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Financing Sustainable Development in the Era of COVID-19 and Beyond

An analysis and assessment of innovative policy options

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Executive Summary

In the early days of the COVID-19 pandemic, the United Nations (UN) estimated that developing countries needed an extra US$ 2.5 trillion in external finance to cope with the consequences of the crisis. This vast sum is needed because additional spending needs – for example on health services and social protection – coincide with a simultaneous collapse of all traditional sources of development finance: tax revenue, export earnings, migrant remittances, foreign direct investment and, to a lesser extent, also official development assistance (ODA).

In order to discuss how these finances could be mobilized, the governments of Canada, Jamaica and the UN Secretary-General launched the policy dialogue on "Financing for Development in the Era of COVID-19 and Beyond" at the UN in May 2020. By September, the process had delivered a 129-page menu of options that contains about 200 policy proposals. Our paper picks some of the most promising and most innovative proposals that have the highest potential to raise the resources needed to reach the target, and explains and assesses them. We also look at the political feasibility of each of the proposals.

BRIEFING

The UN's menu rediscovered **the use of monetary resources for development finance** in the COVID-19 crisis. Following the example of advanced economies, where central banks bore the brunt of crisis response, the menu suggests that the International Monetary Fund (IMF) should issue Special Drawing Rights (SDRs) for the benefit of developing countries. The UN had originally suggested an issuance worth US$ 1 trillion. The vast majority of IMF Member States support the option. A new US government could ensure the necessary 85 % majority on the IMF board to adopt the proposal.

A second set of options is related to debt. Debt relief would not inject fresh money into developing countries but it would ensure that they could use their own domestic resources for crisis response rather than debt service. Debt relief can release substantial amounts of money, but the impact is stretched over time as the maximum amount freed up in a given time period is the debt service due during that period. For the group of low-income countries, debt service on external debt is about US$ 40 billion annually. Consensual debt relief is difficult to organize as creditors are dispersed and many face their own constraints to grant debt relief. Creditor governments can only make direct decisions for official loans. Cancelling private debt would require international financial architecture reforms – or drastic measures such as a UN Security Council Resolution. Debtors can suspend payments at any time, but this might trigger creditor litigation or other sanctions.

A third set is related to raising taxes. Alongside debt payments, tax dodging is the second black hole for developing countries' resources. Policy options are to improve the tax governance architecture so as to curb tax dodging, and to raise more taxes through progressive taxation. The profit shifting by multinational enterprises alone causes a global loss of tax revenue of more than US$ 500 billion annually. In a similar way to debt relief, reforming the international architecture and/or national tax systems takes some time, and would provide few additional resources per time unit. However, it would do so in a sustainable manner. Tax reforms towards more progressive tax systems do not require multilateral agreement, but might lead to capital flight and tax arbitrage when done unilaterally in an uncoordinated manner. Setting up a global tax body at the UN level would help to coordinate tax policies.

A fourth set is the use of external public resources – loans and grants – through new multilateral facilities. The largest suggested in the UN's menu is the Fund to Alleviate COVID-19 Economics (FACE), which would provide funding to the tune of 3 % of developing countries' GDP. However, new vertical funds such as a Global Fund for Social Protection are also now being discussed. The bottleneck is that new facilities would need to be fuelled by grants from richer countries if they were to provide highly concessional finance. Just closing the gap from the current level of official development assistance that rich countries provide – 0.3 % of their Gross Domestic Product (GDP) in 2019 – to the UN's 0.7 % target could provide an extra US$ 204 billion per year for additional grants, or through leveraging an even larger volume of concessional loans. Richer countries should act in solidarity and at least deliver the 0.7 % of Gross National Income (GNI) in ODA committed for 50 years now.

Lastly, the menu includes options to **redirect private finance into more sustainable purposes,** align it with the Sustainable Development Goals (SDGs) and the Paris Climate Agreement. Institutional investors manage about US$ 200 trillion in assets, and while the share of money dedicated to green and social investments is already rising, it remains small. Better taxonomies and standards for disclosure of environmental and social information related to investment products could guide investors' decisions and prevent 'green washing'. A second option here is that governments – which collectively spend US$ 11 trillion on public procurement every year – could insist that private contractors comply with the highest social and environmental standards when they are bidding for public tenders.

No single option is a silver bullet to respond to this crisis. In an optimal case, the international community would start now to set simultaneous processes in motion: issuing and redistributing SDRs, debt relief, scaling up Multilateral Development Bank (MDB) lending and increasing national ODA budgets are speedy ways to mobilise fresh liquidity, while reforms of the international financial architecture are needed to ensure sustainability and more resilience to face the next shock.

Introduction: The UN process Financing for Development in the Era of COVID-19 and Beyond

The COVID-19 crisis has been a wake-up call for the international financing for sustainable development agenda. It has unleashed an enormous political momentum, including at the UN, where the ad hoc process "Financing for Development in the Era of COVID-19 and Beyond" was kicked off by a joint initiative of Canada, Jamaica and the UN Secretary-General in May 2020.[1]

The process's first High-Level Meeting on 28 May 2020 saw an impressive participation by Heads of States, including all from the five largest EU Member States. The Finance Minister Meeting on 8 September was the largest such gathering under the auspices of the UN ever, convening close to 40 Finance Ministers and Vice-Ministers, and other senior representatives. The second High-Level Meeting on 29 September 2020 was similarly impressive as it again convened a large number of heads of states or governments, although with diminishing interest from the global north, whose countries in some cases (UK, FR, EU) scaled down their participation to ministerial level, or were absent (DE, US).[2]

Also remarkable was the consistent and constructive engagement of the Heads of the IMF (Kristalina Georgieva), the World Bank (David Malpass) and the Organisation for Economic Co-operation and Development (OECD) (Angel Gurria) in a UN process. In an era where the cooperation of nation states within international organizations does not always work so well (the crisis of multilateralism), at least the interagency cooperation between these organizations shows signs of improvement. In the case of the IMF, it might have helped that Georgieva – a former EU Commissioner for Humanitarian Aid – is not as alien to the UN system as her predecessors were, most of whom had previous careers in finance ministries or central banks and thus little experience in engaging with the UN system.

Apart from the new political dynamic, this year also saw a remarkable conceptual and intellectual renaissance of the financing for development agenda. The UN process culminated in a 129-page menu of options that outlines about 200 'policy options'.[3] This includes rediscovered or entirely new proposals for financing facilities, new ways of mobilizing finance, an extensive selection of measures around debt and a large variety of regulatory measures, incentives or standards around sustainable private finance.

The menu of options is an aggregation of ideas developed by six Discussion Groups (DGs) between June and August 2020. All of these groups were co-led by two or more UN Member States, enjoyed Secretariat support by UN agencies, and were composed of a multi-stakeholder membership consisting of UN Member States, as well as experts of international organizations, civil society organizations (CSOs), private sector and academia.[4] The thematic focus of the six DGs was:

The six discussion groups of the FfD in the COVID-19 era process

1. External Finance and Remittances, Jobs and Inclusive Growth
2. Recovering Better for Sustainability
3. Global liquidity and financial stability
4. Debt Vulnerability
5. Private sector creditors engagement
6. Illicit Financial Flows

Source: United Nations

1 The process's official website is: https://www.un.org/en/coronavirus/financing-development

2 The second High-Level Meeting was renamed in "Financing the 2030 Agenda for Sustainable Development in the Era of COVID-19 and Beyond".

3 There are four different versions of the menu of options: One long, and one short version produced for the 8 September Finance Minister Meeting: One long, and one short version for Heads of State meeting on 28 September. All references in this paper refer to the long version for the Heads of States: https://www.un.org/sites/un2.un.org/files/financing_for_development_covid19_part_ii_hosg.pdf

4 Global Policy Forum contributed to the debates of DG4 and 5. Some of the ideas we had fed into the debate did not make it into the menu of options. That is to say that the debate was intellectually even richer than the menu of options.

When the process began in May, it was not clear if the outcome would be an actual "decision" – the term appeared on the website for quite some time as an intended outcome – or just a selection of proposals. It turned out to be the latter. This was unfortunate on the one side, as the COVID-19 crisis requires bold policy actions, which so far no multilateral body has been able to deliver at the adequate scale. But it was good on the other side, as many of the policy options cited in the paper had been unlikely to find unanimous consensus by the whole UN membership, especially not in such a short timeframe and under the difficult negotiating conditions in the pandemic summer of 2020.

The composition of the six different DGs also indicated country preferences and country needs. While DG3 (on liquidity), DG4 and 5 (on debt) and DG6 (on illicit financial flows) had a relatively strong balance of developing countries in their membership, the DG2 (Recovering Better) and DG1 (external private and public finance) saw disproportionately strong representation by richer countries.

The Member States' preferences for different issue groups show that especially smaller developing countries expect the UN to be the place where international financial policies and affairs is discussed. This is not surprising given that they do not have a seat at the table at bodies such as the G20 or the G7, nor at the Western nations' creditor cartel Paris Club, or at the OECD. Richer countries saw the UN mainly as a place to discuss SDG-related issues.

Ironically, a comparison of the options or policy suggestions by DG1 and DG2 also indicated the range of opinions in the debate, which was no doubt influenced by group composition. Both groups dealt with partly overlapping themes, but came to different conclusions. DG2 very much continued the neoliberal discourse on 'sustainable finance' that was dominant over the past decade, putting much emphasis on private sector action that the state should merely incentivize. DG1 continued to have large elements of it in their suggestions, but added much more state intervention to it.

Illustrative for such discrepancies is the issue of credit rating agencies. The related reform suggested by DG2 is: "Credit rating agency regulators, with the agreements of the agencies themselves, should devise common guidelines to progressively incorporate longer-term SDG-aligned, social and environmental indicators into agency ratings …."[5] DG1 in turn suggested, "Creation of publicly owned credit rating agencies, so that agencies are not both market evaluators and market players as at present."[6] The first is essentially a suggestion for public-private partnerships along a soft-law suggestion. The second would replace or at least complement private sector institutions in a strategic area through public sector institutions – expanding the state's role and taking back democratic control of that area.

The remaining part of this briefing paper picks some of the policy suggestions from the 'Menu of Options', analyses and evaluates them. Additional literature or data sources have been used where it makes sense to explain the rationale of the option explained.

As the "FfD in the era of COVID-19" process itself did not lead to any agreed decision, the implementation of the options depends on future actions by policy- and decision-makers, either within the UN context, or in other multilateral bodies such as the IMF or the MDBs, or on country-level in UN Member States.

It is helpful in this regard that Munir Akram, Pakistan's Ambassador at the UN and the current chair of the UN's Economic and Social Council (ECOSOC), already stressed the intention to let this process inform the regular Financing for Development process at the UN, and the forthcoming Economic and Social Council (ECOSOC) Financing for Development Forum, which is scheduled to take place on 12–15 April 2021.

However, many options would need to be implemented by the International Finance Institutions (IFIs), where voting procedures build on the 'one dollar-one vote' approach and majorities are different than at the UN where each state's vote counts equally.

5 Menu of Options, p. 37.
6 Menu of Options, p. 15.

Option 1: Issuing and redistributing Special Drawing Rights

The UN suggested early on that Special Drawing Rights (SDRs) could play a role in the financing response: When UNCTAD estimated the external financing needs of developing countries at US$ 2.5 trillion in Spring 2020, they suggested that US$ 1 trillion of those could be mobilized through a new issuance of SDRs.[7]

There is historical precedence for using SDRs in times of crisis. They played a key role in managing the fallout of the global financial crisis a decade ago. In 2009, the IMF made SDRs worth US$ 250 billion available in a special allocation.[8]

SDRs are a global reserve asset issued by the IMF. Member States that receive them can swap them against hard currency such as the US Dollar or the Euro. In doing so, they gain new liquidity, which they can use to finance expenses in foreign currency, such as imports of goods and services, or also debt service on external debt. They are widely seen as the fastest and most effective way to make huge amounts of financing available to a large number of countries.

Issuing SDRs essentially means creating fresh money, a policy option currently used at ultra-large scale by the central banks of the major economic powers. But while these create money mainly for their own nation's benefit (the European Central Bank for the whole Euro zone), SDRs are distributed among all IMF Member States, according to their IMF quota. If the IMF issued SDRs worth US$ 500 billion, about US$ 200 billion of those would go to developing countries. Economists supporting the proposal explain: "a new SDR issuance is the only case in which these (developing) countries share in the 'seignorage' of creating international money."[9]

The universal distribution is, however, also a disadvantage, as the lion's share goes to richer countries that actually do not need them. The new issuance should therefore come with an additional commitment by richer countries to distribute their share among developing countries.

Key advantages of SDR issuance over alternative provisions of hard-currency liquidity – say an IMF or World Bank loan – is that it does not come with the onerous policy conditions that these institutions would usually impose, and that the transaction costs are very low. Some critics argue that issuing SDRs could create inflation, but IMF-commissioned research found this is unlikely to happen. A key advantage of SDRs is that they are not debt – they don't need to be repaid and do not increase heavily indebted countries' debt distress further.[10]

There are also alternative uses for the SDRs, as well as disbursing them to countries directly. For instance, they could also fund the World Bank's concessional lending facility for low-income countries, the International Development Association (IDA), which is usually funded and regularly replenished directly by Member States. It is now facing a funding gap of US$ 25 billion for the coming years, as it frontloaded disbursements in 2020. Using SDRs that way means that spending could be better targeted to specific countries and sectors, but it also means having policy conditions and politically determined allocations back. A second option is to use SDRs to finance multilateral debt relief, for instance by filling up the IMF's CCRT facility, and creating a similar trust fund at the World Bank.[11]

Even without a new issuance of SDRs, the instrument can play a role: At the end of 2019, the advanced economies held 126 billion unused SDRs idle at the IMF, worth US$ 177 billion. This is more than all the OECD Development Assistance Committee (DAC) donors together provide as ODA in a year. Rich countries could unilaterally decide to use them for the purposes above. Canada has already allowed the IMF to use their SDRs, as announced by Managing Director Georgieva at the September High-Level Meeting.

Political Feasibility: The IMF can issue new SDRs when Member States representing 85% of IMF voting rights agree to it. The vast majority of IMF Member States claim to do so, including the "major shareholders" from Europe such as Germany and France. The USA as de facto veto power at the IMF has, however, not yet supported the new issuance. The change of government in the USA

7 https://unctad.org/news/un-calls-25-trillion-coronavirus-crisis-package-developing-countries
8 https://www.imf.org/en/News/Articles/2015/09/14/01/49/pr09283
9 https://www.brookings.edu/blog/future-development/2020/03/26/imf-special-drawing-rights-a-key-tool-for-attacking-a-covid-19-financial-fallout-in-developing-countries/
10 https://cepr.net/report/the-world-economy-needs-a-stimulus-imf-special-drawing-rights-are-critical-to-containing-the-pandemic-and-boosting-the-world-economy/
11 https://www.theglobalist.com/coronavirus-covid19-pandemic-debt-relief-imf-world-bank-sdrs-ccrt/

in early 2021 could change this. An SDR issuance larger than US$ 649 billion needs approval by the US Congress, not just by the government, which might complicate and in any case delay the process.[12] Thus, a somewhat smaller allocation could be quickly agreed. The fact that SDR issuance has successfully been used in the 2009 crisis response is a strong argument for using it again. Once the decision has been made, the option can easily be implemented.

Each Member State can decide unilaterally what to do with its SDRs that lie idle at the IMF. More countries can follow the example of Canada and others, and redistribute their SDRs.

Option 2: Creating fiscal space through debt relief

Even before the COVID-19 crisis hit, debt levels had reached record highs. CSOs as well as the UN have argued that rising debt service costs reduce the fiscal space of developing country governments: each dollar that is transferred to creditors is a dollar not spent on health services or sustainable development. Just the 68 low-income countries for which reliable debt data is available currently transfer about US$ 40 billion annually in debt service to their creditors.[13] For heavily indebted middle-income countries, the figure is naturally much higher. Moreover, debt sustainability assessments that have been made before the crisis hit are no longer valid, as the economic recession has substantially reduced borrowers' payment capacity.

Debt moratoriums

Action on debt has been on the agenda of the international community since the beginning of the crisis. But the economic powers of the G20 merely offered a debt moratorium – the Debt Service Suspension Initiative (DSSI) agreed in April 2020 – and they offered it only to low-income countries and least-developed countries. The shortcomings of the DSSI include that it covers only bilateral loans, which constituted a shrinking share of the debt stock and of debt service costs. The duration was initially limited to the end of 2020, and it was of no use for heavily indebted middle-income countries, of which there are many. Extending the DSSI to more creditors, or to more indebted countries, or to 2021 and beyond, was therefore one set of options discussed by the UN.[14]

Most importantly, however, the DSSI does not actually constitute debt relief. It is just a moratorium that has been designed in a 'net present value neutral' way, meaning that debtors need to make all the payments later that they do not make now. Given that, it provides some breathing space, but it does not actually solve the solvency problems of overindebted countries. It is just kicking the can down the road. Only actual debt relief can restore solvency in countries where it is no longer given.

Debt relief through debt swaps

Debt relief was suggested in two forms: Either as largely unconditional debt cancellation, or as debt swaps. In the case of debt swaps, the indebted country commits to spending freed up resources on a certain purpose, which might be health services, climate change measures, nature conservation or sustainable development in general. Debt-to-SDG swaps came up during the debates as well as debt-to-climate-adaptation swaps. These build on a proposal that has been developed by the UN's Regional Economic Commission for Latin America and the Caribbean (ECLAC) already before the COVID crisis.[15]

Small Islands Developing States (SIDS) in the Caribbean have been simultaneously hit by debt crises and climate crises for quite some time now. Debt-to-climate swaps try to address both crises at once. The COVID-19 crisis makes support for SIDS even more urgent as the collapse of tourism, trade and remittances has been an additional shock. SIDS governments were also among the strongest advocates for actions on debt during the UN process. Debt swaps assume that there is some payment capacity in indebted countries, and that payment streams should rather be diverted to more urgent/important purposes than debt service.

Debt relief through debt cancellation

An actual debt cancellation is usually the preference of indebted countries as it creates actual fiscal space. In some cases, when the debtor is actually bankrupt and has lost the ability to pay, it is the only viable option on debt. Solvency is more difficult to assess

12 https://som.yale.edu/blog/the-g20-s-impasse-on-special-drawing-rights-sdrs
13 https://www.eurodad.org/g20_dssi_shadow_report
14 Menu of Options, p. 85-87.
15 https://www.cepal.org/sites/default/files/news/files/nydbtreliefcaribbeannovember2017.pdf

when it comes to sovereign debtors than when it comes to e.g. private firms, as states have both 'assets' and 'liabilities' that cannot be expressed in monetary values, or simply sold.

CSOs argue that a state should already be obliged to cease payments to creditors when it runs out of the funds needed to fulfil its human rights obligations to its citizens – including ensuring an adequate level of social protection and health and education services. This view is also reflected in the UN Guiding Principles on External Debt and Human Rights. The IMF and World Bank in turn define debt sustainability more from the perspective of default risk.[16] No matter which interpretation is used, some debtors can no longer pay and – despite the moratorium on bilateral debt offered by the G20 – some have already entered into negotiations on debt relief with their creditors.

A key problem is that effective institutions that could govern a speedy and comprehensive debt workout do not exist – a gaping hole in the international financial architecture. Debtors that have a complex debt portfolio comprising debts owed to a myriad of different bilateral, multilateral and private creditors would have to enter into a myriad of parallel negotiation processes with these creditors. This causes delays, and may lead to unfair and insufficient outcomes when one creditor writes off more than the other, or some creditors do not participate at all (the so-called too little – too late problem). The more reluctant 'free-riders' so far in this crisis have been private creditors and multilateral creditors, but also bilateral creditors still need to make the step from moratorium to relief.

Bilateral Debt: Bilateral debt can be cancelled by a simple political decision of the creditor(s), which makes it look relatively easy to achieve. There is abundant historical precedence for bilateral debt relief: the actions taken by the Paris Club, and the multi-country Heavily Indebted Poor Countries (HIPC) Initiatives. No surprise that the option to launch "a new HIPC" was promoted during the UN dialogues.[17]

Multilateral Debt: Multilateral debt is difficult to cancel as much funding from MDBs as well as the IMF is revolving, i.e. new loans are funded by repayments of old loans. Moreover, the World Bank argued during the debates that debt relief might put their AAA credit rating at stake, which would lift their financing costs on capital markets. There is precedence, however: The Multilateral Debt Relief Initiative set up in 2005 to cancel World Bank and other MDB loans. The IMF can cancel loans when the operation is refinanced through a Trust Fund – the Catastrophe Containment and Relief Trust (CCRT). Due to donor support, the CCRT has already funded some debt service relief for 28 countries by October 2020.[18] One option stressed was to set up similar trust funds at the World Bank and other MDBs. However, the trust fund approach would not be a net gain for developing countries, because it absorbs ODA that can no longer be used elsewhere. Additional options include that trust funds could be filled with earnings from selling a share of the IMF gold reserves,[19] or that new or idle SDRs could be used.

Private debt: Ensuring private creditor participation is a central objective of the UN process, which is why a dedicated discussion group (DG5) dealt exclusively with "private sector creditor engagement". UN Member States such as Germany, as well as international organizations such as the World Bank, explicitly demanded their participation during the policy dialogues at the UN. This for good reasons: the fresh resources that the World Bank provides and the debt standstill through the DSSI provide indebted countries with the necessary cash to continue paying private creditors – but using it for this purpose undermines the idea to create fiscal space for a COVID-response. The global network of the finance industry, the Institute of International Finance (IIF) has developed a term sheet to guide private creditors' participation in the G20 debt initiative (DSSI), but so far the call for voluntarily participation of private creditors has yielded no results at all.

Unfortunately, the policy options to enforce private creditor participation are limited. Debt buybacks – where taxpayers' money is used to buy privately held debts (at a discount price) on secondary markets – have been mentioned as a fallback option. Because the COVID-19 crisis can be considered an

16 Cf for this discussion: https://www.eurodad.org/the_evolving_nature_of_developing_country_debt_and_solutions_for_change

17 In November 2020, the G20 announced a "Common Framework" to make debt treatments beyond DSSI possible, but this fell way short of a new HIPC, especially because the framework aims to avoid actual debt write-offs.

18 In October 2020, the IMF announced an extension: Relief could be provided for debt service falling due until April 2021: https://www.imf.org/en/News/Articles/2020/10/30/pr20328-mali-imf-executive-board-extends-immediate-debt-service-relief-for-another-six-months

19 https://jubileedebt.org.uk/press-release/imf-gold

unforeseen event beyond either parties' control, debtor countries could also invoke the legal doctrine of "necessity" and/or make use of force majeure clauses in bond contracts, where they exist. This should help to restructure private debt in a legally sound way. However, it is unpredictable if all courts worldwide follow this view. Creditor litigation against sovereign debtors has been a major problem for speedy and sustainable debt restructurings in recent years.[20]

One of the few international law options to enforce private creditor participation is to shield an indebted country through a UN Security Council Resolution – an option that was used to make debt relief for Iraq possible in 2003. Doing so makes enforcement of creditor claims through the courts temporarily impossible if the debtor country stops paying.[21] Generally, the Paris Club creditors expect comparability of treatment by countries that seek bilateral debt relief, meaning that the debtor should request similar relief from all other creditors. However, in practice not all creditors easily agree to that.

Debt architecture reforms

The difficulty in ensuring private creditor participation is a key reason why more fundamental reforms of the debt architecture are needed. The UN's menu of options suggests two options. The first is to create a Sovereign Debt Forum, which would provide a platform for discussions between debtors and creditors for actions on debt. The second is the slightly more ambitious one to create a Sovereign Debt Authority, which would provide expert advice to debtors, but could also do the conceptual groundwork to create a real sovereign debt workout mechanism.[22]

Political feasibility: The question of how to solve debt crises has been a major focus of the UN debates. Developing country governments and UN negotiating groups such as those of the Small Island Development States (SIDS) and the African Union (AU) demanded this topic in almost every intervention made at the High-Level Events. G20 countries had offered the DSSI early. The DSSI is the first debt-initiative for the benefit of a larger country group for 15 years, which proves that the COVID-19 crisis created a conducive environment. The pressure on the holdout creditors is high: Several governments, as well as the Managing Directors of the IMF and World Bank, have pushed for private creditor participation. Influential powers such as China pushed for World Bank participation. Some donors have channeled ODA grants to the CCRT to enable IMF debt service relief. This time of crisis certainly provides better political momentum for debt relief than at any other point in the past 15 years. In November 2020, the G20 decided to extend the DSSI to June 2021, and agreed on a "Common Framework" for debt relief beyond the DSSI, but in practice this framework added little value.[23] A key challenge for comprehensive debt restructurings remains the limited power of governmental decisions over private debt in the absence of an international insolvency law, or a sovereign debt workout mechanism.

It should also be noted that an indebted country can always unilaterally suspend debt payments and request debt relief from creditors, or even repudiate those debts fully. But this procedure might lead to lawsuits by private creditors, or to sanctions by official creditors.

Option 3: Raising taxes

While raising taxes seems the most obvious way of creating more fiscal space, the topic of fair and effective taxation has not been a central topic of the recent UN process, perhaps because the focus was very much on mobilizing external finance. However, there is an external dimension to tax, when capital flight or harmful tax competition leads to tax dodging. Consequently, tax matters have mostly been discussed in the context of illicit financial flows (DG6), much of which are due to tax dodging, but also in in the context of growth and jobs (DG1).

While not very prominent here, taxation was, however, high on the agenda elsewhere: Parallel to the FfD policy dialogue, the UN's High Level Panel on International Financial Accountability, Transparency and Integrity for Achieving the 2030 Agenda (FACTI Panel) was debating illicit financial flows (IFFs) at the UN.[24] The UN Conference on Trade and Development (UNCTAD) did substantial policy work and research on it for their Eco-

20 https://voxeu.org/article/how-creditor-lawsuits-are-reshaping-sovereign-debt-markets
21 UN Security Council Resolution 1483 http://unscr.com/en/resolutions/doc/1483; see also https://fas.org/sgp/crs/mideast/RL33376.pdf
22 Menu of Options, p. 95-96.
23 https://jubileedebt.org.uk/press-release/reaction-to-g20-common-framework-for-debt-treatments
24 https://www.factipanel.org/

nomic Development in Africa Report 2020.[25] Last but not least, the OECD continued negotiations on minimum taxes for corporations to pay in all the countries in which they operate and new rules for taxing the digital economy.[26] The latter does not properly address the needs of developing countries, most of which are non-OECD members, which is why the request from the global south for a fully inclusive international tax architecture has been high on the UN's agenda.

UN Tax Convention

The most far-reaching option was put forward by DG6, a UN Tax Convention established by a UN General Assembly negotiation. The rationale is, according to the UN's options paper: "It is time to back a truly universal, intergovernmental process at the UN to comprehensively address tax havens, tax abuse by multinational corporations and other illicit financial flows that obstruct redistribution and drain resources that are crucial to challenging inequalities, particularly gender inequality."[27] The call for a UN Tax Convention seems owed to the fact that there are so many flaws and gaps in the area of cross-border tax matters that the first step to take is to create a space in which they can be addressed in a comprehensive and continuous manner. Adding a Tax Convention to the UN system could also ensure that taxation works to support other agreements under the UN, such as the international human rights framework or the Paris Climate Treaty.[28] A UN Tax Convention would be a first step towards addressing the multiple forms of tax dodging. According to the FACTI Panel's Interim Report, just the profit shifting of multinational corporations to low tax jurisdictions causes a loss of US$ 500 billion in corporate tax revenue every year. And private wealth worth US$ 7 trillion is hidden in tax havens, largely untaxed, and often of criminal origins.[29]

Progressive taxation

When it comes to the type of taxes, several DGs referred to the need for progressive taxation. The financial transaction tax (FTT) had a brief revival in DG1, where it was seen as a potential source of funding for social protection – together with digital taxes.[30] DG1 and 2 also suggested using fiscal policies for green transition. They called for environmental taxes, mainly carbon taxation, and phasing out fossil fuel subsidies.[31]

Several options suggested in the UN's menu propose, however, to reduce tax revenue. Especially DG1 and 2 also advocated the use of tax incentives, for example, to promote environmental, social and corporate governance (ESG) investments, to revive remittances, or to help formalize the economy. Also suggested was for governments to conduct fiscal incidence analysis in public finance systems, so that the redistributive impact of taxes is better understood.

Political feasibility: Designing tax systems is largely a sovereign national affair, so it does not require any multilateral agreement. Many countries have, however, signed bi- or multilateral tax, trade or investment treaties that restrict their policy space. Moreover, different tax rates between countries might lead to capital flight or reallocation of economic activities and even people, which is why some degree of international agreement on tax harmonization is needed. The OECD and the EU have tried to achieve such an agreement in recent years, but to little effect. Strengthening the UN's role in tax matters has been on the agenda for quite some time and enjoys the support of the G77 (representing 134 Member States of the global south), but lacked endorsement by most of the major powers of the global north. A UN Tax Convention would need to be adopted by the UN General Assembly, but not necessarily by unanimous consensus. In order to have a legal standing, a pre-specified number of countries have to ratify the Convention on national level.

Option 4: New multilateral financing facilities

One of the key challenges that often featured during the UN debates is developing countries' dependence on external finance, and the extremely high financing costs that come along with that. This challenge has become even more severe during the ongoing crisis. Most developing countries

25 https://unctad.org/webflyer/economic-development-africa-report-2020
26 https://www.oecd.org/tax/beps/international-community-renews-commitment-to-address-tax-challenges-from-digitalisation-of-the-economy.htm
27 Menu of Options, p. 124.
28 Ibid.
29 https://uploads-ssl.webflow.com/5e0bd9edab846816e263d633/5f7f44f76cf2f11732c2b5f0_FACTI_Interim_Report_final_rev.pdf; p. V
30 Menu of Options, p. 29.
31 Menu of Options, p. 35.

can now borrow from private creditors through financial markets, but at prohibitively high interest rates. The representative of the UN Economic Commission for Africa, Vera Songwe, stressed at the September High Level Event (HLE) that "there must be some equity between developed and developing countries in accessing the trillions [of private finance] we are talking about." While a country like Germany borrows at 0% or even negative interest rates, and borrowing costs dropped since the beginning of the crisis, larger countries in Africa are being penalized by financial markets. They pay prohibitively high interest rates, which have even increased since the beginning of the crisis, from 8% to 9% in South Africa, and to a staggering 15% in Egypt.[32] Bilateral and multilateral development banks provide concessional loans at better terms. But their volume is limited – not all countries have access to them, and they come with a high non-pecuniary price in terms of ceasing national sovereignty to foreign policy conditions and foreign funding priorities.

The UN has stressed early that the COVID-19 crisis would require a new Marshall Plan. Of the US$ 2.5 trillion in external financing that developing countries need to cope with the crisis, US$ 500 billion should come from official development assistance. The UNCTAD argued that rich countries have accumulated a huge delivery gap, as they failed to meet the 0.7% target for ODA over several decades.[33] The argument was also backed by CSOs. Oxfam, for example, argued in a recent report entitled "50 years of broken promises" that the non-paid ODA has added up to US$ 5.7 trillion over the past 50 years, or US$ 114 billion annually.[34] Official OECD-DAC figures for 2019 are that ODA accounted for US$ 152.8 billion, or 0.30% of DAC members' GNI.[35] Meeting the 0.7% target would deliver US$ 204 billion more.

Concessional financing facilities already exist, of course. The most prominent is probably the World Bank's International Development Association (IDA) Facility, and the credit facilities of the IMF's Poverty Reduction and Growth Trust (PRGT). But the crisis has revealed that neither scale nor scope of existing facilities is up to the task, which is why a large number of new facilities were proposed.[36]

Fund to Alleviate COVID-Economics

Perhaps the boldest suggestion is the Fund to Alleviate COVID-Economics (FACE), an outcome of the DG3 discussions: This a huge facility for low- and middle-income countries, but also high-income countries in debt distress, which should provide funding to the tune of 3% of GNI of eligible countries, or a total of US$ 516 billion.[37] Lending from the FACE facility would be extremely long-term: provided for 50 years, with five years grace period, and a 0% interest rate, or an interest rate fixed at the current LIBOR-rate, which is around 0.7%. On the funding side, the capital would be provided by the "world's richest economies" and would amount to 0.74% of their GDP. FACE loans would have no policy conditions attached, but should come with a commitment to be used for SDG-related purposed, and with requirements for good governance and fighting corruption.

Liquidity and Sustainability Facility (LSF)

The objective of this yet-to-be established Liquidity and Sustainability Facility (LSF) is to provide fresh liquidity and ensure lower borrowing costs for developing countries, especially for frontier markets whose access to financial markets in times of crisis is shaky. At the UN debates, the UN Economic Commission for Africa in particular was keen to see this facility enter operations. The facility would be funded by central banks that possess hard currency. It is essentially a special purpose vehicle where private lenders could swap developing country bonds against bonds with longer-maturity, and lower coupons. The LSF would create new liquidity and lower borrowing costs for developing countries. Private investors have the advantage that they receive liquid and higher (probably AAA-rated) bonds for the high-risk and high-yield assets that they swap.[38]

32 Cf. the statement at the HLE by Vera Songwe, UNECA: https://www.un.org/en/coronavirus/financing-development/heads-of-state-and-government-meeting (time 3:20:00).

33 https://unctad.org/news/un-calls-25-trillion-coronavirus-crisis-package-developing-countries

34 https://www.oxfam.org/en/press-releases/poor-countries-denied-57-trillion-aid-because-rich-countries-50-year-failure-deliver

35 https://www.oecd.org/dac/financing-sustainable-development/development-finance-data/ODA-2019-detailed-summary.pdf

36 Additional innovative financing facilities that were suggested during the UN debates include a fund to support public procurement of food and healthcare products (by Venezuela), a UN Infrastructure Fund (by Pakistan) and a trust fund for assistance to tourism-dependent states (by the Maldives).

37 Menu of Options, p. 54.

38 Cf. https://www.businesslive.co.za/bd/world/africa/2020-04-28-africa-considers-own-brady-plan-as-debt-relief-proposal/

Resilience Funds

This fund was strongly supported by the UN Economic Commission for Latin America and the Caribbean. Caribbean SIDS in particular have been hard hit by the COVID-19 crisis, as their economies strongly depend on trade and tourism. Beyond the current crisis, climate change and the natural disasters (hurricanes) that come along are causing severe damages. At the same time, most Caribbean countries are middle- or even high-income countries. This means they are not eligible to receive highly concessional loans from e.g. the International Development Association (IDA). Regional Resilience Funds would be the primary vehicle for financing climate change adaptation and other resilience building measures. They would be funded by external support from international financial institutions and donors, but also domestic resources freed up through, for example, debt-to-climate swaps.

Global Fund for Social Protection

The COVID-19 crisis has raised awareness about the importance of universal access to social protection. According to the International Labour Organization (ILO), currently only 27% of the world population enjoys an adequate level of social protection.[39] The funding gap for social protection floors in all developing countries is estimated at US$ 1.2 trillion in this year, but only US$ 76 billion is needed for all low-income countries (LICs) that cannot close the gap with domestic resources.

Currently, only a tiny fraction of ODA goes to social protection, amounting to 0.0047 of DAC donors' GNI. International human rights law states that rich countries have a duty to support the achievement of human rights in poorer countries. Therefore, the idea for a Global Fund for Social Protection was fed into the debate by two independent UN human rights experts in 2012.[40] It had been rediscovered by DG1 in the current UN process, which put forward the proposal to "Consider a multilateral framework on universal social protection financed through global FTT and digital tax." The International Trade Union Confederation backs the idea to finance the Global Fund through financial transaction taxes (FTTs), currency taxes, wealth taxes and a general crack-down on tax dodging.[41]

Political Feasibility: Setting up a new financing facility is not necessarily difficult to achieve politically, although many governments and other stakeholders are opposing a further proliferation of funds and facilities, as the 'aid architecture' is already complex and fragmented. The politically challenging aspect is to fuel new funds and facilities with sufficient capital so that they can provide grants or highly concessional loans. If money is simply reallocated from other purposes, the new facilities would undermine ongoing international cooperation in the sectors or areas where funding is withdrawn.

Thus, additional financing facilities only make sense if there is additional funding. If these are fiscal resources coming from richer countries, these would need to pass supplementary budgets, in most cases with parliamentary approval. This takes time and is politically challenging, as the crisis has caused revenue shortfalls and unexpected expenses in all countries, competition for scarce resources is high. While rich countries spend vast sums on countercyclical crisis response at home, so far few of them have announced that they will make additional money for third countries available. Germany and Canada are notable exceptions. Germany provides €1.5 billion extra in 2020 and the same sum in 2021 through a supplementary budget,[42] Canada has announced CAD$400 million in additional aid.[43] A reasonable alternative is to use innovative financing for new facilities, for example, revenue from new taxes (such as financial transaction taxes, carbon taxes, digital taxes), or monetary instruments from the IMF, such as SDRs, or national central banks.

Option 5: Redirecting private finance

The enormous accumulation of wealth in some private hands after decades of neoliberalism has also raised interesting questions about how these trillions could be used to finance sustainable development. Institutional investors currently have more than US$ 200 trillion under management.[44] In particular, DG1 and DG2 explored options concerning how to redirect some of this money to finance a

39 https://www.ilo.org/global/topics/social-security/lang--en/index.htm
40 https://www.ilo.org/global/about-the-ilo/newsroom/news/WCMS_759106/lang--en/index.htm
41 https://www.ituc-csi.org/IMG/pdf/ituc_campaign_brief_-_a_global_social_protection_fund_en.pdf
42 https://www.dw.com/en/bundestag-to-talk-coronavirus-aid-to-impoverished-countries/a-53865705 https://donortracker.org/country/germany
43 https://www.theglobeandmail.com/politics/article-trudeau-pledges-an-additional-400-million-in-humanitarian-aid-to/
44 Menu of Options, p. 13.

sustainable recovery, and to align investments better with the SDGs and the targets of the Paris Climate Agreement.

Despite the crisis, there has already been a boom in ESG-investment. Public borrowers try to capitalise on investor appetite for SDG investments by issuing social bonds or green bonds, for example, the EU through the SURE social bonds,[45] but also the African Development Bank or the World Bank.[46]

However, the boom is also due to the fact that criteria for what counts as ESG investment are not quite clear, or not very strict. Many different sets of standards compete with each other, which creates ample space for abuse and 'green washing' or 'social washing' by private investors. The menu suggests therefore developing "comparable frameworks for alignment of both public and private finance with the SDGs and the Paris Agreement". This would include better harmonized taxonomies, similar to the EU's new green taxonomy adopted in June 2020,[47] and a global set of standards for climate-related financial disclosures and other ESG factors. Such standards would make it easier for market participants to identify actual sustainable investment opportunities.

DG1 suggested that the governments could be more proactive in pushing for SDG alignment than just through standard setting, e.g. by making the ESG and SDG performance of private companies a requisite in public procurement processes. As the size of the global government procurement market accounts, according to World Bank, for roughly 12% of global GDP, or US$ 11 trillion, this could have an enormous impact on transformation towards sustainable business models in the private sector.[48]

Little has been proposed in the area of due diligence: DG1 called on UN Member States to participate in the ongoing negotiations on a Binding Treaty for Business and Human Rights and recommended supporting local enterprises that strive to incorporate ESG approaches and SDG impacts in their business models.[49]

Political feasibility: Private wealth is available in large amounts, but the options presented for its redistribution are tentative, and likely to reallocate only smaller shares of investment. Moreover, as private investors seek profits, there is a question of sustainability: Over the investment cycle they are likely to withdraw higher amounts from developing countries than they have invested in them in the first place. There has been a boom in national, regional and global initiatives on 'sustainable finance' in recent years, which led to a proliferation of different standards. The EU delivered a green taxonomy in June 2020, which has been a step forward, but has yet to deliver a social taxonomy. Delivering a global standard would require leadership by a global institution. The slow progress towards a UN Binding Treaty on Business and Human Rights indicates that severe political obstacles continue to block effective regulation of private sector activities for sustainability. Incorporating social or environmental criteria in public procurement is possible, e.g. under the EU procurement directive,[50] but in some cases free trade agreements restrict policy space.

Conclusion

The UN process for "Financing for Development in the Era of COVID-19 and Beyond" resulted in a rich selection of policy options. As such, the process has been fruitful. It has strengthened the role of the UN as a forum to foster discussions about the reform of the global financial architecture. The fact that Member States chose in which of the Discussion Groups to participate created a constructive atmosphere that very few tried to obstruct. In particular, Member States that are not well represented – or not represented at all – on other bodies of global economic governance made use of the opportunities. Remarkable, for example, was the strong involvement of governments of small island development states. The UN's Regional Commissions as well as UNCTAD and the UN Department of Economic and Social Affairs (DESA) have proven that they are able to provide significant research and policy support to global policy-making on financial policy and financial architecture reform.

45 https://ec.europa.eu/commission/presscorner/detail/en/qanda_20_1809
46 Menu of Options, p. 14.
47 https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32020R0852&from=EN
48 https://blogs.worldbank.org/developmenttalk/how-large-public-procurement
49 Menu of Options, p. 29.
50 https://ec.europa.eu/environment/gpp/eu_public_directives_en.htm

However, the menu of options presented to Heads of State at the High-Level Event in September 2020 has so far not led to any new policy or institutional innovation in policy-making at the global level. The drivers of the process deliberately avoided requesting adoption by consensus so that the different parties' particular views appear more or less in their entirety in the menu of options, through aggregation. Any attempt to build consensus under the given time constraints would have predictably led to substantial deletions, especially under the difficulties of negotiating via video conference.

The approach to simply aggregate the proposals of different stakeholders, however, also has the downsides that the UN's menu includes options that are partly contradictory. Also problematic is that the complexity of the menu was likely one key reason why no decision at all had been made when Finance Ministers and eventually the Heads of States convened in September. Presenting a reduced and prioritized set of options probably has higher chances for real implementation.

What could the way forward look like?

1. Firstly, to create a major decision-making moment at the highest political level at the UN. The aim should be to actually raise external finance for countries hit hardest by the COVID-19 crisis, but also to set reforms of the international financial architecture towards more resilience and better crisis response in motion. In this regard, some stakeholders suggested the UN should hold a major UN Economic Reconstruction and Economic Reform Summit. The preparations for such a Summit should start immediately, with the aim to hold the actual summit in 2021.

2. Secondly, to keep a process alive at the UN where policy dialogue can continue to take place. Concerning this proposal, it would be advisable for the UN to keep the Discussion Groups alive. Their topics could be adapted over time – according to changing needs.

3. The procedural steps mentioned above would complement the existing infrastructure that the UN already offers: Especially the ECOSOC Forum on Financing for Development that takes place annually in April should be better used as a decision-making space for pertinent FfD matters. The already existing Inter-Agency Task Force on Financing for Development could help to elaborate some of the policy concepts of the menu of options further.

The selection of policy options presented in this paper has enormous potential to mobilize new resources for development, to free up resources for development that are tied up elsewhere, or to redirect resources from less to more useful purposes. In tandem, the UN and its Member States should work on cross-cutting issues such as thoroughly embedding financing for development in the human rights framework, and strengthening the links to the UN Climate Action Agenda and the 2030 Agenda for Sustainable Development as such. Work on reforming the international financial architecture is also important, making it fit for the tasks of the present and the future. This reform has made little progress over the past few decades, meaning that governance gaps have become wider and the world has become more vulnerable to crises such as the one that we are currently witnessing.

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An analysis and assessment of innovative policy options

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