments regarding the modalities of finance, the Addis consensus document will also provide for increased monitoring and mechanisms for follow up, which will enhance the accountability of the overall framework.

Following Mr. Trepelkov's presentation, members discussed the implications of the FfD agenda and the preparatory process for Addis, including the elements of potential consensus. Lead discussants from India, Lebanon, and Peru provided a range of country perspectives to initiate the Group's deliberations. India pointed to the importance of domestic resource mobilization, but also noted that setting tax revenue to GDP and other targets must be approached with sensitivity and caution, given the sovereign nature of the issue. There are important avenues for support from international community and institutions, particularly in terms of assistance for capacity building and enhanced international tax cooperation so as to address harmful practices. On the part of Peru, it was pointed out that the overarching importance of inclusive growth must remain at the center of the FfD agenda, given its role in generating sufficient resources to reduce poverty and meet development goals. In this regard, development financing frameworks will need to be underpinned by sound policies and institutions, in order to create market conditions for investment and economic transformation. Implementing these reforms will require strong political will, persistence in implementation on the part of policy makers, and an ability to learn from experience and mistakes. The discussant from Lebanon focused more specifically on the challenges for international public finance and ODA, particularly in light of the changing global economic circumstances and the failure to meet commitments made in Monterrey.

Building upon these insights during the open discussion, participants broadly expressed support for the elements of FfD and the need to tap diverse sources of financing, agreeing nevertheless that the responsibility for sustainable development, and the utilization and mobilization of finance, will first and foremost lie with sovereigns. Countries will need to strengthen their domestic public financing pillars through effective domestic resource mobilization and allocation of public expenditures. At the same time, it was noted that any targets on revenue and expenditure set by the global community must give due consideration to widely divergent situations and capacities at the country level, and must avoid being unduly prescriptive. It was also stressed that efforts at the national level will need to be complemented by global efforts to support capacity building and to foster effective international tax cooperation in tackling harmful tax practices such as tax evasion and profit shifting. In this regard, the work of the High-Level Panel on Illicit Financing Flows from Africa was referenced, particularly vis-à-vis the challenges posed by illicit flows and the need to measure and address these better.

Members strongly agreed that private finance has a growing role to play, but that leveraging the full potential of private funds will require a strong enabling environment and new instruments, especially in order to facilitate investments in infrastructure. At the domestic level, a number of G-24 countries have experienced success in leveraging domestic savings, notably through better pension systems, in order to support long-term financing, and such experiences could provide valuable insight for the Group. The attention given to infrastructure within the FfD agenda was welcomed by participants, in conjunction with the focus on poverty alleviation and investing in human development. In this regard, the MDBs and international financial institutions (IFIs) can play a constructive role through knowledge provision and sector assistance, as well as wide a range of supply- and demand-side interventions, including financing provision, capacity building, institutional improvements, and risk intermediation. A number of participants noted that more attention could also be given to remittances, including, for example, the roles of home and host countries in reducing associated costs. There was also broad discussion of the need to reform development assistance, both official (ODA) and non-official, so as to ensure it supports those most in need, particularly in the LDCs. Fulfillment of commitments, improved targeting and effectiveness, and greater accountability must be at the core of such activities.

Finally, there was strong consensus that the G-24 has a central role to play in engaging in global discussions on behalf of members and pushing for ambitious and appropriate outcomes in Addis and beyond. Given the scope of the agenda and the need to ensure ownership and implementation of commitments made, members stressed the importance of meaningfully involving Ministers of Finance and Central Bank Governors in the broader international consultations.

Session 2: Addressing Shortcomings in Sovereign Debt Restructuring

The second session of the meeting covered the issue of sovereign debt restructuring and the need to address the shortcomings in the existing framework for dealing with sovereign debt. Domenico Lombardi, Director of Global Economy at the Centre for International Governance Innovation (CIGI), gave the first presentation. Mr. Lombardi began by describing the history and context of sovereign debt restructuring, noting that, while the phenomenon is not new, novel challenges have arisen in recent years that have given rise to discussions on reform of the international debt architecture. Against this backdrop, he outlined possible avenues for addressing the systemic challenges inhibiting the orderly resolution of debt difficulties, and discussed the perspectives of various stakeholders across regions[2]. He summarized a variety of reform approaches under consideration in the international arena, including those of a contractual, statutory, and arbitrational nature, as well as more innovative proposals such as the Sovereign Debt Forum[3]. Noting the widely divergent views within the global community regarding the way forward, he concluded by

[2] These perspectives were collected as a part of the Global Consultations on Sovereign Debt, being undertaken by CIGI in partnership with the New Rules for Global Finance Coalition. The aim of this process is to collect input from a diverse group of stakeholders, including in academia, civil society, national government, international organizations, think tanks, and the legal field. The final report will be presented at the Annual Meetings in Lima in October.

[3] The proposed Sovereign Debt Forum would operate as a semi-formal institutional venue where sovereign debtors and their creditors could come together without stigma and discuss concerns and strategies for dealing with debt difficulties.

emphasizing that these approaches are not mutually exclusive. Rather, it is possible to reform the arrangements governing sovereign debt in a multi-modular manner, selecting from a menu of options to address the scope and nature of the challenges in the existing architecture. He noted that adequate financial safety nets and appropriate lending frameworks in the IMF will be important complements to any reform efforts.

Mr. Lombardi was followed by the session's second lead speaker, Reza Baqir, Chief of the IMF's Debt Policy Division. Mr. Baqir outlined the IMF's ongoing work related to sovereign debt restructuring and described the analytical and policy-based efforts underway to improve the Fund's lending framework and its ability to prevent and manage sovereign debt crises. He framed his presentation by noting that the IMF's work centers on reforms that are both desirable and feasible, with a market-based/contractual focus. Mr. Baqir outlined the four main elements of the Fund's work program: strengthening the Fund's lending framework to make it more efficient to prevent and resolve sovereign debt crises, improving contractual provisions in international sovereign bond contracts, clarifying the framework for official sector involvement in light of the changing landscape of official bilateral lending, and reviewing the Fund's policy on lending into arrears. Mr. Baqir noted that the Fund's current work is focused on improvements to the lending framework. He described the evolution of the Fund's lending policies culminating in the creation of a 'systemic exemption' that allowed Greece to obtain assistance in 2010 despite the absence of a high probability that its debt was sustainable. He concluded by noting that the IMF's Executive Board is set to consider adjustments to the lending framework to (a) make the underlying lending framework more flexible with the introduction of a debt reprofiling option and, at the same time, (b) remove the systemic exemption which has not proved effective at resolving debt crises or addressing contagion.

Following the lead speakers, a lead discussant from Trinidad and Tobago outlined the unique and significant debt challenges faced by Caribbean countries. For these countries, particular vulnerabilities resulting in large debt burdens have left them with unsustainable levels of debt and significant risk of distress; at the same time, their middle-income status renders them ineligible to access concessional international debt relief funding. For this reason, Trinidad and Tobago has proposed the heavily-indebted middle-income country (HIMIC) initiative – a framework for debt restructuring for Caribbean countries that would enable them to escape intractable debt difficulties[4]. Nigeria served as the second lead discussant and provided an overview of the country's experience leading up to its debt relief and restructuring in 2005 through the Paris Club. A number of key lessons were distilled for the Group: specifically, that the multiple players, complex relationships, and blurred responsibilities of sovereign debt necessitate effective communication and clear stakeholder ownership in debt discussions and restructuring processes. It was also emphasized that a strong voice from developing countries is essential in ensuring the international system of sovereign debt restructuring is strengthened in a balanced and effective manner.

The issue of sovereign debt restructuring is a complex and contentious one, and open deliberations amongst participants reflected the divergent views held within the Group. Nevertheless, there was broad agreement regarding the need to consider the issue more deeply at the collective level and find points of consensus. Participants recognized that the inadequacies and deficiencies in the existing framework for dealing with sovereign debt have had very costly results, and a number of challenges must be examined further, including: excessive sovereign debt indebtedness, interventions that come 'too little too late', disorderly sovereign defaults, and the difficulties posed by hold outs and intractable creditors.

There was extensive discussion of the positive steps that have been taken to strengthen the contractual framework for debt issuance and clarify IMF lending policies in recent years. It was noted, for example, that the revised collective action clauses (CACs) are already yielding results, with seven countries using them in

[4] The framework would also share responsibility between, and safeguard the rights of, various stakeholders

their recent bond issues. Progress in the contractual framework and in the IMF lending framework addresses a number of shortcomings in existing processes for debt and default management which will have a beneficial impact going forward. However, many participants pointed out that contractual measures are not, in fact, a panacea, and do not resolve many of the problems associated with the existing stock of sovereign debt. For this reason, some members favor pursuing multilateral dialogue and a statutory approach, overseen by an external commission. In this context, it was mentioned that the UN provides a potential forum for such discussion, and can bring to bear a stronger voice of developing countries[5]. In general, most participants stressed the importance of countries managing their debt and investing in a productive way.

More broadly, it was recognized that this issue has potential implications for the stability of the overall financial system, of which all countries are stakeholders. As such, a variety of dimensions and modalities for strengthening the framework for sovereign debt restructuring should be considered and explored. The session concluded with agreement that further dialogue, both internally amongst members and externally with broader stakeholders, should be pursued.

Session 3: The Role and Reform of Multilateral Finance

Multilateral development banks have served as a central pillar of the global financing architecture for over half a century, and it is clear that they will have a key role to play in meeting the enormous financing needs across the developing world in the years ahead. The third session of the meeting focused on the scope and mechanisms by which MDBs can more adequately and appropriately contribute to the development finance agenda in the context of an evolving global financing architecture.

Lead speaker Chris Humphrey from the University of Zurich discussed the challenges and opportunities within the MDB system vis-à-vis capital requirements, instruments, business practices, and governance, emphasizing the need for adaptation and innovation in both existing and new institutions. Mr. Humphrey framed his presentation by noting the structural change that has taken place in the global economy, whereby developing countries now account for a far greater share of growth and the profile of MDB borrowers has evolved considerably. He also noted that while MDBs have served as a useful model for development finance cooperation, many existing institutions face a number of operational limitations that prevent them from maximizing their potential, with governance serving as an overriding constraint. In order for institutions to exercise their full potential as an important intermediary and catalyst of development finance and assistance, they will need to address a number of key challenges:

- In terms of financial capacity, most MDBs are undercapitalized to deal with the enormous needs of borrower countries, especially for infrastructure investments. This is due, in part, to the inability of the non-borrower countries to either contribute to capital or allow borrower countries to do so, as well as to a very low ratio of paid-in to callable capital; at the same time, many institutions are highly conservative in their use of capital.
- The bureaucracy of existing institutions continues to be very slow and cumbersome, resulting in extensive and uncertain delays in loan processing. At the same time, safeguard policies have become increasingly complex and burdensome. The many protection layers that respond mostly to concerns of non-borrower countries have contributed significantly to the consistently slow and inflexible process of loan approvals, especially for infrastructure projects.
- The issue of governance lies at the core of many of the challenges faced by MDBs, with most institutions continuing to be dominated by non-borrower countries, despite shifting global economic realities[6]. Outdated governance structures continue to define the policy- and decision-making processes, creating tension between borrower and non-borrower shareholders and undermining the effectiveness and even

[5] To this end, it was noted that the UN will be releasing a roadmap on sovereign debt workouts at the end of March.
[6] Albeit with a few important exceptions, such as CAF and the Islamic Development Bank.

perceived credibility of the institutions. The presentation noted differences in operational practices of other MDBs that are borrower-owned, with their consequent strengths and challenges.

Mr. Humphrey concluded by noting the emergence of new institutions in the MDB landscape, both in response to the enormous financing needs as well as to the challenges facing existing institutions. The New Development Bank proposed by the BRICS's countries (Brazil, Russia, India, China, and South Africa) and the Asian Infrastructure Investment Bank (AIIB) have strong potential to contribute to meeting investment requirements across the developing world, particularly in infrastructure. They also represent an opportunity for developing countries to engage the multilateral system on their own terms, with potentially catalytic effects on the MDB system more broadly. Yet, their effectiveness will be greatly influenced by their ability to learn from the strengths, limitations and structures of existing institutions.

Following Mr. Humphrey's presentation, China served as the session's lead discussant, providing an update on the establishment of the AIIB and the efforts underway to ensure the institution is as effective and catalytic as possible. The main rationale for the AIIB's establishment is to focus on infrastructure development and address large funding gaps, to improve regional resilience to external financial shocks, and to enhance regional integration and connectivity. The AIIB's Articles of Agreement are expected to be signed by its founding members by mid-2015, and the Bank is expected to start operations by end-2015. It was also stressed that AIIB will complement rather than compete with existing MDBs. Lastly, it was recognized that the AIIB intends to learn from the lessons of the existing MDBs, adapting their best practices while, at the same time, avoiding their failures.

During the open discussion, members drew from the framework and insights of the presentations provided, and deliberated in what manner and extent to which multilateral finance should reform in order to meet the growing needs of developing countries. There was strong consensus about the crucial role MDBs have to play in FfD and sustainable development, particularly with regards to infrastructure and public goods. MDBs have a unique capacity to address demand-side constraints through capacity building and assistance in identifying and preparing projects, as well as supply-side challenges, through risk mitigation and leveraging of private finance (including new and innovative sources such as institutional investors).

Members emphasized, however, that the constraints in the existing multilateral architecture inhibit MDBs from fulfilling their potential as financing catalysts and intermediaries, and prevent them from meeting developing countries' needs. For this reason, reform was seen as crucial and participants highlighted the need to adapt instruments, safeguard policies, lending capacity, and business practices as a matter of priority. There was also widespread agreement that the emerging institutions should work in cooperation and collaboration with the existing MDBs in order to create additional financial capacity for development rather than further fragmentation.

Most importantly, members acknowledged that governance represents the central challenge for existing MDBs, and could also serve as a potential impediment to the success of new institutions. To this end, there was strong agreement that reformed governance structures are essential, and that these must give a strong voice to developing countries in a manner that reflects their important and growing role in the global economy. Participants expressed optimism regarding the proposed inclusiveness of new institutions, but cautioned that their credibility and legitimacy will depend on their ability to learn from the mistakes of existing MDBs and ensure inclusive membership as well as balanced voice and representation for all members.

Session 4: Enhancing the Tax Base and International Tax Cooperation

At the core of the FfD agenda is the issue of domestic resource mobilization, and it will be crucial for developing countries to enhance their tax bases in order to meet growth and development aspirations. Although these efforts must revolve around augmenting capacity, increasing revenue collection, and improving expenditure management, it will also be necessary to address the interaction of tax structures that enable multinational corporations and individuals to avoid or evade the payment of taxes. International tax cooperation, therefore, has a central role to play, in order to ensure a more efficient and inclusive global tax system.

The session's first lead speaker was Pascal Saint-Amans, Director of the OECD's Centre for Tax Policy and Administration (CTPA). He began by outlining two of the CTPA's primary work program priorities at present: promoting exchange of information and putting an end to bank secrecy, and addressing base erosion and profit shifting (BEPS). With regards to the latter, he noted that the OECD was called on by the G20 in 2013 to develop an ambitious action plan that would coordinate country efforts to address BEPS. Mr. Saint-Amans described the fifteen point action plan that is underway, which revolves around bridging the gaps and mismatches between domestic tax systems, addressing deficiencies in international standards and bilateral instruments, and increasing transparency, while also addressing issues related to the digital economy, to which current international standards do not apply. Among G20 members, progress on a number of key action items has taken place; yet, there is much left to do. More broadly, Mr. Saint-Amans emphasized that BEPS is a collective challenge requiring collective solutions. As such, the G20 requested the OECD to deepen the engagement with developing countries in the BEPS project, in order to strengthen cooperation in tackling harmful tax practices and aggressive tax planning. This issue has important implications for G-24 members, and a number of avenues for engaging in the ongoing global work were outlined.

The session's second lead speaker, Michael Keen, Deputy Director of Fiscal Affairs at the IMF, provided an overview of the Fund's analysis regarding the spillovers of international corporate taxation on developing countries. He highlighted the complex nature of the interactions in the international tax system and discussed the cross-border effects of mismatches and gaps created by domestic legislation and bilateral treaties. He emphasized that, although complex and difficult to measures, the negative spillover effects of the corporate tax system are significant for developing countries, especially low-income countries with fewer alternatives to corporate tax revenue. Mr. Keen identified three key issues that have a particular impact on developing countries and need to be addressed: (i) 'treaty shopping', whereby multinationals utilize treaties that reduce their tax burdens under the guise of stimulating investment; (ii) indirect transfer of interest, whereby capital gains are realized in low-tax jurisdictions (this is especially important with regards to extractive industries); and (iii) transfer pricing, which takes advantage of weaknesses in the 'arms-length' principle of valuing transactions. Mr. Keen concluded by stressing the importance of capacity building in order to overcome these challenges. He also stressed that rules matter, and developing countries should be given a strong voice during international deliberations on how the rules evolve, given how much they have at stake.

Following the presentations, South Africa and the Philippines served as the lead discussants of the session. As a member of the G20 and an active participant in the G20-OECD BEPS work, South Africa noted that it uses its presence in these deliberations to voice the position of developing countries and ensure their concerns are taken into account. With regards to the global discussions underway, three key issues were outlined: the importance of capacity building, not just on technical issues but on the basics of setting up an efficient and effective revenue administration; the exchange of information, which serves as a powerful tool for cooperation, particularly through the work of the Global Forum on Transparency (which South Africa chairs), as well as through the automatic exchange of information (AEOI) efforts; and the BEPS project, which is an ambitious and wide-reaching initiative that will effectively enable tax administrators to develop tools to collect more revenue that can be mobilized for domestic purposes. The second lead discussant from the Philippines built on these comments, noting the challenges faced by developing countries in an increasingly globalized world, where the capacities of multinational corporations to aggressively tax plan and avoid taxation exceed the capacities of governments to implement effective revenue administration and benefit from international initiatives. To address this, the Philippines has been actively engaging in global efforts across a number of areas – including the exchange of information, ending bank secrecy, addressing transfer pricing, and collecting data – and noted the importance of continued support from the global community and international organizations.

During the open discussion, there was strong agreement on the value of collective action to address harmful tax practices. Members concurred that developing countries are often most affected by harmful tax practices and negative spillovers, given that they rely more heavily on corporate income as a part of their domestic resource base. For this reason, they have a strong stake in the evolution of international tax rules, and need to be actively engaged. However, it was also noted that many developing countries, including within the G-24, lack the capacity to influence, participate in and benefit from global initiatives. For this reason, participants stressed that international discussions must acknowledge that differing levels of capacity and readiness across countries and regions, taking these into account when identifying timelines and priorities for common measures.

At the same time, capacity building was seen as imperative, given that it underpins progress both domestic and global efforts. International partners, including multilateral and regional organizations, have an important role to play in this regard. It was suggested that the Group should pursue these efforts with vigor, including by first performing diagnostic exercises where appropriate.

In discussing the importance of tax cooperation to developing country efforts to mobilize sustainable resources, attention was drawn to the results of the High-Level Panel on Illicit Financing Flows from Africa, led by former South African President Thambo Mbeki. According to the report, such flows deprive countries in the continent of tremendous resources, which manifestly impacts their sustainable financing endeavors. Addressing this challenge was seen as essential, though an important clarification was made regarding the distinction between illegal actions such as tax evasion and those tax practices which are entirely legal but still detrimental to countries whose revenue bases are eroded through tax avoidance, harmful practices and aggressive tax planning.

Participants concluded in consensus regarding the need for greater engagement in international discussions by developing countries; however, they underscored that this must be meaningful and on equal footing, which would require greater effort on the part of those leading the initiatives. Importantly, it was agreed that the G-24 can play an important role in engaging systematically and providing a collective developing countries voice in global processes.