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Development Finance: Beyond Budgetary "Official Development Assistance"

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DEVELOPMENT FINANCE: BEYOND BUDGETARY “OFFICIAL DEVELOPMENT ASSISTANCE”

*Anthony Clunies-Ross**

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I. INTRODUCTION

Budgetary appropriations by rich-country governments constitute the standard method of providing external funds for welfare and growth in developing countries. This source seems likely, however, to prove inadequate to meet the estimated external finance needed to contribute to the achievement of the Millennium Development Goals.

Yet there are other possibilities that may require less politically difficult, or less costly, or even—rationally-considered—self-interested, cooperation from rich-country governments, and yet could put significant additional funds into the hands of poor households, developing-country governments, or global development intermediaries.

For those who regard it as urgent that more of these funds should become available, an appropriate strategy is to campaign and argue for

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the activation of those methods that currently present the softest political targets. Particular sources of finance might be judged as soft targets on the ground that there are no coherent and legitimate interests ranged against them. The task facing their proponents would then be to work for the removal of the remaining obstacles of inertia, lack of imagination, ignorance, or prejudice that put otherwise promising methods out of reach.

Among the devices with these characteristics that would put extra resources into the hands of developing-country governments, or of many of their poor households or local communities, are: various forms of international tax cooperation to reduce avoidance, evasion, and competitive tax-degradation; the resumption of regular allocations of Special Drawing Rights (SDR) from the International Monetary Fund (IMF); and the creation by a global institution of an SDR-denominated bond, granted certain immunities, and designed especially for preserving the assets of poor migrant workers and their families and communities.

Among the intrinsically most promising ways of increasing the resources available to international organizations for use on behalf of the world community are: recycling for world-development purposes of SDRs that have no net value to the countries initially receiving them; and internationally-coordinated taxes on world resources, activities, or externalities, in particular a tax on currency transactions, which could now be instituted effectively at small cost through the cooperation of a handful of governments, but is hampered by prejudice and also by lack of precise enough knowledge of the effects of the tax at various rates on its base.

II. THE MID-CENTURY VISION OF GLOBAL RESPONSIBILITY

After the end of the Second World War, the idea of mutual responsibility across the world came to take novel forms. Official rhetoric, and the underlying thinking of many people concerned about world affairs, implicitly supposed a general responsibility for the material conditions of human life everywhere. Because it was clear that what many considered intolerable could nevertheless not be remedied at once, the objective of "development" came to be accepted as a matter of course. And much world opinion regarded governments—including the governments of the relatively rich countries—as having a vital role to play in bringing the desired changes about.

There have been plenty of occasions for disappointment and cynicism that between them provided abundant pretext for "the easy

speeches that comfort cruel men:"¹ failings by both rich-country and poor-country governments; misapprehensions recognized too late about the nature and possibilities of "development;" and dogmatic ideologies that directed attention away from what was actually happening. Yet the vision dramatized and activated in the late 1940s and early 1950s by the Marshall Plan and President Truman's "Point Four" persisted through the changing scenes of the second half of the century.

III. THE SEARCH FOR ADDITIONAL SOURCES OF "DEVELOPMENT FINANCE"

Around the turn of the millennium, the United Nations (UN) directed the world's attention to the need for additional outside finance to be made available by or for the people of developing countries if reasonable interim welfare goals were to be met. The declaration by the UN General Assembly in the year 2000 of the Millennium Development Goals, mostly to be met by 2015;² the report of the Zedillo High-Level Panel in mid-2001;³ and the Financing for Development process, undertaken by the UN, the IMF, and the World Bank, and culminating in the Monterrey meeting of March 2002⁴; these, with their attendant studies, have served to fix a figure of about \$50–60 billion a year in external finance as what is minimally necessary. This is on top of the extra effort toward improving health, education, water supply, sanitation, and other welfare components, that can be generated within developing countries (generally considered in the projections to be greater in value than the additional outside assistance). This annual amount of \$50–60 billion is roughly equal to the current annual rate of Official Development Assistance (ODA),⁵ bilateral and multilateral, so that what is required is an approximate doubling of ODA.

Why the realization and enhanced sense of urgency (at least on paper) now? We may speculate. Possibly a factor has been the realization

1. G.K. Chesterton, *The Hymn*, in *THE COLLECTED POEMS OF G. K. CHESTERTON* 146, 147 (5th ed. 1936).

2. U.N. GAOR, 55th Sess., 8th plen. mtg., U.N. Doc. A/55/PV.8 (2000). For a listing of the Goals with explanatory material, see, SHANTAYANAN DEVARAJAN, ET AL., *GOALS FOR DEVELOPMENT: HISTORY, PROSPECTS AND COSTS* 34–35 (World Bank Research, Working Paper No. 2819, 2002).

3. *High-level International Intergovernmental Consideration of Financing for Development: Report of the Secretary-General*, U.N. GAOR, 55th Sess., Agenda Item 101, at 19–22, 49–51, U.N. Doc. A/55/1000 (2001) [hereinafter *2001 Report of the Secretary-General*].

4. See Abdel Hamid Bouab, *Financing for Development: The Monterrey Consensus: Achievements and Prospects*, 26 MICH. J. INT'L L 377 (2005).

5. *2001 Report of the Secretary-General*, *supra* note 3, at 54.

that the devastation caused by the AIDS epidemic, especially in Sub-Saharan Africa, has added enormously to the dreadful experience of that region over the past 20–25 years—or the resurgence of famines there. Perhaps an element is what many regard as the disappointing result of the Highly Indebted Poor Countries debt-reduction process near the end of two decades of sovereign-debt “crises” among developing countries.⁶

How do we raise the additional \$50–60 billion? The Monterrey meeting and its aftermath led to additional pledges by the Organization for Economic Cooperation and Development (OECD) country governments estimated to amount to around \$12 billion a year.⁷

The U.K. finance minister in early 2003 proposed that the donor governments should use that annual sum to accumulate a servicing fund in order to be able to raise loans from the markets in amounts that would allow the extra roughly \$50 billion a year to be disbursed from about 2005 to 2015.⁸ But this idea, the “International Finance Facility,” has not been taken up widely enough to be realistically considered as on the table. In any case it raises problems over what would happen after 2015 when all the extra ODA pledges from the donors (even on the optimistic assumption that they would treat themselves as implicitly bound to increase the extra annual amount initially pledged by four percent a year in real terms for the next thirty years) would be already committed to debt-servicing.

Should we therefore be looking beyond the ODA that OECD governments provide through their ordinary budgetary processes? The answer is emphatically yes. There are measures that rich-country governments have in their power by common agreement to adopt; measures that can significantly increase the resources at the disposal of developing-country governments, or of their citizens directly. And this can often be done without any cost, or even with manifest gain, to the treasuries of the rich countries. There are other measures for which the cost to the rich countries is likely to be trivial, or at least widely dispersed and barely identifiable. Any clear domestic interests in the rich countries against these measures are likely to be not entirely respectable, if not actually criminal.

What is preventing the adoption of these measures? The answer presumably has to be some mixture of inertia, lack of imagination, prejudice, and ignorance. Measures to which these, rather than objective

6. Bernhard Gunter, *Achieving Long-Term Debt Sustainability in Heavily Indebted Poor Countries (HIPCs)*, in CHALLENGES TO THE WORLD BANK AND IMF: DEVELOPING COUNTRY PERSPECTIVES 91–118 (Ariel Buira ed., 2003).

7. See HM TREASURY & DEP'T FOR INT'L DEV., INTERNATIONAL FINANCE FACILITY 13 (2003) [hereinafter INTERNATIONAL FINANCE FACILITY].

8. *Id.*

interests, are the only obstacles that should be treated as “soft targets” by those who accept the urgency of extra funding for the fight against extreme poverty in its various forms. The intrinsic political difficulties that they face should on reasonable calculations be less than those likely to arise over additional budgetary ODA. The challenge is to dispel the inertia, the lack of imagination, the prejudice, and the ignorance.

I shall consider two classes of these measures: first, those putting additional resources potentially available for “development” into the hands of governments or private residents of developing countries; second, those allowing extra funds to be available internationally, enabling “global” decisions—decisions by institutions that represent, however imperfectly, the world’s people as a whole—to be made about their use.

IV. RESOURCES FOR GOVERNMENTS AND HOUSEHOLDS IN DEVELOPING COUNTRIES

Two painless (or even pleasurable) ways of putting significant extra resources into the hands of governments in developing countries are: international tax cooperation (which can bring fiscal benefits to most countries, rich or poor, either by increasing revenue or by enabling tax rates to be reduced, and need harm the interests only of small tax-haven States—which may be compensated—and certain classes of people with criminal, or socially dubious, intent); and regular issues of the IMF’s SDRs. A method of putting more resources into the hands of large classes of private people in a number of developing countries (painless except just possibly to certain financial intermediaries) would be to issue a bond with certain characteristics that would make it suitable for holding and transfer by migrant workers and their non-migrant families and home communities.

A. International Tax Cooperation

Considered here is legislative and administrative cooperation to check avoidance and evasion of taxes and to remove the incentives to the self-defeating practice of competitive reductions in the rates of taxes and competitive concessions over their application (so-called “tax-degradation”).

From the viewpoint of the treasuries of countries covering most of the world’s population, this cooperation can be a win-win game. Estimates of the positive fiscal gains depend on an inevitable element of guesswork. A very crude summary by the present writer, on the basis of detailed studies by others, is that present arrangements lead to “an

annual revenue loss for developing countries at least of the order of magnitude of total ODA, with a loss for the world several times as high.”⁹ These fiscal revenue losses are lying around waiting to be recovered.

It is true that revenue gains to a country’s treasury are not identical with gains to its public. But reducing revenue losses that arise from evasion and avoidance, or from granting concessions motivated only by a desire to outbid other countries for inward investment, expands a country’s choice for either additional public spending or reduction in general tax rates.

Because of the fact that elimination of these revenue losses would result in direct gains to the treasuries of countries covering the overwhelming majority of the people of the world, there is every reason to expect attainment of this goal by consensus.¹⁰ Though there would be advantages in the adoption of certain elements of common practice, there would be no need for different countries to adopt the same rates or patterns of taxation.

These defects have not been ignored entirely, and cautious moves toward reducing the most readily remediable of them have been recently made in the EU and the OECD. Efforts have also been very recently mooted¹¹ for upgrading the UN’s Ad Hoc Group of Experts on International Cooperation in Tax Matters (Ad Hoc Group) as a first move toward making it into an intergovernmental forum, so that reforms can be negotiated in an arena that includes poor as well as rich States.

The defects of present arrangements relate mainly to the taxation of income from capital and enterprise.¹² Direct investment and portfolio investment entail different problems requiring differing remedies, and

9. ANTHONY CLUNIES-ROSS, *RESOURCES FOR SOCIAL DEVELOPMENT* 35 (Policy Integration Dep’t, World Commission on the Social Dimension of Globalization, ILO, Working Paper No. 21, 2004), at http://www.ilo.org/public/english/bureau/integration/download/publicat/4_3_206_wcsdg-wp-21.pdf.

10. The residue of small “tax-haven” states that would directly lose out could probably be compensated. Additionally, as Reuven Avi-Yonah argues in this issue, their refusal to cooperate in some of the potential agreements would not necessarily render those agreements ineffective. Reuven Avi-Yonah, *Bridging the North/South Divide: International Redistribution and Tax Competition*, 26 MICH. J. INT’L L. 359 (2005).

11. See, for example, notes distributed for a lecture entitled “International Tax Co-Operation” delivered by Ghislain T. J. Joseph at a Conference on Feasible Additional Sources of Finance for Development staged by the Friedrich-Ebert-Stiftung New York Office and others. Ghislain T. J. Joseph, *International Tax Co-Operation* (May 30, 2003) (on file with author). Information received in a personal communication from Daniel Platz of the U.N. Department of Economic and Social Affairs indicates that one step in this direction was made by the U.N. Economic and Social Council on November 11, 2004, with the re-naming of the Group as a Committee and a decision that it should meet annually to discuss issues of international tax cooperation.

12. See Avi-Yonah, *Bridging the North/South Divide*, *supra* note 10.

there are also measures that are relevant to both. Briefly, the most important measure needed for reducing evasion over portfolio-investment income is for the rich countries to remove any tax-exemption on such income that applies to foreigners or non-residents, and at best perhaps to agree that they will apply a withholding tax to foreigners' income at a common high rate.¹³ The most important counter-measures to evasion and avoidance over direct-investment income are probably: (a) to require each enterprise that has income sources in several jurisdictions to file a return of its whole world income to each of those jurisdictions; and (b) to agree on a simple formula, based on one or more readily identified variables, for dividing the tax base among the jurisdictions and hence assessing the revenue due to each.¹⁴ Measures reducing the scope for evasion that apply to both portfolio- and direct-investment income are the elimination of conventions of bank secrecy insofar as they involve withholding information from tax authorities; the sharing of information among the authorities of various countries, extending at best to a common system of identification numbers for taxpayers; and perhaps also coming as close as possible to a uniform definition of income for tax purposes.

A simple and direct way of reducing the incentives to competitive tax-degradation in the form in which it most commonly occurs is for the countries of a taxpayer's residence to apply consistently the credit principle (treating tax paid in the source country as if it were a contribution to the tax due in the country of residence) in assessing the taxability of income earned abroad. This means that any advantage (for purposes of attracting inward investment) to a host (source) country from lowering its corporation-tax rate (either generally or preferentially to foreign investors) below that applying in the enterprise's country of residence, or from offering tax holidays, will be eliminated.

Many developed countries do indeed apply the credit principle, but, as explained in the paper by Michael Littlewood¹⁵ in this issue, they often do not do so consistently, in that they do not universally tax the undistributed income accruing to overseas subsidiaries of resident companies. Hence, at least some of that income is subject to tax only in the host country, so that the host may expect to attract additional investment by lowering its corporation-tax rate or by giving foreign firms preferences. Littlewood illustrates that closing this gap requires a comprehensive system on the part of OECD countries for taxing both

13. See Reuven Avi-Yonah, *Globalization, Tax Competition, and the Fiscal Crisis of the Welfare State*, 113 HARV. L. REV. 1573 (2000).

14. See VITO TANZI, *TAXATION IN AN INTEGRATING WORLD* 26 (1995).

15. See Michael Littlewood, *Tax Competition: Harmful to Who?*, 26 MICH. J. INT'L L. 411 (2005).

“controlled foreign corporations” (CFCs) and “foreign investment funds” (FIFs), as is done by New Zealand.¹⁶ Though he is doubtful about the ethics of anything in the nature of coercion from the OECD to reduce competitive tax concessions on the part of developing countries, it would appear that this method of removing the incentives to such concessions would not be subject to that objection.¹⁷

Initiatives are in place, especially on the taxing of portfolio income and the attempt to get more information from tax havens.¹⁸ Citadels of resistance among the rich countries, such as Luxembourg and Switzerland, seem to be giving way. There are clearly a number of fronts on which movement ought to be possible. It may be that progress would be faster and more acceptable if there were a regular and fully international negotiating forum comparable in some ways to the World Trade Organization, as Vito Tanzi and the Zedillo Panel among others have argued. But the first-term George W. Bush Administration set its face against even discussing this option. Maybe, however, the more modest moves to upgrade the UN Ad-Hoc Group into an intergovernmental body, added to the activity of the OECD, will provide the forum needed. That this field lies open, analyzed but untapped, seems an example of the mysterious ways of human political behavior.

B. Regular Allocations of Special Drawing Rights

The IMF's Special Drawing Rights (SDR), authorized from 1969, were designed as a form of international money for supplementing the assets held as international reserves. Under existing rules, any issue (“allocation”) of SDRs is made to IMF members in proportion to their “quotas,” that is their contributions to the organization.¹⁹ A dominant belief at the time was that there could be a global shortage of assets available for international reserves, and that this could restrict world output and income. Beliefs about the behavior of the world monetary institutions that SDRs were designed to serve changed very soon after their creation was authorized in 1969—partly because the objective situation itself changed with the end in 1971 of the Bretton Woods system of exchange-rate management. And in fact, since they were authorized, only six years have seen allocations of SDRs, the last of them being 1981. Though most members of the IMF have been in favor of further allocations, a

16. *Id.*

17. See TANZI, *supra* note 14 (exploring the case for these changes in detail); Avi-Yonah, *supra* note 13 (same). See also Clunies-Ross, *supra* note 9, at 5–14 (summarizing the arguments).

18. See Avi-Yonah, *supra* note 13, at 1653–66.

19. See GEORGE SOROS, GEORGE SOROS ON GLOBALIZATION 77 (2002).

small group of industrialized countries blocked any moves in this direction until the mid-1990s, when the Clinton Administration backed an allocation under amended rules that would have given new IMF members the same ratio of total cumulative allocations to their quotas as old members.²⁰ But, because this measure entailed changing the IMF's Articles of Agreement, it necessitated submission to members' legislatures for ratification of support amounting to eighty-five percent of voting power, and the U.S. Congress rejected it, eliminating this possibility.

Latterly, however, both the Zedillo High-Level Panel²¹ and two eminent IMF insiders²² have argued convincingly that further SDR allocations are of significant (and cumulative) positive value to many or most developing countries, on the ground that they reduce (virtually to zero) the cost to those countries of holding additional international reserves. In so doing they encourage those countries to hold more reserves, and thus to reduce the vulnerability to crises of confidence, both of those countries themselves and of the world financial system at large.²³

The holding-cost benefit of SDRs comes about because of the interest arrangements applying to SDRs and the terms on which various countries' authorities can borrow in the markets. The IMF pays interest at the SDR rate *to* the holder of SDRs. Then, the IMF receives interest at the same rate *from* the original recipient of the SDRs, the authority that received them in the "allocation." So, if a monetary authority holds more than the volume of SDRs that it has received in allocations, it is a net recipient of interest. If it holds less, it is a net payer. But receiving SDRs in an "allocation" and continuing to hold them has no net cost. The authorities of industrialized countries can generally borrow in the markets at rates corresponding to the short-term interest rates that they would expect to receive from the holdings of reserve assets. So adding to their reserve holdings has effectively no cost for them, and hence the receipt of extra allocations of SDRs has no particular value.²⁴ But many

20. *Id.*

21. *2001 Report of the Secretary-General, supra* note 3, at 58–59.

22. PETER B. CLARK & JACQUES J. POLAK, INTERNATIONAL LIQUIDITY AND THE ROLE OF THE SDR IN THE INTERNATIONAL MONETARY SYSTEM (IMF Working Paper No. 02/217, 2002).

23. These benefits are quite independent of those, considered below in Part V.A, that would come from the recycling for global purposes of SDRs that had been allocated initially to industrialized countries but were superfluous to their needs.

24. This possibly explains why the United States, the United Kingdom, Japan, and Germany were against further allocations through the 1980s. Their currencies provided the great bulk of the reserve assets for which SDRs would be a substitute, and the desire of other

developing countries have to borrow at higher rates than those that they would receive on their reserve holdings, so that increasing reserves has a cost for them. They can eliminate this cost if they can instead add to their reserves through allocations of SDRs.

Michael Mussa estimated that an allocation of SDRs amounting in total to SDR 36 billion (then worth rather more than the same number of U.S. dollars) would convey income benefits to developing countries (those that would otherwise incur a net cost in adding to their reserves) of about SDR 1 billion *per year* thereafter.²⁵ So, as follows from Mussa's estimate, the total effect of an allocation of this amount each year for ten years would provide income benefits of SDR 10 billion *a year* from then on.

What scale of allocations can we reasonably expect? Mussa used his figure of SDR 36 billion because the IMF Managing Director was then advocating an allocation of that level. If the IMF's members took half-seriously the intention, expressed in the 1978 Second Amendment to the Articles of Agreement, that SDRs should eventually form the "principal reserve asset in the international monetary system"²⁶—and compromised, for example by supposing that the demand for reserves would increase roughly in proportion to world trade and aiming that SDRs would account for all the *future increase* in reserves—then, according to a rough estimate based on the basis of trade growth over the 1990s, SDR allocations by about the year 2000 would be of the order of SDR 100 billion a year (then about \$130 billion).²⁷ But IMF insiders seem to consider that the most that monetary authorities in aggregate will be prepared to hold as annual additions to the SDR content of their reserves—and therefore the most that should be issued in any year—is more like SDR 20–35 billion, Mussa's hypothetical figure or less, which would still come over the years to make a significant contribution in additional income to the beneficiary developing countries.

The fact that removal or reduction of the marginal cost of reserve-holding for developing countries would encourage them to hold more reserves would serve national and world stabilization objectives, and might be even more important for welfare than the net income gain.

countries' authorities to hold their currencies provided them with an additional source of cheap loans.

25. CLARK & POLAK, *supra* note 22; MICHAEL MUSSA, ET AL., EXCHANGE RATE REGIMES IN AN INCREASINGLY INTEGRATED WORLD ECONOMY (IMF Occasional Paper No. 193, 2000).

26. JAMES M. BOUGHTON, SILENT REVOLUTION: THE INTERNATIONAL MONETARY FUND 1979–1989 924 (2001).

27. CLUNIES-ROSS, *supra* note 9, at 36.

Any *cost* of these measures for industrialized countries or anyone else would be hard to identify and at most trivial. If the measures contributed to world financial stability, on this account alone there would be benefits far exceeding any hypothetical cost. Greater reliance on SDRs for reserves would somewhat diminish the world's demand for short-term securities expressed in dollars and the other main reserve currencies, and thus slightly reduce the capacity of the citizens of the countries issuing those currencies to borrow at low cost on world markets. Official holdings of these securities, however, are only a minor part of total holdings, and in any case an extra SDR 20–35 billion a year would still, as the figures above imply, leave even the official holdings of these assets expanding.

The Group of 24, campaigning development NGOs, globalization protesters, internationalist politicians, concerned lawyers and economists, should surely then all be clamoring loudly for regular SDR allocations.

C. A Migrant Bond²⁸

Migrants' remittances, officially recorded around \$80 billion in 2002²⁹ and almost certainly underestimated, are a larger source of external finance for developing countries as a whole than foreign aid though smaller than foreign direct investment, and their volume is relatively stable across cycles and may even be counter-cyclical in the recipient country. They represent generally a flow of disposable income from richer to poorer countries. Studies suggest that they have a positive impact on the level of investment in the recipient countries and on economic growth there.³⁰ Some of the money goes to community

28. The suggestion here and the argument for it draw largely on information and ideas in Andrés Solimano, *Remittances by Emigrants: Issues and Evidence*, in *NEW SOURCES OF DEVELOPMENT FINANCE* 177 (A.B. Atkinson ed., 2004). The author of that paper has no responsibility for the use I have made of it, and the expedient suggested here is not one of a number that he proposes.

A further WIDER Discussion Paper, Tony Addison & Abdur R. Chowdhury, *A Global Lottery and a Global Premium Bond*, in *id.* at 156, floats the possibility of the issue by an international institution of a UK-style premium bond denominated in a convertible currency or a basket of currencies. This is considered as an instrument more for raising funds internationally than for maintaining the value (including the value in cross-border transfers) of the assets of small savers and community organizations, but, without actually mentioning migrants, the authors recognize its value for this purpose, and also for providing reliable collateral for small business loans and as a medium for gifts between individuals and for charitable donations.

The main proposal made below draws on ideas from both of these papers.

29. Solimano, *supra* note 28 at 182.

30. Solimano cites a study by Dilip Ratha which records "positive effects of remittances on investment in receiving countries such as Mexico, Egypt, and [Sub-Saharan

institutions in the home countries such as schools and churches. The costs that migrants face for transmitting funds home are high, especially through the greatly predominant class of intermediary, however, Money Transfer Operators.³¹

To increase development and welfare value, it appears best for funds remitted to get through in as large a volume as possible. It is also right that, in order to fulfill the migrants' wishes to remit, the only deductions should be for the necessary costs of transmission; and efficiency demands that the senders should not be deterred by the imposition of charges that are excessive in relation to these necessary costs. Reducing the transmission costs will probably help in two ways: in bringing the amount received closer to the amount sent; and for that reason probably also encouraging migrants to send more (though the opposite response is in principle possible).

It seems to follow from the figures that a quite plausible reduction in transmission charges, say of five percentage points on average all round, would mean that additional funds of the order of \$4 billion a year would reach people of generally low or modest incomes (or in some cases community institutions) in developing countries; possibly more if the reduction in charges increased the willingness of the remitters to remit. Andrés Solimano, from whom this account of the basic elements of the situation are derived, suggests a number of ways in which the governments of receiving and sending countries might cooperate with banks and other financial institutions to reduce the transmission costs.³²

Here I add one further possibility. An international financial institution, possibly the World Bank, might issue loans designed specifically as durable stores of value for migrants and for their families and communities in their countries of origin. The bonds should be purchasable over the counter in a network of institutions in sending countries, and they should be negotiable for cash in local currency at rates of exchange fixed by formula for each country in relation to the current official or market rate. Administration of the bonds might be franchised for a period of years by competitive tender to an alliance of

Africa], where remittances [had] financed the building of schools, clinics and other infrastructure". Solimano, *supra* note 28, at 189 (citing Dilip Ratha, *Workers' Remittances: An Important and Stable Source of External Development*, in WORLD BANK, GLOBAL DEVELOPMENT FINANCE: STRIVING FOR STABILITY IN DEVELOPMENT FINANCE: ANALYSIS AND SUMMARY TABLES 157-76 (2003)).

31. Solimano's figures for the average charges on sending various sums from the U.S. to several of the Andean countries indicate that, for transmitting in local currency to certain countries, they can amount to as much as 13-14 percent of the value of the remittances, and averages for sending \$200 in late 2001 and 2002 from the U.S. to Latin America were respectively 10.1 percent and 8.5 percent. *Id.* at 194.

32. *Id.* at 195-97.

banks that possessed the outlets necessary to provide accessible services for the people at whom the bonds were directed. Expressing the bonds' value in SDRs is a way of maintaining their value as far as possible in the face of currency fluctuations. Agreement with relevant governments might be necessary so that the bonds might pass legally across borders without incurring fiscal charges or needing to convert from one currency into another.

Potentially this would provide not only protection for the funds of migrant workers and their relatives but also an additional source of loan funds for the international institution issuing the bonds, possibly the International Bank for Reconstruction and Development (IBRD) or another arm of the World Bank Group created for this purpose.

V. RESOURCES FOR GLOBAL ALLOCATION

This section considers two ways to raise funds with no particular national label on them for global disposition. Again, the authorities that would have to contribute or raise them could do so (or so it would seem on dispassionate analysis) at very low or negligible cost to themselves fiscally or to their peoples economically, and without the political cost of budgetary allocation.

There is a further condition required before funds in this category can be raised. That is that there should be some agreement on the institution that will allocate them—even if the only decisions that that body will have to make about the funds are to which of the other international institutions it will hand them over. Yet this problem should not prove insoluble.

A. *Recycled Special Drawing Rights*

George Soros recently revived an idea that in essence has surfaced periodically since as far back as 1958 (before SDRs were in existence).³³ This proposal is that international liquid assets, created by the world community primarily for reasons of economic stabilization, should be channeled into the system by giving either the governments of developing countries or international organizations these assets to act as additional purchasing power. The form in which SDRs were created, described above, and the character of the international monetary system as it developed in the years immediately after their birth, determine the form that this device must now take.

33. SOROS, *supra* note 19.

As has been explained above, industrialized countries, which can raise funds at interest rates similar to those that they would earn on the assets used for international reserves, derive no significant benefit from the receipt of SDRs. Soros proposes, therefore, that allocations of SDRs should first be resumed, and then the industrialized-country authorities should make over their own allocations (about sixty percent of the total in each issue) for development purposes.³⁴ With annual allocations of \$20–35 billion, the range that insiders seem to think is worth discussion, \$12–21 billion each year would be available for recycling. The complication is that the authorities allocated SDRs remain liable to the IMF for interest on them at the SDR rate. So long as they are also holding the SDRs allocated, they are also receiving interest on them at the same rate. So in that case the net cost to them is nil. If they give up the SDRs, however, they continue to be liable for the interest without any corresponding receipt. Accepting a liability to pay interest in perpetuity on a capital sum is equivalent to making a gift of the capital sum. So, if the authorities concerned are not prepared to make a *gift* of the capital value of the SDRs that they would be handing over, they will not be prepared to hand them over *and* continue to pay the interest on them.

It seems to follow from this that, in order to make the transfers contemplated by Soros possible, the original recipients of the SDRs handed over (the industrialized countries' authorities) must continue to receive interest on them to compensate for the interest that they must continue to pay to the IMF. As a result, what they are handing over then—the hypothetical \$12–21 billion a year—will come in the form not of grants but of low-interest loans without a terminal date. This would require an international institution authorized as a “prescribed holder” of SDRs that would receive them from the national authorities to which they had initially been allocated. It would pay the interest due on them to those national authorities, and would itself have loans, not grants, to dispose of. While it held them, this institution would also be receiving interest at the same rate (from the IMF) and so incurring no net cost. When it allocated them (or more probably their equivalent value after the SDRs themselves had been sold back to monetary authorities) to other multilateral institutions or other bodies, it would presumably require interest at the same rate.

Recognition of these realities, which I consider inevitable while the terms of SDRs remain as they are, takes some of the shine from the Soros proposal. It would be a no-cost scheme from the viewpoint of the rich-country authorities, but it would provide global institutions or

34. *Id.* at 73–96.

developing countries with a source not of grants but of *loans*—at lower interest rates admittedly than IBRD loans but higher rates than those from the International Development Association (IDA).

The loans might, however, have several valuable uses. At the rate of interest involved, the SDRs (or assets received in exchange for them) would be of value to any authority, national or international, that: had debts that needed to be serviced at higher rates; required further reserves, which it would otherwise have to borrow at higher rates; or had favorable investment opportunities that could not otherwise be financed as cheaply. The proceeds of the recycled SDRs might enable a further lending arm of the World Bank Group to be set up for providing loans that were concessional in relation to those that developing-country governments could borrow from the IBRD, let alone those that they could borrow commercially. They might be used to buy-out more burdensome loan obligations currently borne by developing-country governments, reducing their servicing burden. Though there is much of the foreign-loan burden, especially that borne by the poorest countries, that would not be relieved by converting to loans at the SDR rate, a significant part of it could be reduced. In 1999, low-income countries owed twenty-nine percent of their debts to private creditors.³⁵ In that year, the rate of interest on new loans from the private sector to low-income countries was 7.1 percent,³⁶ while the average SDR rate for the year was only 3.5 percent.³⁷ International institutions might also benefit in certain circumstances from being offered costless ways of holding large reserves against contingencies.

If there are benefits from this arrangement or indeed from the creation of SDRs itself, for developing countries, or for the global institutions serving them, or more generally for procuring global public-goods, where do those benefits come from? Two elements between them probably provide the answer. First, funds are available to the relevant governments at less cost than they would otherwise be because the IMF in its SDR dealings, and possibly also some other global institutions in the chain, can act as if they are not risk-averse, so that some of the negative externality introduced by risk is removed. Second, insofar as national monetary authorities are prepared to absorb the extra SDRs, they will hold in their reserves correspondingly less dollar and other-currency securities. In effect, this diverts a part of their low-interest lending from the major-currency countries; and correspondingly

35. WORLD BANK, GLOBAL DEVELOPMENT FINANCE: BUILDING COALITIONS FOR EFFECTIVE DEVELOPMENT FINANCE: COUNTRY TABLES 4 (2001).

36. *Id.* at 53.

37. INTERNATIONAL MONETARY FUND, INTERNATIONAL FINANCIAL STATISTICS YEARBOOK 111 (2002).

additional low-interest lending goes, through the process described, to the authorities that receive the recycled SDRs. The recycling itself, after the allocation of SDRs has been made, does not generate any additional costs for the governments that allow their SDR allocations to be recycled. It would seem that no relevant interests could be opposed to it.

B. Globally Coordinated Taxes

Considered in this section in principle is any proposal for a tax to be collected by national authorities but on a global scale and by something approaching global agreement. To be worth considering in the context, any of these approaches must in some way be economically, politically, or administratively preferable to ordinary budgetary ODA contributions. There must be some reason why governments would be prepared in combination to impose and collect one of these taxes and transmit the proceeds for global use, rather than contribute an equivalent amount from their budgets.

For example: (1) the tax imposed in combination might have a cost that was widely dispersed and not readily noticed; (2) the process of legislating for it or administering it or both might simply be less demanding on political time and effort or bureaucratic outlay than regular domestic alternatives; (3) it might compensate for some negative externality against which global action seemed to be needed; or finally (4) a global or near-global decision to proceed might bind-in all parties in a way that precluded free-riding and was therefore reassuring to each party that it would not be bearing an undue part of the burden. Any one or more of these conditions might conceivably tip the scales and cause finance—unavailable through the usual channels—to be forthcoming.

1. A Carbon Tax

One possible revenue project often mentioned because it appears to meet the third of these conditions (that of countering a negative global externality) is a coordinated tax on carbon burning. On the face of it a global carbon tax would kill two birds with one stone. But the countries of the world already have a profusion of both taxes and subsidies that bear on the use of hydrocarbons. The attraction to their governments of an additional consistent tax on the activity is likely if anything to be reduced, rather than enhanced, by the prospect that the proceeds would be surrendered for global purposes rather than contributing to domestic revenue. Tantalizingly a carbon tax at a tiny rate (the equivalent of 5 U.S. cents on a U.S. gallon of gasoline) across the world would realize (on 1996 figures) annual revenue of the order of \$130 billion, and, even if the affluent countries alone contributed the proceeds for global purposes,

the amount would be of the order of \$60 billion. And maybe an extra tax at that low level would hardly be noticed. But no one supposes that an extra tax at this rate would have any significant impact on carbon use, so that the argument that the tax would kill two birds with one stone would fall. And there is no obvious reason why the proceeds of a tax on carbon use, rather than a tax on any other activity or benefit, should be directed internationally. The tax would be relatively easy to impose and collect, but each participating country would separately have to undertake the political process of legislating for it.

2. A Tax on International Air Transport

A tax on international air transport has some of the same immediate attraction as a tax on carbon use and is open to similar difficulties. Both in different ways would also raise doubts about equity. A uniform tax on carbon use across the world would take much more revenue as a proportion of national income from some countries than others, and much more from certain poor than from certain rich countries. An air-transport tax would bear especially hard on those small poor countries that specialized as tourist destinations.

3. A Currency-Transaction Tax (The Tobin Tax or CTT)

In spite of the turbulent and confusing history of the idea of a world tax on currency exchanges, I believe that it has large objective advantages as a source of revenue for global purposes and that the obstacles are now largely those of lack of imagination, prejudice, and ignorance. Some of the ignorance, however, extends to the best-informed and its elimination requires further research.

The potential tax base—the volume of wholesale currency transactions on which the tax would be assessed—has recently been of the order of \$300 trillion a year, so that, *if* a tax at a rate of say 0.02 percent could be imposed without significantly reducing the base itself, as Paul Bernd Spahn gives some tentative reason for supposing, it might raise about \$60 billion a year.³⁸

Until the mid to late 1990s, two major elements appeared greatly to weaken the case for a CTT: a policy problem and an implementation problem.³⁹ The policy problem was that the device had been advocated on the ground that, as well as raising revenue, it would reduce a negative

38. See PAUL BERND SPAHN, ON THE FEASIBILITY OF A TAX ON FOREIGN EXCHANGE TRANSACTIONS (2002) available at <http://www.wiwi.uni-frankfurt.de/professoren/spahn/tobintax>.

39. For earlier extensive discussion of these problems and their possible solutions, see THE TOBIN TAX: COPING WITH FINANCIAL VOLATILITY (Mahbub ul Haq, et al. eds. 1996) [hereinafter THE TOBIN TAX].

externality, the currency instability supposed to follow from speculation in the markets. This raised the difficulty, familiar to economists, of seeking to fulfill two objectives with one policy instrument. In addition, it was at least disputable whether such a tax would really reduce the impact of destabilizing speculation rather perhaps than making it worse, and in any case there was no agreement, even among those who took the former view, over what level of tax would be necessary to make a significant difference. On the revenue side there were further complications introduced by the fact that there was no clarity on how responsive the volume of transactions would be to various rates of tax, and hence on how differing tax rates would affect the revenue yield. And, even if one knew the tax rates that were optimal on both grounds, there would be no reason to expect that they would even approximately correspond.

Spahn resolved this difficulty by following the logic of the rule that two independent objectives require two independent policy instruments.⁴⁰ He proposed the use of two “tiers” of CTT: one very low, universal, and permanent, for revenue; the other, for stabilization, capable of temporary implementation in one country only at any particular time, and if necessary at a very high rate.⁴¹ The stabilization use that he envisaged for this second tier was as a “circuit-breaker” that would come automatically into action in response to certain cues indicating the risk of a speculative run on a country’s currency.⁴² The circuit-breaker would be a penal rate of tax on sales of the currency that would be high enough to prevent further sales.⁴³ Rodney Schmidt showed that there were further possible stabilization uses of a local, temporary, and *ad hoc* application of a CTT that also need in no way interfere with its long-term, universal application at a low rate for revenue.⁴⁴

The implementation problem was that imposing the tax in the market, that is to say in the arena where currency exchanges were agreed, by the tax jurisdiction in whose domain the market was situated, seemed open in various ways to avoidance or evasion. Perhaps twenty or so authorities might need to impose and collect the tax even if no new market sites were to emerge in response.⁴⁵ Moreover, it seemed quite

40. See Paul Bernd Spahn, *The Tobin Tax and Exchange Rate Stability*, Fin. & Dev. 24–27, (June 1996), available at <http://www.worldbank.org/fandd/english/0696/june96.htm>.

41. See *id.*

42. See *id.*

43. See *id.*

44. See Rodney Schmidt, *Efficient Capital Controls*, 28 J. ECON. STUD. 199 (2001) [hereinafter Schmidt, *Capital Controls*].

45. Peter Kenen suggested that all the then fifteen countries of the European Union, together with at least seven others, would need to impose the tax at a uniform rate if migration of transactions from taxed to untaxed or less taxed sites were to be prevented. See Peter B.

possible that new markets could emerge in jurisdictions not imposing the tax or where its administration seemed likely to be ineffective. Whether or not these apprehensions were exaggerated, it was hard to dispel them.

Then Rodney Schmidt hit, through institutional research, on a method of imposition and collection that appeared to be both watertight and inexpensive and to enable five monetary authorities to collect the revenue for the whole world.⁴⁶ What he proposed was that a national monetary authority should impose the tax at the point at which the relevant foreign-exchange transaction was “settled” within its national banking system.⁴⁷ In effect, an authority with a modern settlement system can know the gross values of transactions into and out of its currency.⁴⁸ Offshore netting systems are regulated by central banks and can be required to give the information on gross transactions where it is needed.⁴⁹ Since there are now five currencies (dollar, euro, yen, pound, and Swiss franc) one or two of which will be involved in virtually every wholesale currency trade, it requires only five monetary authorities in cooperation to impose the tax for revenue purposes on all wholesale transactions.⁵⁰ Offshore netting systems are subject to control by central banks and can be brought within the framework by insisting that they provide the necessary information on the gross values of the transactions that they are netting, in order to enable those gross transactions to be taxed. This can be a condition on which any offshore netting system may have access to the relevant national banking system.⁵¹

Schmidt found difficulty at first in having his ideas published. In September 2003, however, I was present when a conference participant representing the IMF spoke of Schmidt’s method of imposition and enforcement as if it was generally recognized as effective, whatever one thought on other grounds of the tax.⁵²

Kenen, *The Feasibility of Taxing Foreign Exchange Transactions*, in *THE TOBIN TAX*, *supra* note 39, at 109, 120.

46. See Rodney Schmidt, *A Feasible Foreign Exchange Transactions Tax* (1999) at http://www.currencytax.org/files/research_items/schmidt1999.pdf, reprinted in *GLOBAL FINANCE* 215, 215–238 (Walden Bello, et al. eds. 2000) [hereinafter Schmidt, *Transactions Tax*]; Schmidt, *Capital Controls*, *supra* note 44.

47. See Schmidt, *Capital Controls*, *supra* note 44, at 199–200.

48. *Id.* at 201–03.

49. *Id.* at 208–09. See Schmidt, *Transactions Tax*, *supra* note 46, at 217–18.

50. Schmidt, *Capital Controls*, *supra* note 44, at 203.

51. *Id.* at 208–09. See also Schmidt, *Transactions Tax*, *supra* note 46, at 217–18.

52. See Teresa Ter-Minassian, *Comments on the UNU/WIDER Project on Innovative Sources for Development Finance* 5 (Sept. 5, 2003) at <http://www.wider.unu.edu/conference/conference-2003-3/conference-2003-3-papers/ter-minassian.pdf>.

Given Schmidt's method of collection, the CTT has the following economic, political, and administrative advantages as a tax providing a source of global revenue:

1. The base is otherwise untaxed.
2. The use of this form of tax for revenue can be effectively independent of its use for other purposes (in this case stabilization).
3. The active cooperation of five national authorities will be enough to collect the tax across the world, though it will be useful if another eight or so stand ready to impose it in case any of their currencies come to be used, like the big five, as "vehicles."
4. The method appears watertight for all transactions ultimately settled within national banking systems (and there are fairly straightforward ways of dealing with other transactions).
5. Administration will be very inexpensive.
6. The burden of the tax will be highly diffused and difficult to detect, apart possibly from its impact on financial institutions dealing in foreign exchange. Aside from that special interest, the burden will fall on various countries and classes roughly in proportion to their engagement, directly or indirectly, in foreign transactions. Across classes in any country, this will tend to make the burden of the tax "progressive" in relation to income (the proportion to income rising as income rises). Across nations, the burden will be very roughly proportional to income, though with quite large variance at any income level. The distribution of the burden across nations will be less objectionable on equity grounds than that of a uniform carbon or air-transport tax.
7. Because the proportions in which the tax is collected (by the five rich-country authorities alone) will bear no relationship whatever to the distribution of the tax burden (which will be general), the imposition of the tax will not be tolerable except on the explicit understanding that the revenue raised will be devoted entirely to global uses such as public-goods or other common purposes such as poverty reduction. At most the authorities undertaking the collection may be allowed to deduct fees for the (small) cost of their administration. In

other words, the tax by the nature of its imposition will only be international (again unlike carbon or air-transport taxes).

In view of these advantages, and the fairly strong possibility that it might alone be capable of raising half, if not all, of the missing \$50–60 billion a year, with little or no readily detectable impact on anyone except possibly foreign-exchange traders, why is a world currency-transaction tax not now on the table? One reason is that the developments of thought in the late 1990s on how to settle the main problems perceived about it are still fairly recent. Its supporters, no less than its opponents, still debate it largely in the terms in which it was considered by a famous symposium in 1995.⁵³ A second reason is probably that it offended the extreme market ideology that was recently quite fashionable among international economists, especially in the years before the 1997–98 East Asian crisis. A third reason is the violent reaction of the very conservative 104th U.S. Congress to the UI-Haq symposium, a response to the fact that this combined the hated idea of a tax with the hated idea of international organization. There was talk of taxing U.S. citizens without their consent—as if discussion of a CTT supposed the imposition of a sovereign world government. In fact, the adoption of any of the means of administration considered would largely result in the U.S. authorities' taxing the citizens of other countries. Though a scheme of tax-collection such as that supposed above would be unthinkable without nearly-universal consent of the world's governments, the United States, or probably any other of the big five, would hold an effective day-to-day veto over the allocation of the revenue or any other feature of the project, since it could effectively scupper the scheme at any time by withdrawing from it.

Though many in America (and some elsewhere) would retain ideological objections to any device that seemed capable of making a large addition to the revenue at the disposal of international institutions, there is surely a strong possibility of dispelling the misapprehensions over what a currency-transaction tax would actually mean. If we seriously consider it important that an extra \$50–60 billion a year should be available in external resources for developing countries in order that the world's current anti-poverty aspirations may be fulfilled, a device such as this, with no equally promising substitute, must surely be considered.

The tax, however, suffers a further handicap that needs to be removed. We do not know with any confidence how the volume of currency transactions would respond to a CTT at various rates. A 0.02

53. See THE TOBIN TAX, *supra* note 39.

percent tax, Spahn has argued, would have little impact on the volume,⁵⁴ but we can not be sure. An expedient might be to impose the tax first at an extremely low rate, say 0.01 percent or less, and to judge the effect of then raising the rate by small increments. But it would be more reassuring to have further research on the nature and behavior of the currency markets directed to answering this specific question. Because of this gap in knowledge and of the weight of prejudice and misapprehension that remains to be dispelled, we should maybe think of the CTT as a device that might be brought in at best five or ten years from now.

VI. CONCLUSION

The message of this paper is that there are plenty of politically soft options to target, moves of common advantage to identify, misapprehensions to dispel, new insights to propagate, institutions to create or reform, and research to conduct, if we are serious about the urgent need of extra resources for development.

54. See SPAHN, *supra* note 38.