Bundesministerium für
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Concept Paper on Approaches for a New Reporting System on Development Finance

The global landscape has been fundamentally transformed over the past few decades. Traditional development finance, as captured notably by ODA, will continue to be an important catalyst, but in the majority of developing countries, it is far exceeded by other flows.

There is agreement on the need to review the extent to which current measurements and their underlying concepts continue to be relevant in today's world. Providers of aid are looking for a better way of capturing contributions to development in order to get a fuller picture of total development efforts. ODA has been and continues to be instrumental in encouraging and measuring increasing international commitments and donor effort for development in a transparent way. Key factors framing this discussion about the revision of the reporting system are:

a) coherence with the post-2015 development goals (aimed at a comprehensive sustainable development agenda, covering not only poverty but also global public goods such as climate protection and security);

b) based on this, the need to capture not only traditional budgetary effort but also other officially stimulated flows as well as the need, in assessing development cooperation, to increasingly include outputs and results (recipient benefit) rather than just pure inputs (donor effort);

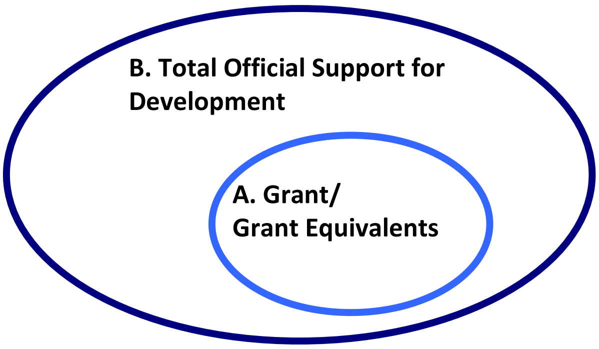
c) the necessity to preserve the achievements and credibility that ODA brought about, and the need to hold donors accountable while at the same time creating incentives for a more catalytic use of official resources for the mobilisation of additional private funds.

An Integrated Approach: The Two Circles Concept

All the above-mentioned key factors could be appropriately addressed by what is called the **Two Circles Concept**, which includes a reduction of ODA to its core elements (circle A: Donor Effort) while introducing an enhanced measure of other public development finance (circle B: Recipient Benefit). In this integrated approach, circle A would be part of the broader measure of circle B.

The inner circle would only measure grants and the grant elements of loans, while the resulting non-grant elements of donor funding would be captured in an outer circle, which represents the ultimate benefit of the entire intervention for the borrower.

Example: grants and the grant element of a loan would be reported in circle A, while additionally the non-grant part of the loan would be reported in circle B, adding up to the face value of the loan (including the grant equivalent part from circle A). Circle A mainly reflects net transfers, while circle B reflects gross transfers.



This concept ensures full transparency of donor effort on the one hand, while at the same time allowing for a measure presenting a much broader picture of official development finance on the other. It provides incentives to mobilise additional resources in line with the HLM mandate and still holds donors accountable in that it encourages them to provide budget-financed grants. In addition to the more political arguments for this concept mentioned above, there are several technical advantages.

The concept covers all financing schemes which comprise elements that are eligible for the inner circle (i.e. that have a positive grant element). This also solves the problem of the need to fix an adequate minimum grant element and of defining "concessional in character", as any financing mobilised with official financial support would be reportable under this system, no matter with which form of subsidy the grant element has been achieved (by injecting budget funds or by providing a guarantee), and it provides a solution to the net/gross measurement question.

The approach allows the inclusion of innovative financial instruments (e.g. the value of guarantees and other risk mitigation instruments), which could be treated the same way as loans (grant equivalent under circle A, resulting total face value of mobilised capital (including circle A amount) under circle B).

The concept however still requires donors to agree on an up-to-date and sufficiently dynamic discount rate for calculating the grant element. In our view, in order to avoid setting the wrong incentives, the calculation of the grant element should follow a market-based approach, taking into account the specific risk of a given recipient country.

Moreover, as the size of the grant element is the decisive factor for accounting towards the inner or outer circle, grant-financed interventions that remain disputed, such as student costs, refugee costs, etc. are still part of the system.

As a possible alternative to the focus on grants and grant equivalents, the donor effort in circle A could be captured by measuring donors' budgetary effort for development, while again the outer circle would capture total official support for development (including officially mobilised funding from the market).

Conclusion

The two circles approach might not be a perfect solution to each of the said challenges in every respect, and the details of this proposal – particularly the criteria for transparent differentiation – certainly need to be elaborated. However, it is a fairly simple approach to overcome some of the most important shortcomings of the present system, and it is fully in line with the HLM mandate: it keeps the value, credibility and achievements of the traditional ODA definition but also acknowledges its weaknesses and the increasing significance of other financing instruments for sustainable development which should be included in the monitoring and reporting effort in future.