Building new foundations: Reimagining the International Financial Architecture

Views and proposals from civil society

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With contributions from

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Introduction: Reforms to the international financial architecture – a work in progress

By Bodo Ellmers and Jens Martens

Reforms to the international financial architecture are among the most contested and controversial issues on the global political agenda. Many governments, United Nations (UN) institutions, expert groups and civil society organizations (CSOs) are critical of the network of institutions and rules that currently shape global monetary and financial policy and control global financial flows, arguing they are not fit for purpose when it comes to addressing the current global crises.

UN Secretary-General António Guterres described the international financial architecture as "outdated, dysfunctional and unfair"[1] and called for a "new Bretton Woods moment" to adapt the architecture to today's economic realities and power relations.[2]

However, what we refer to as the 'international financial architecture' encompasses much more than the Bretton Woods institutions (i.e. the World Bank and International Monetary Fund (IMF). According to a definition used by the UN Conference on Trade and Development (UNCTAD):

> "the international financial architecture (IFA) is a framework of institutions, policies, rules and practices that govern the global financial system. Its aim is to promote international cooperation with a view to ensuring global monetary and financial stability, enabling international trade and investment, supporting the mobilization of the stable and long-term financing required for economic development, combatting the climate crisis, and achieving the Sustainable Development Goals."[3]

The way the current architecture is structured, however, is far from robust enough to fulfil these ambitious tasks.

The challenges are immense

When the UN Member States agreed the 2030 Agenda and its Sustainable Development Goals (SDGs) in 2015, the annual financing gap was estimated at US$ 2.5 billion per year. By 2024, this gap had risen to US$ 4 billion per year, as stated by the UN Secretary-General in his speech at the UN Financing for Development Forum 2024.[4] In other words, the international community is not just failing to close the financing gap, the chasm has widened substantially over the past decade. On the one hand, this increase in financing needs is due to the failure to mobilize sufficient funds in previous years, which has led to a backlog in investments. On the other hand, the cascading crises of recent years that the current IFA institutions have not been able to prevent or cushion have set back development progress. The current system is neither resilient to these crises nor is it able to provide countries with the support they need to deal with them. To

1 https://www.un.org/sg/en/content/sg/speeches/2023-09-18/secretary-generals-remarks-the-high-level-political-forum-sustainable-development

2 https://estatements.unmeetings.org/estatements/10.0010/20230920090000000/tV32tvvz19xc/797EyWwwkqqt_en.pdf

3 UNCTAD (2023), p. 102.

4 https://www.un.org/en/desa/un-chief-urges-%E2%80%98surge-investment%E2%80%99-overcome-4-trillion-financing-gap

make matters worse, countries in the Global South are disproportionately affected by these challenges.

The COVID-19 crisis was an eye-opener: countries in the Global North had access to almost unlimited finance at near-zero interest rates, enabling them to increase health spending and finance gigantic stimulus and social protection programmes, effectively shielding their economies and societies from economic shocks. In turn, many countries in the Global South, hit hard by the economic turbulence caused by the pandemic and the responses to it, were quickly shut out of financial markets and unable to access affordable financing on the scale required, either from public or private sources. The result was severe economic recessions, sharp increases in poverty, unemployment and hunger, and a general setback in development progress. When the UN reviewed progress towards the SDGs in its 2024 report, the findings were sobering: only 17 percent of the SDG targets are on track; nearly half are showing minimal or moderate progress; and trends for more than a third have stalled or even gone backwards.[5]

Today's IFA is ill-equipped to provide foundations for the financial conditions necessary to address other crises, particularly the global climate crisis. The countries that are most affected by climate change do not have access to affordable finance for adaptation or compensation for loss and damage. Efforts to mitigate climate change are being hindered by insufficient investment in the green transformation.

To make matters worse, the prevailing monetary hierarchy in the global economy means that poorer and smaller countries are hit hard by the policy decisions of richer and larger countries. The decision by major central banks in the Global North to raise interest rates in 2022 – initiated by the US Federal Reserve in response to rising inflation at home (i.e. domestic needs) has had major negative spillovers for countries in the Global South.[6]

The cost of servicing increased debt levels has skyrocketed. In summer 2024, the UN Global Crisis Response Group (UN GCRG)-Technical Team at UNCTAD reported that 54 developing countries were spending more than 10 percent of their public revenues on interest payments, up from 30 countries a decade earlier.[7] According to this *World of Debt Report 2024*, debt service on external public debt reached US$ 365 billion in 2022, which is equivalent to 6.3 percent of export revenues. By way of comparison, the report emphasizes that the 1953 London Agreement on Germany's war debt limited the amount of export revenues that could be spent on external debt servicing to 5 percent to avoid undermining the recovery.[8]

The main reason for the increase in debt servicing is the massive borrowing costs. Countries in the Global South have to borrow at rates that are two to four times higher than those of the USA and six to 12 times higher than those of Germany.[9]

Increasing transfers to creditors have serious implications for the ability of governments to finance development and public services. Higher debt service payments combined with lower government revenues are considerably restricting governments' financial room for manoeuvre. Urgently needed funds for healthcare, education, climate and social spending is not available. The UN GCRG warned that 3.3 billion people now live in countries that spend more on interest payments than on healthcare, and 2.1 billion people live in countries that spend more on interest payments than on education.[10]

In 2022, net transfers on external debt from low- and lower-middle-income countries to private creditors were negative at US$ –52.2 billion. This means that even the positive flows still provided by multilateral

5 United Nations (2024).
6 Ellmers (2022).
7 United Nations Global Crisis Response Group (2024).
8 Ibid., p. 10f.
9 Ibid., p. 14.
10 Ibid., p. 18.

development banks and the IMF (US$ 32.3 billion) and bilateral creditors (US$ 3.7 billion) no longer financed development, but simply allowed heavily indebted countries to continue transferring money to private creditors, absorbing scarce financial resources that were badly needed elsewhere.[11]

Debt indicators around the world have deteriorated to such an extent that Development Finance International is already warning of “the worst ever global debt crisis”.[12]

In particular, the poorer countries of the Global South are falling through the financial safety net and do not have access to sufficient liquidity. Only a fraction of the Special Drawing Rights (SDRs) issued by the IMF are available to them. This is not least due to the fact that their interests are still underrepresented in the decision-making bodies of the international financial institutions, in particular the IMF and World Bank. This also applies to international tax cooperation, where African countries in particular are pushing for equal participation under the umbrella of the UN. Finally, there is a considerable need for action in the regulation of financial markets. The inadequate supervision of the non-banking sector in particular is a ticking time bomb for the financial system – and for the global economy.

In view of all these unresolved challenges, it is becoming increasingly clear that systemic reform of the IFA is long overdue.

Systemic problems require systemic solutions

In his speech at the opening of the High-Level Dialogue on Financing for Development on 20 September 2023, UN Secretary-General António Guterres emphasized:

> “It is clear that the systemic problems of financing for sustainable development require a systemic solution: reforms to the global financial architecture. That architecture was created at a time when many of today’s developing countries were still under colonial rule. It is deeply skewed in favour of the developed world. And it has not kept pace with the growth of the global economy.”[13]

But Guterres’ recognition of the need for fundamental reform of the international financial architecture is by no means new. Discussions have repeatedly broken out in response to crises – from the debt crises of the 1980s and 1990s to the global economic and financial crisis of 2007–2008. Over the past four decades, academics and expert panels such as the Commission on Global Governance (1995)[14] have developed proposals for the creation of a global decision-making and coordinating body for economic and financial issues, for example, under the name Economic Security Council. As early as 1999, the Colombian economist José Antonio Ocampo explored areas of consensus and divergence in the disputes over the reform of the international financial architecture.[15]

In its report in preparation for the first Financing for Development Conference in Monterrey in 2002, the so-called Zedillo Panel (Chaired by the former President of Mexico, Ernesto Zedillo) proposed *inter alia* the creation of an International Tax Organization.[16] And in 2009, the Stiglitz Commission (led by American economist Joseph Stiglitz) presented a comprehensive and far-reaching list of measures to regulate and reform the global monetary and financial system.[17]

Over the years, the crises and the resulting calls for reform have led to numerous initiatives and changes in global economic governance. The G20 was upgraded, the banking system was given stricter capital ade-

11 https://findevlab.org/the-collapse-of-external-finance-to-developing-countries/
12 https://development-finance.org/files/Debt_Service_Watch_Briefing_Final_Word_EN_0910.pdf
13 https://estatements.unmeetings.org/estatements/10.0010/20230920090000000/tV32tvvz19xc/797EyWwwkqqt_en.pdf
14 Commission on Global Governance (1995).
15 Ocampo (1999).
16 Zedillo Panel (2001).
17 Stiglitz Commission (2009).

quacy rules (Basel III),[18] the Organisation for Economic Co-operation and Development (OECD) attempted to combat harmful tax competition and aggressive tax avoidance by multinational companies with its Base Erosion and Profit Shifting (BEPS) project,[19] and the IMF provided its Member States with additional liquidity in 2021 in response to the COVID-19 crisis by distributing Special Drawing Rights (SDRs) worth US$ 650 billion.[20]

However, these and other piecemeal measures have failed to address the fundamental problems in the global financial architecture. As we have seen above, the countries of the Global South are still under-represented in the decision-making bodies of economic and financial institutions, there are still trillions of dollars missing when it comes to financing sustainable development, the risk of worsening debt crises is growing and there are still significant gaps in the regulation of global financial markets.

New momentum

In view of the unresolved challenges, global efforts to reform the IFA have recently gained new momentum. A number of initiatives were launched to overcome the acute reform backlog. One example has been the Bridgetown Initiative, which was initiated by the Prime Minister of Barbados Mia Mottley in 2022. It includes a call (in version 2.0) on the shareholders of the IFIs "[to] update the 1945-based institutions to be more inclusive and equitable, including issues of governance, voice, representation, and access to finance".[21]

In June 2023, French President Emmanuel Macron convened a Summit for a New Global Financing Pact in Paris. It formulated the ambitious aim "to lay the foundations for a renewed international financial system, creating the conditions for a financing breakthrough so that no country has to choose between reducing poverty, combating climate change and preserving biodiversity".[22] Ultimately, however, the main purpose of this summit was to promote the discourse on IFA reforms and to prepare decisions in multilateral meetings at G20 and UN level.

At the UN level, Member States have followed the Secretary-General's proposal and made IFA reform a priority topic at the UN Summit of the Future (SotF), which took place in New York on 22 and 23 September 2024. The outcome document of the Summit, the Pact for the Future, contains a chapter on "Transforming global governance", which includes six so-called 'actions' to accelerate IFA reform. While governments decided in general terms to "(c)ontinue to pursue deeper reforms of the international financial architecture to turbocharge implementation of the 2030 Agenda",[23] they failed to reach consensus on any fundamental reform steps.

They noted "with appreciation" the initiative to convene a Biennial Summit at the level of Heads of State and Government "to strengthen existing and establish more systematic links and coordination between the United Nations and the international financial institutions".[24] They also committed "to engage constructively in the process towards developing a United Nations framework convention on international tax cooperation" and to "(s)ecure an ambitious outcome at the Fourth International Conference on Financing for Development in 2025 to close the Sustainable Development Goal financing gap (…)."[25]

In view of its inadequate results, the Summit of the Future was not the endpoint, but merely a milestone in a lengthy process of reshaping the IFA, which will continue at the UN level with the Fourth International Conference on Financing for Development (FfD4) in Spain (30 June to 3 July 2025).

18 https://www.bis.org/publ/bcbs189.pdf
19 https://www.oecd.org/en/topics/policy-issues/base-erosion-and-profit-shifting-beps.html
20 Ellmers (2021).
21 https://www.globalpolicy.org/sites/default/files/Bridgetown2.0-1page%20(2).pdf
22 https://www.elysee.fr/en/emmanuel-macron/summit-on-a-new-global-financing-pact
23 United Nations General Assembly (2024), Action 47.
24 United Nations General Assembly (2024), Action 49.
25 United Nations General Assembly (2024), Action 4.

Continuing reform efforts in various fora

The FfD4 Conference is expected to adopt a successor document to the 2015 Addis Ababa Action Agenda. It will encompass multilateral agreements on domestic and international sources, as well as private and public sources of financing for development, and on the institutions that govern the financial flows. As such, the FfD4 outcome will become the international community's most comprehensive international agreement on financing for development and international financial architecture. It will accompany the Agenda 2030 for its remaining years and will be a central pillar of its means of implementation, and thus a key factor for determining the success or failure of SDG implementation.

There are parallel fora that are relevant for IFA reform, however. Agreements on climate finance and related institutions, for instance, have traditionally been made at the UN Framework Convention on Climate Change (UNFCCC) annual Conference of Parties. The UN strives to negotiate a Framework Convention on International Tax Cooperation until 2027 in an Intergovernmental Negotiating Committee, entering a process innovation in the area of tax norm-setting, which was dominated by the OECD for decades. Norm-setting in the area of financial regulation is dispersed in several plurilateral bodies (and has lost traction recently as the memory of the global financial crisis has faded, while a reform of the Basel Accords and other relevant agreements seems long overdue).

Reform of the IMF and World Bank will also continue to be discussed in the institutions' own governing bodies. One of the main points of conflict at recent UN summits was the question of whether decisions on IFI reform can also be taken under the auspices of the UN or whether they should be reserved exclusively for the governing bodies of the IFIs themselves. Almost the same Member States are represented in both, but with differently weighted voting rights. Most of the IFA reforms of the past two decades have been pre-agreed de facto by the G20 and its Annual Summits. This means that about 90 percent of the world's countries were not directly represented at the negotiating table when these decisions were made. Regaining lost space from the G20 was one of the UN's main intentions for the Summit of the Future.

The interplay between these different fora is complex, especially because many institutions are norm-setters and implementers at the same time. Sometimes one forum sets a mandate for the other to implement (and vice versa). A general feature of global governance is that the outcome of a policy-making process is determined by the process, and the process is determined by the institutions, by the forum that hosts it. The choice of the forum is therefore crucial.

Calls for transformative steps in IFA reform

The contributions to this report take the urgency of fundamental steps towards reform of the International Financial Architecture seriously. The authors deal with various aspects of IFA reform from different perspectives, both geographically and thematically. What they have in common is the conviction that progress and economic justice can only be achieved if all countries are fairly represented in the financial architecture institutions; that the mandates of these institutions are reformed so that the protection of human rights is given top priority; and that the institutions are updated and upgraded with new and effective instruments to address the challenges of our times.

Maria Ron Balsera, Maria Emilia Mamberti and **Matthew Forgette** from the US-based Center for Economic and Social Rights (CESR) address the important topic of debt architecture reform. Since the current non-system is hopelessly overwhelmed by the severe debt crisis, they suggest a transformative approach that integrates existing soft law principles with a new independent statutory mechanism under the UN. This could ensure that governments prioritize social spending over debt service, and thus promote fiscal justice and enable them to fulfil their human rights obligations.

Patricia Miranda from the Latin American Network for Economic and Social Justice (LATINDADD) presents Special Drawing Rights (SDRs) issued by the IMF as an alternative financing instrument that provides liquidity to developing countries without creating debts. She advocates new SDR allocations, using a fairer distribution key that is more closely aligned with the needs of the IMF Member States, so that developed countries could rechannel unused SDRs to developing countries as grants rather than loans. This would thus improve and expand the existing options for rechannelling, currently limited to IMF lending facilities.

Researchers **Oliver Pahnecke** and **Juan Pablo Bohoslavsky** look at one of the key reasons for surging debt levels and debt crises, the high-risk premiums that countries in the Global South have to pay. They identify recommendations on banking regulations issued by the Basel Committee on Banking Supervision, the Basel Accords, on weighted risk as a key reason why creditors charge high-risk premiums to some debtors. A reform of these regulations in the direction that risk premiums would be legally treated as collateral in future could make loans significantly cheaper, because risk premiums would have to be returned after full repayment, or adjusted over time in accordance with the real default risk.

The contribution by **Chenai Mukumba** from Tax Justice Network Africa focuses on one of the most relevant recent innovations in global economic governance – the process leading to a UN Framework Convention on International Tax Cooperation that was initiated in 2024. She describes the Convention as an essential element for creating a fully inclusive tax system, which has been a priority for African countries that have been sidelined by norm-setting on other bodies, in particular the OECD. At the same time, the still-to-be negotiated Convention promises to create a more effective tax system, raise more public revenues and help to curb illicit financial flows.

Avantika Goswami and **Sehr Raheja** from the Centre for Science and Environment in India deal with the important area of climate finance. The authors emphasize the need to mobilize substantially larger amounts of international climate finance transfers. This is reflected in the negotiations on the New Collective Quantified Goal to be set by the UNFCCC. They argue that the IFA needs to mobilize significantly more public finance and that transfers must come in the form of grants rather than debt if support is to be effective and sustainable.

Daniel Kostzer from the International Trade Union Confederation looks at the reform of international financial institutions, in particular the World Bank. He argues that a governance reform that gives borrower countries more influence is a prerequisite for the Bank to work in a more client-oriented way and to become more effective. In addition to a package of operational reforms, he emphasizes above all that the World Bank itself must be larger and better financed. Revenues from a financial transaction tax, he argues, could serve this purpose.

Daniel Oberko from Public Service International (PSI) contributes an analysis of the situation in Ghana, a country that has had recent experience of the IFA, especially with debt crisis management under the G20 Common Framework, and IMF programmes. He argues that the policy prescriptions imposed on Ghana by IMF conditionalities are not working for the country and have stifled health spending. Instead, he argues, the government should improve the accountability and efficiency of public spending, and embark on tax reforms, remove spurious tax incentives and close loopholes for tax abuse.

The chapter by **Ohiocheoya (Ohio) Omiunu** and **Chioneso Samantha Kanoyangwa** from the African Sovereign Debt Justice Network (AfSDJN) looks at the IMF from the viewpoint of social legitimacy. Like Kostzer, they advocate for a fundamental IMF governance reform. This reform should go beyond the minimalist approach that the IMF has taken, which was adding a third African chair to its Executive Boards. It must elevate the quota of low-income countries. Debtor creditors should also be included in IMF-hosted policy forums, such as the Global Sovereign Debt Roundtable, and IMF tools such as the Debt Sustainability Framework need to be reformed to de-emphasize the commitment to austerity.

Conclusion

Reforms of the international financial architecture have emerged as a priority in international relations, both to raise sufficient and more affordable finance for development and public goods, and to protect countries and people from the multiple crises facing our planet. A growing number of civil society actors are tackling this important issue, honing their critique while also making proposals for reform. The contributions to this report show that it is possible to redesign an international financial architecture based on the principles of human rights and economic justice. The key now is to keep up the public pressure on policy-makers around the world to make the most of the opportunities ahead to drive forward the necessary reforms quickly and successfully.

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Rethinking debt restructuring

Rethinking debt restructuring: A rights-aligned approach

By Maria Ron Balsera, Maria Emilia Mamberti and Matthew Forgette

The global debt crisis has reached unprecedented levels with a disproportionate impact on developing countries, which exacerbates inequality and hinders social progress. Numerous attempts at debt restructurings have failed, perpetuating cycles of unsustainable debt. The absence of a coherent international legal framework further complicates these issues, leaving negotiations inequitable and opaque. In this chapter, we propose a transformative approach to debt restructuring reform that integrates soft law principles – such as transparency and sovereignty – with an independent statutory mechanism under the United Nations. Such reforms not only align with human rights standards but also promote fiscal justice by ensuring governments prioritize social spending over debt servicing. By addressing systemic flaws, the proposed reforms aim to establish a fair and sustainable global financial architecture that respects and realizes human rights while fostering equitable development worldwide.

Introduction

The world is in the midst of a global debt crisis. Global public debt-to-Gross Domestic Product (GDP) ratios have more than tripled since the 1970s and are continuing to rise.[1] In 2023, global public debt surged to a historic peak of US$ 97 trillion, growing by 90 percent since 2010. Simultaneously, there is a rising disparity between which countries hold this debt, with developing countries' debt levels rising twice as fast as their developed counterparts.[2]

Many countries have been forced into debt restructurings, negotiated agreements with creditors to cancel (usually just part of) the outstanding debt. However, these restructurings have often failed to achieve lasting results. Data from the International Monetary Fund (IMF) indicates that, between 1950 and 2010, up to 61 percent of countries defaulting on their debt service were repeat defaulters.[3] Restructurings are clearly failing to achieve their fundamental goal: to restore public debt to a sustainable level. Far too often, borrowing governments are forced to divert resources from social services that are essential for realizing human rights in order to pay onerous debts, leading to lower-income countries spending five times more on debt than they spend on dealing with climate change.[4]

This prevalence of repeated restructuring begs a few questions. Namely, what is the existing legal framework for sovereign debt restructuring? And why do these restructurings keep failing to deliver? There is currently no common international framework for sovereign debt restructuring. Instead, leading economists Martin Guzman and Joseph Stiglitz describe the global approach to debt restructuring as "a non-system" that "makes sovereign debt crisis resolution a

1 Gaspar/Poplawski-Ribeiro/Yoo (2023).
2 UN Global Crisis Response Group (2024).
3 Corkery et al. (2023).
4 https://debtjustice.org.uk/press-release/lower-income-countries-spend-five-times-more-on-debt-than-dealing-with-climate-change

complex process – marked by inefficiencies and inequities".[5] This absence of an international legal basis has led the IMF to assume the role of facilitator in many of these negotiations between debt-distressed nations and creditors. However, it has often fallen short in this capacity.

The legal vacuum regarding debt restructuring is most problematic for countries in the Global South. Perceived economic vulnerability means these countries pay significantly higher interest rates than their counterparts in the Global North. In 2022, countries in Africa borrowed at rates four times higher than those in the United States and eight times higher than those in Germany.[6] Countries in the Global North have also banded together to create informal institutions, such as the Paris Club, created in 1956, to collectively negotiate debt restructurings and enhance their bargaining power to serve the role of a "creditor cartel". Calls for the creation of a similar body for countries in the Global South to play the role of a "debtor cartel" exist but have yet to gain traction within the International Financial Architecture.[7]

Put simply, the current state of sovereign debt restructuring is inequitable, opaque, ineffective and undemocratic. The lack of a statutory regime means that each restructuring negotiation is undertaken separately. These independent negotiations are hampered by unequal bargaining power and the lack of an effective unbiased mediator. However, there are options for reform.

In the following chapter, a legal path is outlined on how the current "non-system" of debt restructuring can be transformed into a fair legal framework that prevents debt crises and promotes growth and development while respecting human rights. This approach involves using soft law, quasi-legal instruments such as principles or guidelines created by international organizations that regulate State behaviour. These principles should be incorporated into an independent debt restructuring mechanism under the auspices of the United Nations (UN), providing equal access to countries undergoing restructuring negotiations. Beyond this, a global debt restructuring reform has to be linked to fiscal justice more broadly, ensuring that governments invest public resources to tackle poverty, inequality and other social problems.

Human rights and soft law principles

Soft law is generally understood as rules that are not legally binding but are nonetheless adhered to due to moral sway, fear of adverse action, social norms or other incentives. These rules can be created by a variety of groups and actors, including the UN, the IMF, development banks and many others. Soft law is particularly prevalent in the field of international financial law, given the complexity of the international financial system and thereby the difficulty in designing and implementing hard rules to govern it.

A variety of sources contain relevant soft law standards on debt restructuring. These include the UN Guiding Principles on Business and Human Rights,[8] the G20 Operational Guidelines for Sustainable Financing[9] and the UN Trade and Development (UNCTAD) Principles on Promoting Responsible Sovereign Lending and Borrowing,[10] among many others. However, the most pertinent and specific document related to debt restructuring is the 2015 UN General Assembly Resolution 69/319, which established a set of nine principles to be observed in sovereign debt restructuring procedure: sovereignty, good faith, transparency, impartiality, equitable treatment of creditors, sovereign immunity, legitimacy, sustainability and the principle of majority restructuring.[11]

5 Guzman/Stiglitz (2016).
6 UN Global Crisis Response Group (2024).
7 Corkery et al. (2023).
8 United Nations (2011).
9 International Monetary Fund/World Bank (2019).
10 UNCTAD (2012).
11 UN General Assembly (2015).

Some of these principles, such as impartiality and equitable treatment, extend from the very core of international human rights law. The principles of equality and non-discrimination appear explicitly in the UN Charter and the Universal Declaration of Human Rights (which states that "all are equal before the law and are entitled without discrimination to equal protection"). These have subsequently featured in almost every major human rights instrument. In the context of debt restructuring, this principle restricts creditors from attaining inequitable outcomes through predatory methods. In the past, certain creditors have been able to secure disproportionately favourable outcomes by withholding from debt restructurings and demanding full repayment of the original debt.

The principle of **impartiality** also applies to the debt mediator. It restricts the set of institutions that could host a mechanism for sovereign debt restructuring, since institutions that have a biased representation of the stakeholders involved, or are creditors themselves, are not suitable. It is worth noting that many emerging market States have expressed their dissatisfaction with global financial tribunals (such as the International Centre for Settlement of Investment Disputes), which have been proposed as potential arbitral hosts, as well as with international financial institutions (IFIs), such as the IMF, which is currently playing a key role in facilitating restructuring processes.

Similarly, the principle of **transparency** is derived from the Universal Declaration of Human Rights, which guarantees the right to "seek, receive, and impart information and ideas". Similar language has later been reflected in the International Covenant on Civil and Political Rights (Art. 19). In debt restructuring, transparency is essential. As noted by Guzman and Stiglitz, debt restructuring negotiations often give rise to "perverse incentives for those at the negotiation table [...] transparent negotiations require disclosure of any potential conflict of incentives that could undermine the outcome of a restructuring process".[12]

In the current debt restructuring regime, investors can engage in sovereign credit default swaps, allowing them to swap their credit risk with that of another investor. Unfortunately, the markets for these swaps are currently opaque and do not require public disclosure. The responsibility of creditors under the principle of transparency is spelled out explicitly in the G20 Operational Guidelines for Sustainable Financing, which states, "creditors should facilitate information sharing among themselves and with the IFIs by disclosing comprehensive and updated information on their existing and new lending operations".[13]

Creditors must take measures to ensure that they are publicly disclosing their investment positions so that restructurings take place fairly. Additionally, the bias of major credit rating agencies such as Moody, S&P and Fitch towards countries in the Global South has been a longstanding transparency problem. The methodologies of these rating agencies are often based on subjective factors such as expert opinion, which is prone to be shaped by political influence and corruption.[14] The principle of transparency requires an independent and neutral credit-rating mechanism, ideally hosted by the UN or another multilateral space.

The principle of **sustainability** recognizes the primary goal of debt restructuring should be to restore the public debt to sustainable levels. While this principle is perhaps less explicitly articulated in human rights law, a robust understanding of debt sustainability is crucial for the realization of human rights. Indeed, the General Assembly resolution on the Basic Principles on Sovereign Debt Restructuring Processes explicitly endorses "minimizing economic and social costs … and respecting human rights".[15] This is key because rising debt payments have been linked with public spending cuts and retrogressions in the

12 Guzman/Stiglitz (2016), p. 6.

13 International Monetary Fund/World Bank (2019), p. 15.

14 Khanna (2024).

15 UN General Assembly. (2015), para. 8.

achievement of economic and social rights in low-income countries. Unsustainable debt payments thereby have a direct impact on citizens' enjoyment of human rights such as health, education and access to food and clean water. As noted by international sovereign debt experts Juan Pablo Bohoslavsky and Matthias Goldman, "Sovereign debt sustainability is today widely recognized in international legal practice … the private interests of creditors need to be balanced against public interests".[16]

The UN sustainability principle also acknowledges that stakeholders in a restructuring process encompasses informal creditors, such as pensioners and workers. Current debt renegotiations often fail to take these stakeholders into account. As UN Independent Expert on foreign debt and human rights Attiya Waris described after her visit to Argentina to assess its debt situation, "Argentina must maximize its resources to uphold human rights and prevent regression".[17]

Another key principle identified in the UN General Assembly resolution is the duty to negotiate in good faith when debt becomes unsustainable. The UNCTAD Principles on Promoting Responsible Sovereign Lending and Borrowing expand on this principle, specifying lenders' duty "… to behave in good faith and with cooperative spirit to reach a consensual rearrangement (…). Creditors should seek a speedy and orderly resolution to the problem."[18] Notably, this principle is clearly violated by vulture funds, which seek preferential treatment to other creditors through holdout and litigation methods.

Creditors who lend at an interest rate that includes compensation for risk cannot, in good faith, bargain to receive treatment as if the lending were risk-free. It is also important to mention the existence of odious or illegitimate debt, which may have been negotiated under repressive regimes or under exploitative terms.[19] The UNCTAD Principles underline this, emphasizing that "a creditor that acquires a debt instrument of a sovereign in financial distress with the intent of forcing a preferential settlement of the claim outside of a consensual workout process is acting abusively".[20] These types of debts produce little to no public benefit and should be subject to cancellation.

Rights-aligned statutory mechanisms

Of course, the UN Principles on Debt Restructuring will fail to have an impact if they continue to be violated or applied selectively. Thus, codification of these principles in hard law represents a preferable long-term solution. Given the difficulty inherent in any multilateral international endeavour, domestic legislation in individual countries has been identified as a possible first step towards debt restructuring reform. One benefit of this approach is that it is clear which countries should be targeted. The vast majority of sovereign bonds are regulated under either New York or English law. If those jurisdictions were to adopt a domestic legal framework for debt restructuring based on the soft law principles articulated above, this could fill the debt restructuring legal void without having to resort to passing an international treaty.

Unfortunately, these jurisdictions have historically failed to abide by the principles in past debt restructuring adjudications. Perhaps the most cited example is the treatment of the so-called "vulture funds", which emerged in Argentina's initial debt default in 2005. These are hedge funds that specialize in purchasing distressed debt on secondary markets during crises. After purchasing the debt at an extremely low value, the vulture funds then pursue payment in full (as well as additional compensation for risks they did not take) through prolonged and expensive litigation

16 Bohoslavsky/Goldmann (2016).

17 UN Office of the High Commissioner on Human Rights (2022).

18 UNCTAD (2012), p. 7.

19 Corkery et al. (2023).

20 UNCTAD (2012), p. 8.

in either New York or London.[21] These funds tend to have recovery rates of 3 to 20 times their investment,[22] while robbing other creditors of equitable treatment in negotiating processes and citizens of public resources that governments would otherwise provide.

One could certainly envision a better system for the resolution of debt crises through restructuring. Rather than the current mess of decentralized procedures, which feature an array of powerful creditors negotiating with low-income countries entangled in debt distress, there should instead be a simplified, comprehensive framework designed in accordance with the principles discussed above. Already in 2014, UN General Assembly Resolution 68/304 sought the establishment of a "multilateral legal framework for sovereign debt restructuring processes".[23] Support for a statutory-based debt resolution mechanism can even be traced back to 2002, when the debt crisis in Argentina motivated the IMF to create a proposal (although this proposal was quickly shelved due to opposition from IMF board member states).[24]

The establishment of an independent mechanism for debt restructuring, embedded within the UN, has been a longstanding goal for debt justice advocates. This could provide equal access to comprehensive information and independent technical support to the country team in charge of the renegotiation process. It could also codify the human rights-based principles discussed above, ensuring mandatory participation of all creditors in debt restructuring to prevent vulture fund litigation.

A multilateral statutory framework for debt restructuring remains the most effective and fair solution to the debt restructuring problem. A document published by the UN's former independent expert on foreign debt clearly outlines several human rights benchmarks that should be included in the new regime.[25] These include explicit references to the compatibility of debt restructuring with human rights obligations; the inclusion of human rights impact assessments and improving debt sustainability assessments; and the assurance that minimum levels of enjoyment of economic, social and cultural rights can be satisfied amidst debt restructuring.

So far, this vision has been easier to imagine than it is to realize. A number of efforts have been made to strengthen debt restructuring procedures, including the G20 Debt Service Suspension Initiative, the G20 Common Framework for Debt Treatment and the Global Sovereign Debt Roundtable. However, fear that participation would lead countries to have reduced credit ratings has kept many States from engaging, and power imbalances between creditors and debtors persist.

This persistent inequity highlights the importance of mobilizing cross-cutting stakeholders to join future demands for debt restructuring. The case of Pakistan is one of many recent examples illustrating how the problems are interconnected. In 2023, Pakistan spent 46 percent of its government revenue on servicing foreign debt, leaving it unable to combat its climate disaster.[26] At the same time, the country relied on unpaid care and domestic work to fill the labour gap, which worsens economic insecurity and social mobility for women and girls. Clearly, these movements are intersecting, and addressing them will require coordination and collaboration.

Fiscal justice

It is also important to examine the broader link between global debt restructuring reform and fiscal justice. Fiscal justice requires government investment in resources to tackle poverty, inequality and

21 For more information about the famous case of Republic of Argentina v. NML Capital, see https://harvardlawreview.org/print/vol-128/republic-of-argentina-v-nml-capital-ltd/

22 African Development Bank Group (2023).

23 UN General Assembly (2014).

24 Krueger (2002).

25 Bohoslavsky (2015).

26 Corkery et al. (2023).

other social problems. Over US$ 480 billion is lost each year due to abusive international tax practices.[27] This is a similar figure to those cited in calls from UN Secretary General António Guterres in order to meet the Sustainable Development Goals (SDGs) financing gap.[28] Governments also have the obligation under the International Covenant on Economic, Social and Cultural Rights to dedicate maximum available resources to realizing human rights. Currently, many countries in the Global South are forced to take on extreme amounts of debt to fund even basic social services. Thus, a vital part of combating over-indebtedness in the Global South comes down to expanding countries' fiscal space through progressive taxation and the elimination of tax abuse.

Another connection to fiscal justice is that any multilateral debt restructuring mechanism should also ensure that countries are not prevented from fulfilling their basic public spending duties under human rights law. As the Committee on the International Covenant on Social, Economic and Cultural Rights has underlined, States have the core obligation to ensure the satisfaction of, at the very least, minimum essential levels of economic, social and cultural rights.[29] States will find it extremely difficult, if not impossible, to fulfill these minimum essential levels if debt servicing enjoys the same or even greater priority in national budgeting than education or health expenditures. Retrogressive measures should be avoided and would need to be fully justified by reference to the totality of the rights provided for in the Covenant. Even then, retrogressive measures should be temporary, necessary and proportionate as well as being non-discriminatory.

Conclusion

There are several complementary recommendations towards a rights-aligned debt restructuring reform. First, soft law human rights standards and principles must be respected and used as a guide when interpreting and applying the law in sovereign debt disputes. This means, for example, not imposing any economic policy conditions on the debtor during the debt restructuring process, because of the principle of legitimacy. Additionally, independent statutory measures should be informed by these soft law principles, and should ensure mandatory participation of all creditors with an unbiased adjudicator. Finally, progressive taxation and other just fiscal policy must be part of the solution towards preventing countries from becoming embroiled in endless debt restructurings.

Reforming international tax law is fundamentally linked with debt restructuring reform. Of course, there are also a myriad of other issues that link to the debt crisis that must be taken into account, such as the right to development, the impact of debt on women's rights, the intersection of debt and climate finance and the legacies of colonialism that are still present in the international financial system. Improving our world's broken debt restructuring system is possible, but it requires rethinking the global policies that make up the current "non-system", as well as respecting fundamental human rights.

27 Tax Justice Network (2023).

28 https://sdg.iisd.org/news/un-calls-for-usd-500-billion-per-year-for-sustainable-development/

29 UN Committee on Economic, Social and Cultural Rights (1990).

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2

Special Drawing Rights

Liquidity without increasing debt: Special Drawing Rights

By Patricia Miranda

In a context of multiple crises, Special Drawing Rights (SDRs) are an important alternative for financing within the international monetary system, as they can generate new resources without increasing debt levels.

Countries of the Global South can use SDRs to contribute to achieving Sustainable Development Goals (SDGs) and the adaptation goals of the climate agenda through a wide range of operations, such as strengthening international reserves, repaying public debt and reducing fiscal space gaps.

Another allocation or frequent allocations of SDRs for at least five years, which aim to benefit countries that are more exposed to economic, social and climate vulnerabilities, could make a difference for millions of people. A fair distribution not linked to quotas could avoid recycling processes through new lending, thus preserving the no-debt creation spirit of SDRs.

In the short term, a change in the Balance of Payments manual would allow developed countries to rechannel unused SDRs to developing countries as grants rather than loans.

Access to fair financing that does not contribute to the debt spiral requires a reform of the International Financial Architecture that includes SDRs as a source of liquidity.

What are Special ghts (SDRs)?

Special Drawing Rights (SDRs) are an international reserve asset, created by the International Monetary Fund (IMF) in 1969 to supplement its member states' official reserves.[1]

SDRs have been created and used historically to enhance international reserves, access more financing, increase foreign investment and contribute to the stability of the purchasing power of a national currency.[2]

SDRs were created to meet liquidity needs and supplement the official reserves of member states with balance of payments crises due to a lack of US dollars and gold, which were the main assets held in foreign exchange reserves in 1969.

The value of an SDR is defined from a weighted-average basket of currencies, which has changed over time and currently includes the US dollar, Euro, British pound, Chinese yuan and Japanese yen.

1 See IMF website: https://www.imf.org/en/Topics/special-drawing-right

2 Arauz (2021).

As an international reserve asset, SDRs represent a potential claim on currencies issued by member countries and are exchangeable in official international transactions between member countries and prescribed holders.[3]

At the same time, SDRs are a unit of account that is officially used by the IMF for transactions with its members, as well as by other financial institutions and international organizations. IMF's lending amounts and transfers can also be nominated in SDRs.[4] Holders can exchange its SDRs into hard currencies with other IMF members. They can use their SDRs in a range of operations with other countries or to settle financial obligations to the IMF.

SDRs do not need to be repaid by recipient countries as they are not a credit or loan, and they do not include conditionalities, in contrast to regular IMF programmes. When a country's actual SDR holdings are lower than the amount of SDRs allocated to it, due to the active use of a portion of its SDRs, it must pay the SDR interest rate applied to the difference between the two amounts.

Conversely, when a country's holdings are higher than the amount allocated, after having received SDRs through a transaction with another country, then that country receives payments corresponding to the SDR rate applied to the difference between the two amounts. The cost of active utilization corresponds to this net interest payment. Interest rates vary and are calculated according to the interest rates of the SDR currency basket. As of August 2024, the SDR interest rate is 3.98 per cent, which is lower than interest rates in international markets.

SDR allocations

SDRs were issued for the first time from 1970-1972 with yearly instalments that reached SDR 9.3 billion. The second issuance in 1979-81 totalled SDR 12.1 billion, bringing total cumulative allocations to SDR 21.4 billion. After that, SDR issuances only reappeared almost three decades later, when a third general allocation took place in 2009, for SDR 161.2 billion, in response to the global financial crisis. This was equivalent to US$ 250 billion.

The last allocation was approved in August 2021, in response to the fiscal emergency caused by the outbreak of the COVID-19 pandemic. This was for a record sum of 456.5 billion SDRs (US$ 650 billion). This has been the largest allocation and, despite being approved 17 months after the COVID-19 outbreak, it was useful in the context of a health crisis where fiscal needs were urgent, in particular for the most vulnerable countries in the Global South. This allocation was one of the main global economic policies that also benefited middle-income countries. In the case of Latin America, the limited fiscal space and deficit registered for several years needed urgent resources without increasing debt.[5]

Allocations are credited to each country's SDR account in the IMF's SDR department. Each of the IMF's 190 member states receive an amount of these reserve assets, according to the proportion of its quota. As the IMF quota is based broadly on a country's relative position in the world economy, the richest economies received 61.4 percent of the allocation. The richest G7 countries alone received 47.2 percent.

Different groups of countries asked for SDRs issuance after the pandemic. African leaders called for additional SDRs for pandemic recovery in 2021[6] and a

3 Prescribed holders are the following official entities approved by the IMF to hold SDRs: African Development Bank (AfDB), African Development Fund (ADF), Arab Monetary Fund (AMF), Asian Development Bank (ADB), Bank for International Settlements (BIS), Bank of Central African States (BEAC), Caribbean Development Bank (CDB), Central Bank of West African States (BCEAO), Development Bank of Latin America (CAF), Eastern Caribbean Central Bank (ECCB), European Central Bank (ECB), European Bank for Reconstruction and Development (EBRD), European Investment Bank (EIB), Inter-American Development Bank (IADB), International Bank for Reconstruction and Development (IBRD), International Development Association (IDA), International Fund for Agricultural Development (IFAD), Islamic Development Bank (IsDB), Latin American Reserve Fund (FLAR) and the Nordic Investment Bank (NIB).

4 XDR is the code standardised for the SDR as a unit account.

5 Miranda (2020).

6 https://african.business/2021/09/economy/unga-african-leaders-call-for-additional-imf-sdrs-for-pandemic-recovery

multilateral financial system reform with new SDR issuances in 2023.[7] Latin American leaders in the Community of Latin American and Caribbean States (CELAC) 2021 declaration called for SDR allocation to access liquidity for developing countries, including middle-income countries.[8] Also in 2021, civil society organisations (CSOs) called on the G20 to urgently support a new allocation of SDRs to the tune of US$ 3 trillion.[9]

Fiscal use of SDRs

In the 2009 special allocation, SDRs were no longer reserved for meeting external needs, but were also used as an instrument of fiscal support, which further enhanced their positive impact. Eighteen countries used more than 50 percent of the allocation received. In Latin America, Ecuador was the first country to use SDRs for fiscal support.

After the last allocation, in 2021, SDRs have been widely used in the Global South, where a limited fiscal space led countries to draw on them for fiscal purposes instead of increasing public debt.

SDRs can be used for fiscal purposes. This varies according to domestic laws and sovereign decisions on their use within each country. The following are some of the main paths for this purpose:[10]

- **SDRs belong to the member state, not the central bank:** To apply this modality, the ministry of finance, prior to receiving the issued SDRs, needs to officially notify the central bank that SDRs should be credited, upon arrival, in favour of the ministry. The corresponding accounting and financial procedures should be executed by the central bank.

  A central bank is generally the fiscal agent of the state. In other words, it is the bank where the finance ministry manages its resources. This does not mean that the central bank substitutes the state or the finance ministry.

- **Exchange Stabilization Fund SDR Certificates:** Under this modality, ministries of finance issue SDR certificates to be acquired by the central bank. Therefore, the ministry could have liquidity from the central bank denominated in foreign or local currency to carry out budget expenses. In this scenario, the original SDRs are not exchanged abroad. Depending on the national monetary laws, this path will most likely need a legal reform or legal interpretation.

  In other words, the establishment of a fiscal or parafiscal instrument is identical to the Exchange Stabilization Fund (ESF) of the US Department of the Treasury. Once the SDRs are received, the ESF issues securities denominated in SDRs, called 'SDR certificates'. The ESF sells these securities to the Federal Reserve Bank of New York (NY Fed). Following this transaction, the ESF receives dollars in its account at the NY Fed and the NY Fed remains the holder of the SDR certificates.

- **Dividend based on extraordinary income:** According to current monetary laws, a central bank's profits at the end of the year are transferred to the country's ministry of finance given that, in the vast majority of cases, the central banks are entirely state owned. Therefore, after SDRs are credited, the significant increase in the equity of the central bank would make this transfer to the ministry of finance possible. If the national central bank insists on an incorrect but common legal argument, the SDRs are assets and the exclusive property of the central bank and not of the state.

  Considering the current crisis reflects more a fiscal problem than a balance of payments problem in most countries, this path could be feasible for several countries.

7 https://media.africaclimatesummit.org/Final+declaration+1709-English.pdf?request-content-type=%22application/force-download
8 https://www.gob.mx/cms/uploads/attachment/file/668541/Celac_2021_Declaracio_n_de_la_Ciudad_de_Me_xico__18sep21.pdf
9 https://latindadd.org/arquitectura-financiera/civil-society-organizations-call-for-quick-special-drawing-rights-allocation/
10 Arauz (2021).

- **Monetary financing:** This path is an alternative in case the central bank refuses to recognize that SDRs are the property of the state and that it would not be willing to record them as income in its budget. This scenario is almost implausible, but in central banks with a tradition of misunderstanding autonomy, or at the suggestion of certain external entities, it is unfortunately possible.

  It consists of financing from the central bank to the finance ministry through commonly used monetary financing mechanisms; central banks can purchase securities issued by ministries of finance. In this case, the central bank would receive the SDRs on the asset side of its balance sheet and increase its equity. The central bank would then buy securities from the finance ministry in dollars or in the national currency for the amount equivalent to the SDRs received. The combination of these transactions would increase the international reserves and also increase the internal assets of the central bank. The finance ministry would have an intra-sectoral domestic debt with the central bank. Since SDRs are indefinite, the debt between the finance ministry and the central bank could also be indefinite. Interest rates on those funds should not be more onerous than charges by the SDR department.

Figure 1:

Active use rates of 2021 SDR allocation by IMF, according to geographic grouping

Estimated active use during the two following years after the SDR issuance, between August 2021 and August 2023

Geographic grouping	Countries with at least 1 use	Used to obtain foreign currency or IMF payments	Used for fiscal support*
Total (95 of 190)	50 %	5 %	12,8 %
Advanced Economies (1 of 36)	2,8 %	0,5 %	0 %
Emerging and Developing Economics (94 of 154)	61 %	12,2 %	33,2 %
Sub-Saharan Africa (41 of 45)	91 %	34,8 %	80,5 %
Latin America and the Caribbean (19 of 32)	59,4 %	14,3 %	42,7 %
Emerging and Developing Economies Asia (14 of 30)	46,7 %	1,6 %	25,3 %
Emerging and Developing Economies Europe (7 of 16)	43,8 %	11 %	5,4 %
Middle East and Central Asia (13 of 31)	41,9 %	18,4 %	38,6 %

Source: Arauz (2023).
Note: (*) SDR use is expressed as percentage of SDRs allocated to the corresponding grouping.

The active use of SDRs is reflected in the fact that 61 percent of emerging market and developing economies used SDRs from 2021 to 2023. The regions that used more SDRs were sub-Saharan Africa, with 91 percent, and Latin America and the Caribbean, with almost 60 percent. In both cases, the main use was for fiscal purposes.

Some concrete examples of the use of SDRs in Latin American countries include:

Argentina: The SDRs were registered in a special account at the Central Bank of the Argentinean Republic (BCRA) to be exclusively used in accordance with the decisions of the Ministry of Economy. They were then recorded as a liability for the central bank and, following the principle of double-entry accounting, they were recorded in the BCRA's assets as reserves.

Subsequently, the Ministry of Economy instructed the central bank to pay external debt obligations with the IMF, during the agreement renegotiation with this institution. To this end, the operation consisted of issuing treasury securities as backup to request funds from the central bank to meet the government's liquidity requirements.

Argentina used SDRs creatively to repay debt to the IMF, reduced the need to cover the fiscal deficit with a monetary issuance or domestic debt (Treasury bills) between the ministry of finance and the central bank, and recovered the central bank's reserve level to sustain economic activity and imports of essential goods and services.

Ecuador: The SDRs were directly allocated to the balance of the Ministry of Economy and Finance (MEF) with the aim of using them for fiscal purposes and to increase reserves. Operationally, SDRs were allocated to the central government, recording them as a deposit in the Single Treasury Account (CUT) on assets, and as an increase in external debt with the IMF on liabilities.

Simultaneously, the Central Bank of Ecuador (BCE) registered an increase in international reserves in assets and an increase in deposits in the CUT in liabilities. The government was able to use these resources, for which a Memorandum of Understanding was signed between the MEF and the BCE. It stipulated that they would be used for international payment needs and for fiscal purposes. The main use of SDRs contributed to strengthening reserves and reducing fiscal space in the public budget.

Paraguay: Prior to receiving SDRs, the Paraguayan Congress approved Law 6809/21, which established measures to finance expenses related to the COVID-19 pandemic. However, these resources were prohibited from financing salary expenses, except those for health personnel. As established by law, SDRs were allocated to the Public Treasury Account as a financial asset through an inter-institutional agreement between the Ministry of Finance (MH) and the Central Bank of Paraguay (BCP).

In accordance with the law, the BCP granted an advance to the state, with no interest and on the condition that they should be amortized and cancelled after the effective SDR allocation, within fiscal year 2022. Regarding allocated SDRs, these were exchanged for dollars and credited to the MH account.

SDR allocation helped to temporarily expand social protection and to alleviate the deficit in the health system with coverage of medicines and outsourced medical care.

The law stipulated that the resources should be used to guarantee social safety nets for the most vulnerable populations, such as the elderly, as well as to guarantee food security for those most affected by the measures adopted within the framework of the Declaration of National Emergency due to the Pandemic.

The resources were allocated with their own code (Source of Financing 818 – Law 6809/21 of Economic Consolidation), which allowed their identification in the budget reports and, in this way, to monitor the use of SDRs once incorporated into the public budget. In total, because of Law 6809/21, a total of US$ 261 million was budgeted, of which some US$ 234 million (89.8 percent of the total) was used.

These cases show that SDRs can be used for fiscal purposes, helping to increase fiscal space while reducing the need to implement austerity measures.

Policy recommendations

SDRs are allocated following a global crisis where countries need immediate access to liquidity. However, as we face future crises – or more immediately, the current climate crisis – the key question is to what extent SDRs could contribute to prevention or serve as part of a more just and timely solution.

Key reforms in the international monetary system through SDR allocations

In the context of multiple crises, implementing structural reforms in the international monetary system is highly relevant.

Urgent responses to the climate crisis, energy transition risks as well as other urgent priorities such as global poverty and hunger are being hindered by mounting debt levels in countries of the Global South. The issuance of SDRs presents an exceptional opportunity to generate liquidity and resources without increasing these countries' debt levels.

Nevertheless, the current SDR system reproduces inequalities by being deployed during a global crisis. Key reforms would be crucial for SDRs to contribute under a fair financing approach. De-linking the quota-based distribution of SDRs would allow countries in need to have access to more liquidity. This reform would need a change in the IMF Articles of Agreement.

This proposal aims to achieve a more targeted and effective distribution to prioritize countries that are exposed to more vulnerabilities. Initiatives such as a 'development link' allows for a more progressive allocation of SDRs.

At the UN Climate Summit in Glasgow in 2021, the Prime Minister of Barbados, Mia Mottley, called for US$ 500 billion in annual issuance of SDRs to finance a transition to renewable energy and to limit the rise in global temperatures.[11]

The issuance of new SDRs remains a powerful alternative to conventional financing mechanisms. A different criterion of allocation for annual issuances for the next five years would make a real difference, based on countries' needs, such as the vulnerabilities they are exposed to.

Nonetheless, SDRs are a reserve asset and developed countries prioritise to maintain this condition. Different distribution criteria through vulnerability ratios would deliver a more focused benefit. Developed countries have a moral responsibility to increase efforts to provide fair financing without increasing the debt of the most vulnerable countries.

Recycling unused SDRs held by rich countries

As expected, SDRs allocated to rich countries were not used and rechannelling, or recycling, was discussed from the beginning as an option to balance the unequal distribution and to provide an important boost for countries in need.

Since 2021, that is exactly what has happened. The G20 and other economically stronger member states have voluntarily pledged more than US$ 100 billion of these reserves.

The initial option was rechannelling through IMF loans, under the traditional Poverty Reduction and Growth Trust (PRGT).[12] A new IMF trust fund was also set up, the Resilience and Sustainability Trust (RST)[13], which aimed to tackle long-term challenges such as climate change, digitalization and health. The RST makes it possible to rechannel SDRs to middle-income countries. It involves loans under IMF programmes, which include conditionalities.

Since 2021, 30 providing countries channelled about US$ 55 billion for the PRGT with 56 beneficiary countries. The RST had 23 partners that channelled about US$ 47 billion.[14]

According to Arauz, the quantity of allocated SDRs held by rich countries is so large that the transfer of about a quarter of them would make it possible to repay and cancel the entire debt of all countries in the world to the IMF and its trusts.[15]

11 https://www.reuters.com/markets/us/barbados-mottley-says-imf-must-help-finance-fight-against-climate-change-2021-12-03/
12 IMF website: https://www.imf.org/en/Topics/PRGT
13 IMF website: https://www.imf.org/en/Topics/Resilience-and-Sustainability-Trust
14 IMF website: https://www.imf.org/en/Topics/special-drawing-right#SDR%20Channeling
15 Arauz (2023).

In May 2024, the IMF Executive Board authorized the use of SDRs by IMF members for the acquisition of hybrid capital instruments[16] issued by prescribed holders, based on a proposal of the African Development Bank and the Inter-American Development Bank. The new SDR use will be subject to a cumulative limit of SDR 15 billion and a review is expected to be conducted when cumulative hybrid capital contributions surpass SDR 10 billion or two years after the authorization, whichever comes first. Nevertheless, this option still faces the restrictions of EU member states, which will not be able to be a contributor due to European Central Bank rules. Rechannelling efforts have been limited so far, especially by the claims that SDRs are a reserve asset. However, rechannelling SDRs as grants is more desirable, to avoid contributing to the vicious cycle of debt. In most rich countries that could potentially act as SDR donors, these assets are featured on the balance sheets of their respective central banks. Central banks currently follow the convention of recording their holdings of SDRs as reserve assets and the allocation of SDRs as reserve liabilities.

Based on a report by the non-governmental organisation LATINDADD and the Centre for Economic Policy Research (CEPR),[17] an innovative proposal for recycling SDRs through grants instead of loans is the change in the accountancy registry of SDRs in central banks, through a change of the Balance of Payments Manual (BoP) rules. The BoP Manual 5[18] states that SDRs are registered as equity and assets in the balance sheet of central banks, and the BoP Manual 6[19] states that SDRs are registered as liabilities and assets.

In the first case – under the old rules – if a rich country wanted to donate its SDRs, it would imply a reduction in assets and an increase in equity. In the second case – under the current rules – a donation implies a reduction in assets without a reduction in liabilities. Therefore there is a gap in equity, and this is the main concern for central banks whose currency is part of the SDRs basket.

In terms of central bank accounting, this difference would imply that a subsequent donation from rich countries, after an SDR allocation, would increase a central bank's equity (in net terms) without involving any balance sheet imbalances, i.e. a donation with no negative (net) impact on a central bank's net worth.

Under this proposal, rich countries would be able to rechannel SDRs through donations instead of loans, without facing the problem of negative gaps in their central banks' balance sheet. This would be more congruent with the spirit of SDR issuances, but would also be key to stop feeding a debt spiral for countries of the Global South.

This kind of change needs a review of the political economy of IMF statistical standards and the Balance of Payment Manual rules, both of which are feasible with dialogue and decision-making between IMF country members.

16 A hybrid capital instrument is a financial instrument with perpetual maturity that has both equity and debt properties.

17 Arauz (2023).

18 https://www.imf.org/en/Publications/Books/Issues/2016/12/30/Balance-of-Payments-Manual-157

19 https://www.imf.org/external/pubs/ft/bop/2007/bopman6.htm

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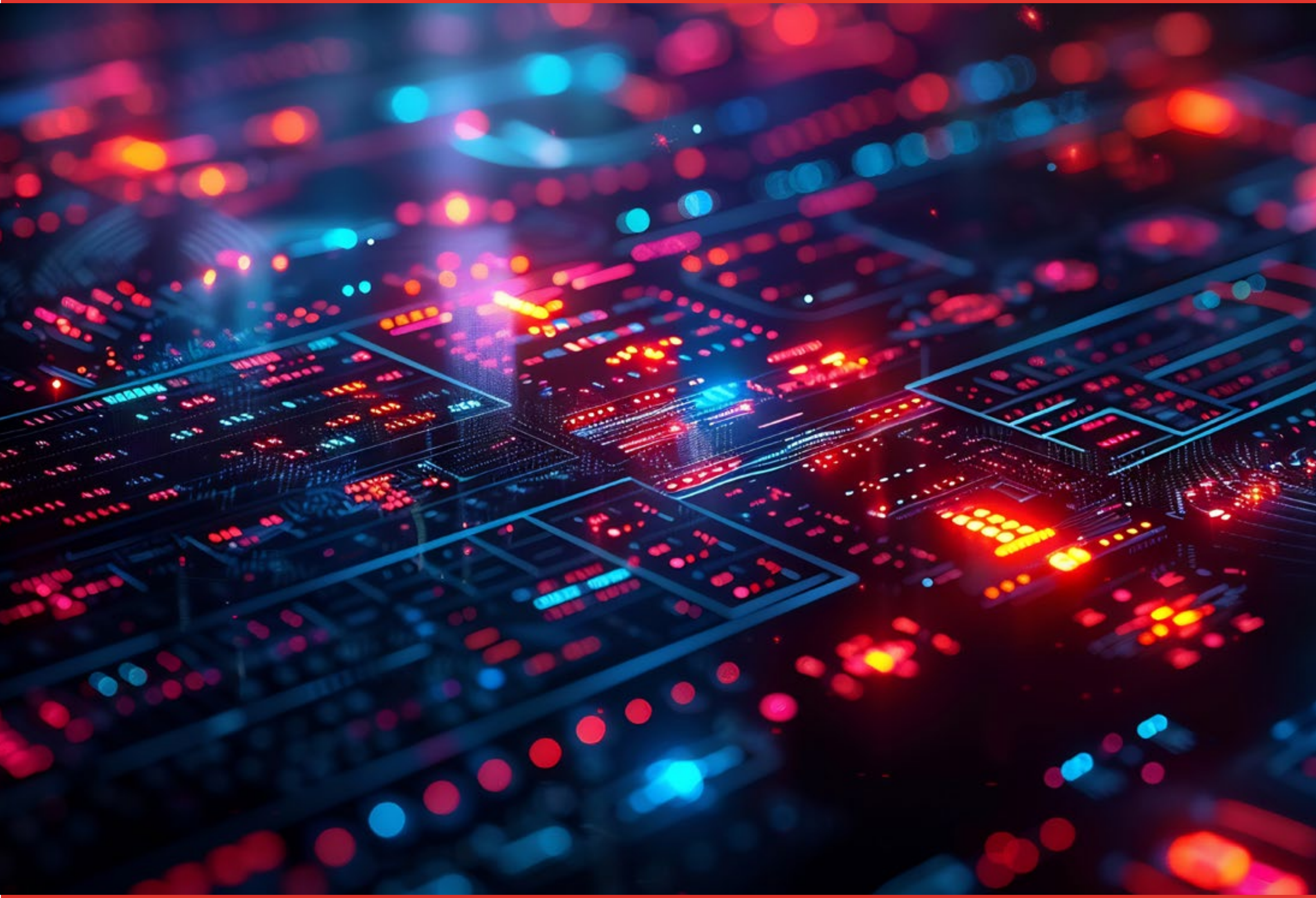
Affordable finance



Affordable finance: How to cancel the hidden expenses of risk premiums for states and private actors

By Oliver Pahnecke and Juan Pablo Bohoslavsky

The global debt burden has reached unprecedented levels.[1] Over 20 years, global public debt has quadrupled, while global Gross Domestic Product (GDP) only tripled.[2] In January 2024, six developing countries had country risk premiums above 20 percent;[3] 39 percent of developing countries make net interest rate payments exceeding 10 percent of total public revenue. Only 14.8 percent of these countries have an investment-grade credit rating.[4] Global debt has been unsustainable for decades but what if there was one mechanism in the International Financial Architecture that is largely responsible for this lack of debt sustainability? What if this mechanism could be corrected to make – to a great extent – the international financial architecture more resilient and lending more affordable? For 30 years lending uses weighted risk, adding risk premiums to the interest rates of loans. In this system, the risk premium can replace collateral and protects the lender's principal.[5] If the risk premium were legally treated as a collateral sui generis, loans could become significantly cheaper because risk premiums would have to be returned after full repayment, or adjusted over time, in accordance with the real default risk. This article analyses the cost of today's risk premium system for States and their citizens' human rights.

Risk premiums in the International Financial Architecture

Before we can analyse the impact of risk premiums on sovereign finance and human rights, we need to understand how risk premiums work and how they are threatening the current International Financial Architecture (IFA).

1) How risk premiums work

In 1974, central bank governors founded the Basel Committee "to enhance financial stability by improving the quality of banking supervision worldwide".[6] Its work led to the introduction of weighted risk in the 1990s to make risk internationally comparable.[7] Weighted interest rates consist of the prime rate – the basic interest rate available for short-term loans to riskless clients, which is the price for the loan – and a risk premium added on top that reflects the borrower's default risk. In cases of poor collateral, the risk premiums in interest rates will be high, while they will be low in cases of good collateral. This shows risk premiums and collateral can be exchanged, meaning they basically have the same function.[8] This argument is supported by the fact that these interest rates,

1 Tiftik/Mahmood/Aycock (2024).
2 UN Global Crisis Response Group (2023), p. 5.
3 Damodaran (2024).
4 UNDP (2024).
5 Pahnecke/Bohoslavsky (2021).
6 Bank for International Settlements, History of the Basel Committee (https://www.bis.org/bcbs/history.htm).
7 Ibid.
8 Pahnecke/Bohoslavsky (2021), p. 18.

which were increased by risk premiums, accelerate the repayment of the principal because then the compounding takes place at a higher rate than before.[9] Accelerated repayments protect the lender's principal in absence of (good) collateral. Since risk premiums can be replaced by conventional collateral, and because they protect the lender's principal, the risk premium has to be understood as a collateral *sui generis*.[10] Accordingly, risk premiums remain the property of borrowers and should either be returned at the end of the loan contract or adjusted over time in accordance with the real risk, just like any other collateral. That way a risky borrower would end up paying the same price for the loan as a low-risk borrower that has a low risk premium due to collateral.

However, current financial practice regards risk premiums chiefly as the price for risk, but also as an insurance or as a means for cross-financing risk among different borrowers. The risk premium cannot be an insurance premium, though, because there is no insurer involved and the finance industry uses other means to hedge risk. According to the Federal Reserve, the risk premium is also not used to cross-finance the risk between borrowers, because this would undermine market discipline on the individual borrower.[11] Most importantly, different prices for the same product based on the clients' financial status and without justification would be discriminatory. Discriminatory pricing would collide with anti-discrimination law, with deep roots in both national constitutional law and international human rights law.[12]

Different prices can be justified only at the beginning of a loan contract since the riskier client will repay the principal to the lender with the help of the risk premium at an earlier point than without. But over time the default risk diminishes with each instalment until the full principal is paid by the borrower. In this moment, the default risk related to the lender's investment – the principal – drops to zero. From now on, the different prices are not justified any longer. To avoid discriminatory pricing, the risk premium could therefore be repaid at the end of the loan contract. Preferably, however, the risk premium should be adjusted over time, in accordance with the real default risk until all clients end up with paying the same price.[13]

It follows that the actual function of the risk premium is indeed the protection of the lender's investment, the principal. As a means to offset risk, it serves as a collateral *sui generis*. Consequently, the risk premium cannot be a price for risk, either.

What looked like – and still is – a practical and smart tool to make loans available for clients with little or no collateral turned into a faultline in the IFA because the Basel Accords confuse price, collateral and property.

Risk premiums as collateral *sui generis* remain the property of the borrowers, as long as there is no default, because collateral is the property that a borrower puts up as security for the lender's payment claim against them.

Interest rates, on the other hand, are the market-driven price for the loan and therefore are not yet the property of the lender. This means that interest rates cannot enjoy the same protection as property. However, because of the Basel Accords, interest rates and risk premiums are treated as if they were the property of the lender, although the only property of the lender that exists in the context of lending is the principal. Only the principal has already been legally acquired and therefore it is protected by constitutions and international treaties as property.

This current practice affects anybody that is not a low-risk prime rate client, and therefore, without justification, targets a large group of people charac-

9 Ibid p. 19-20.

10 "Sui generis" is a Latin term used in law to describe something "unique" or "of its own kind".

11 Ibid p. 16.

12 Ibid p. 23ff and 31ff.

13 Ibid p. 23–29.

terized by their social status and their financial background.[14]

2) Why risk premiums pose a threat to the IFA

Risk premiums would constitute a threat to the current IFA if they increased the counterparty default risk significantly at an international level. If the risk premium caused such a faultline in the IFA, it would counteract the aims of Basel I, which would then need to be amended.

If the risk premium is a replacement for collateral, it belongs to the borrower. From this, it follows that the lender has no legal claim to keep the risk premium once the borrower has fulfilled their contractual duties, which would mean returning the principal and paying the interest. In practice however, the risk premiums are accounted for as if they were the property of the lender. This confusion has far-reaching implications.

Firstly, the price discovery for risk does not work because the natural price for risk would have to be lower if the risk premium had to be returned or adjusted in accordance with the real risk.

Just as problematic for the economy is the silent absorption of the risk premiums by the lenders, although this money should be returned to the borrowers. This mechanism works like an expropriation of all borrowers who are riskier than prime rate clients, based on the wrong assumption that weighted interest rates are a price for risk. If lenders were to keep conventional collateral, such as real estate, which is offered instead of a risk premium, the disproportionality of this flawed practice would become more obvious.

A third problem is derived from paragraph 61 of the Basel Accord III. Based on this, lenders are required to make adjustments in their management of counterparty risk at least every three months, or more frequently if conditions require it.[15] In practice this means that lenders will have fewer expenses for risk management if their risk decreases, but they do not pass these savings on to their clients since borrowers are treated as if they posed the same risk over the whole duration of the contract, although in fact the risk decreases over time with each payment.[16] This also means that lenders are already obliged to collect the data that is necessary to adjust the risk premium in accordance with the real risk to prevent discriminatory pricing. However, the Basel Accords neither demand that lenders pass on the savings that are based on reduced risk management expenses, nor do they require an adjustment of the risk premiums. Instead of funnelling risk premiums and cost savings from clients to lenders, the Basel Accords should be adjusted to reflect the definition of property. This would limit legal protection to the principal and distinguish price from property and collateral.[17]

Another grave problem appears to be that conventional collateral depreciates because of wear and tear. Risk premiums, on the other hand, grow exponentially due to compound interest.[18] This means the risk premium is more attractive for a lender since it grows over time, compared to conventional collateral, which loses value. Additionally, riskier clients are forced to pay far higher risk premiums than prime rate clients, who can offer excellent collateral and therefore only pay for minimum risk. Because of this, the motto seems to have become “the riskier, the better” for some lenders.

Imprudent lending is also facilitated by the fact that, in boom times, it is easy to sell claims against lenders that might face distress. However, in times of crises, the advantage of high-yielding risk premiums turns into the opposite, when everybody is trying to sell the loans of distressed borrowers. This results in plummeting prices and lenders will expect bailouts by the State, especially once they pose a high risk to the

14 For the legal aspects of discrimination based on property, see Pahnecke/Bohoslavsky (2021), pp. 31–42.

15 Basel Committee on Banking Supervision (2011), II. A. 1. 98. §§ 25(i) & 61, pp. 30–31.

16 Pahnecke/Bohoslavsky (2021), p. 31.

17 Ibid p. 43.

18 Ibid p. 20.

economy. Mario Draghi wrote that such “distorted incentive structures that induce borrowers and/or lenders to engage in risky financial behaviour, or inadequately monitor the risks they assume, in the expectation that they will be insulated from the adverse consequences of their activities by the public authorities” are a “moral hazard”.[19]

If lenders can count on help in the form of bailouts, bail-ins or other measures – instead of facing accountability through market discipline – there is no limit to risk. The larger the default risk that one or several lenders face, the bigger the risk for a collapse of the entire IFA. With this in mind, Mario Draghi, Jürgen Stark, Mervyn Allister King and Larry Summers have demanded that “expectations that large-scale official financing packages will be available to meet debt service obligations to the private sector” are discouraged.[20]

Today’s price-for-risk-practice also increases the risk in the financial system and for the lender in another way: Prime rate clients pay only the basic interest rate and almost no additional price for risk but provide excellent conventional collateral. Such borrowers only put up something valuable to secure the lender’s claim in case of a default and therefore the total risk in the financial system does not increase. In contrast, risky borrowers pay the basic interest rate and the risk premium on top. But if a client already has fewer funds for economic activity, increasing payment obligations will increase the counterparty risk for the lender because the borrowers’ default becomes more likely the more they have to pay. The higher the financial burden, the higher the default risk. Depending on how many lenders will default, the risk can spread within the financial system.

It becomes clear that risk-weighted interest rates place a higher burden on riskier clients than riskless clients by accelerating the repayment of the principal. While this acceleration is necessary to protect the lender’s principal, it gives the riskless clients a cost advantage because they can use the principal for a longer period of time. Should the riskless and the risky borrower compete in the same business, the riskier borrower might have to ask for higher prices per unit to pay the higher redemption payments. In turn, the principal remains with the riskless client for a longer period of time due to lower redemption payments, making lower prices possible.

The fact that the Basel Accords treat principal, interest and risk premium as if they were all the property of the lender establishes a mechanism that increases counterparty risk, distorts price discovery and expropriates those of lesser economic capacity. This mechanism also affects the market negatively, as lenders are misled into imprudent risky lending for higher yields, while betting on bailouts and thus causing moral hazard. However, the opposite is likely to happen if the risk premiums were treated as collateral *sui generis* in accordance with their actual function in the loan.

Because of that, the current practice increases counterparty risk internationally, creating a faultline in the IFA. Once the risk premium is treated as collateral, that money will remain with the borrowers, instead of enriching lenders without consideration.[21] While this means a reduction of the windfall profits in the short term, lenders will benefit from the reduced default risk in the long term. However, for a reform that serves all market participants, regulators will have to minimize the bankruptcy risk among lenders. Since the debt burden is becoming increasingly unsustainable and the financial system is becoming more and more fragile, a reform of the Basel Accords is urgently required.

The impact of risk premiums on sovereign finance and human rights

Risk premiums apply to all forms of loans and therefore most borrowers are affected – private individuals, corporations and States alike. This begs the question whether it is possible to quantify how much borrowers pay in excess of the actual interest rates.

19 Draghi et al. (1996).

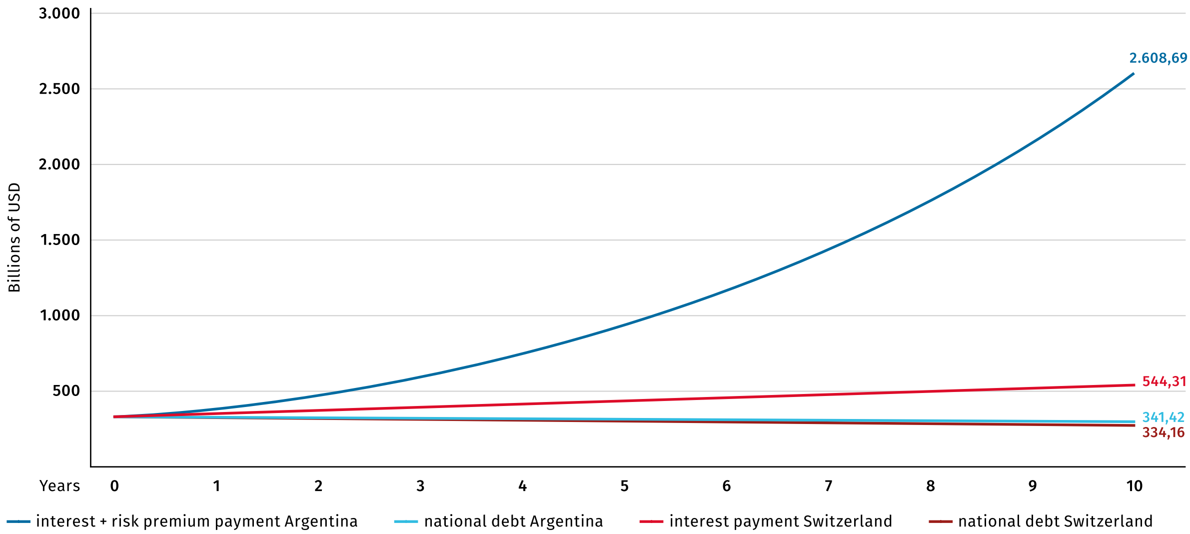
20 Ibid p. 5.

21 See the legal concepts of consideration in common law and the synallagmatic contract in civil law.

Based on calculations of the UN Global Crisis Response Group, a total of 3.3 billion people live in countries that spend more on interest payments than on either education or health.[22] As a concrete example, Argentina's national debt amounted to US$ 341.42 billion in 2023[23] and its country risk premium was 17.55 percent.[24] Switzerland's national debt was similar in 2023, US$ 334.16 billion[25] and in contrast, its country risk premium was 0.00 percent.[26] Both states have similar national debt levels, which makes a comparison of the risk premiums' effect possible if we treat the national debt as one loan over ten years and if we establish a fictitious prime rate of 5 percent. In such a scenario, a 17.55 percent risk premium applies to Argentina, which has to pay a total of US$ 1,719.948 billion after ten years.[27] If we subtract the initial "principal" of US$ 341.42 billion, then Argentina has to shoulder US$ 1,478.528 billion based on the risk premium. Together with the fictitious prime rate of 5 percent, Argentina faces 22.55 percent of compounded interest, which amounts to a total of US$ 2,608.688 billion after ten years.[28] Switzerland, on the other hand, does not incur any debt based on the risk premium over ten years, because the country risk premium is 0.00 percent. As a prime-rate client, Switzerland will pay a total US$ 544.311 billion after ten years.[29] In this case, the prime rate amounts to US$ 210.151 billion.[30] In comparison, Argentina pays US$ 2,608.688 billion after ten years, minus the principal, a total of US$ 2,267.268 billion caused by prime rate plus risk premium. Graph 1 illustrates the drastic difference in outcomes.

Figure 1:

Risk premium expenses: Argentina vs. Switzerland



22 UN Global Crisis Response Group (2024), p. 18.

23 Statista: National debt of Argentina from 2007 to 2029 (https://www.statista.com/statistics/1391782/national-debt-argentina/)

24 Damodaran (2024).

25 Statista: National debt of Switzerland from 2019 to 2029 (https://www.statista.com/statistics/531962/national-debt-of-switzerland/)

26 Damodaran (2024).

27 Duration n = 10 years, risk premium r = 17.55% and principal K_0 = 341.42 billion: K_n = K_10 = K_0*(1+r)^n=341.42 billion*(1.1755)^10 = 1,719.948 billion.

28 Conditions like fn 27, plus a prime rate p = 5%: K_10 = K_0*(1+p+r)^n = 341.42 billion *(1.2255)^10 = 2,608.688 billion.

29 K_10 = K_0*(1+p)^n = 334.16 billion *(1,05)^10 = 544.311 billion. Of course, 5 percent interest is for comparison only; in reality, public bonds of the Swiss Confederation pay interest rates of 0.5 to 1.5 percent and very rarely reach above 3 percent and their maximum of 4 percent. See: https://www.snb.ch/en/publications/financial-markets/gmdh/ch_bonds_res.

30 K_10 – K_0 = 544.311 billion – 334.16 billion = 210.151 billion.

The correlation of Argentina and Switzerland illustrates the drastic difference that riskier states face based on the risk premium, even if they manage to repay the loan just as successfully as a prime rate state with a comparable debt burden. The fulfilment of the right to development is becoming a distant prospect in Argentina with debt burdens like this.

This example clarifies the mechanism by which lenders obtain these funds, which replace collateral. The risk premiums appear to be a major factor for the lack of funds in the public and private sector, and contribute to persistent wealth inequality.[31] Although the country risk premiums are only market driven, they are at prohibitively high levels and actually increase the likelihood of defaults by placing the greatest burden on those with the lowest economic capacity. From the perspective of development, this is counterproductive.

In comparison, debt relief in the form of debt cancellation or from reducing interest rates, which has also been one of the proposals put forward by the United Nations Secretary General's Sustainable Development Goal Stimulus Package,[32] will help in the short term. However, it will not resolve the problem that is caused by the confusion of price and property. For States to fulfill their human rights obligations, debt relief must be the first step, followed by a comprehensive overhaul of the IFA.

Policy recommendations

Although the legal framework of the IFA seeks to facilitate international borrowing and lending in a stable environment, the international financial system has faultlines. Some of the mechanisms lead straight to an increase of debt, such as the International Monetary Fund (IMF) surcharges,[33] while others have been poorly understood, such as the risk premiums, which were instructed by the Basel Accords.

Therefore, policy recommendations need to address the formal and material aspects of IFA reforms:

The Basel Accords are implemented in the G20 Member States,[34] which means that the world's largest economies and most jurisdictions connected with them are obliged to use risk-weighted interest rates.[35] A G20 decision to treat risk premiums legally as collateral would therefore affect developed as well as developing countries immediately because it would release funds in their budgets for development and research, for example. In the specific case of risk premiums, it is necessary to:

1. Carry out further research on risk premiums and their effects on lenders and borrowers.
2. Amend the Basel Accords to treat risk premiums as collateral *sui generis*.
3. Introduce real-risk adjustments of risk premiums for the loans of development banks and other multilateral lenders, for bilateral loans and in the private sector.

International human rights law also calls for the correction of the Basel Accords and national laws so that property, price and collateral are treated adequately and that an adjustment of risk premiums over time, in accordance with the real risk, takes place. This is the only way to reduce interest rate-based discrimination. The Guiding Principles on Human Rights Impact Assessment of Economic Reforms, for example, demand that "[m]onetary policies should be coordinated and consistent with other policies with the aim of respecting, protecting and fulfilling human rights". Furthermore, "[f]inancial sector regulation is required to identify, prevent, manage and fairly allocate the human rights risks created by financial instability (…)" while "[d]ebt policies should be consistent

31 For example, in the USA the overall wealth has grown but the gaps remain, see Hernández Kent/Ricketts (2024).

32 UN Secretary-General (2023), pp. 3–5 and 15.

33 Bohoslavsky/Clérico/Cantamutto (2022).

34 Financial Stability Board (2019).

35 An up-to-date version of the Basel Framework and risk-based capital requirements is also available through the Bank for International Settlements. See https://www.bis.org/basel_framework/index.htm.

with broad goals related to sustainable economic development and the realization of human rights".[36]

Conclusion

As long as risk premiums are not adjusted to reflect diminishing risk over time, the financial economy remains skewed in favour of low-risk clients and lenders. This imbalance increases fragility due to imprudent lending and the excessive burden on borrowers from risk premiums that should only serve as collateral. Reforming the Basel Accords would therefore improve the situation for public and private actors alike.

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36 United Nations Human Rights Council (2019), in particular Principle 11 (c), (d) and (e), and 11.10.

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4

International Tax Cooperation

The UN Framework Convention on International Tax Cooperation: What do we want it to achieve?

By Chenai Mukumba

On 16 August 2024, United Nations (UN) Member States adopted the Ad Hoc Committee's Draft Terms of Reference (ToRs) for a UN Framework Convention on International Tax Cooperation by an overwhelming majority.[1] The ToRs were adopted after an arduous session – the third and last in a series of protracted negotiations.

The decision to convene the Ad Hoc Committee was made in 2023 after the UN General Assembly passed Resolution 78/230 on the promotion of inclusive and effective international tax cooperation. This historic resolution indicated that the General Assembly was to "establish a Member State-led, open-ended ad hoc intergovernmental committee for the purpose of drafting terms of reference for a United Nations framework convention on international tax cooperation."[2]

This article explores what led up to the proposal by the Africa Group and the concerns they have long sought to resolve through this convention.

Introduction

The historic vote on 16 August 2024 came almost a decade after the High Level Panel (HLP) on Illicit Financial Flows from Africa, which was chaired by former South African President Thabo Mbeki, called on Africa to step up efforts to ensure that the UN played a more prominent role in tacking illicit financial flows (IFFs).[3] In the early 2000s, there was growing literature documenting the impact of IFFs globally by various institutions and academics, such as Professor Leonce Ndikumana. As awareness around this issue started to grow, African leaders wanted to understand how much of an impact IFFs had on the African continent.

In 2011, at the 4th Joint African Union Commission/United Nations Economic Commission for Africa (AUC/ECA) Conference of African Ministers of Finance, Planning and Economic Development, Member States mandated the ECA to establish the High Level Panel on Illicit Financial Flows from Africa. Underlying this decision was the determination of African Member States to ensure that Africa's accelerated and sustained development relied as much as possible on its own resources.[4] The decision was also informed by the fact that it was clear that African countries were not going to meet the Millenium Development Goals by 2015. African Member States, therefore, asked the panel to develop a report that undertook the following:

- develop a realistic and accurate assessment of the volumes and sources of these outflows

1 https://financing.desa.un.org/sites/default/files/2024-08/Chair%27s%20proposal%20draft%20ToR_L.4_15%20Aug%202024____.pdf
2 https://financing.desa.un.org/sites/default/files/2024-01/A.RES_.78.230_English.pdf
3 UN Economic Commission for Africa (2015).
4 https://codafrica.org/wp-content/uploads/2020/10/The-Journey-So-Far.pdf

- gain concrete understanding of how these outflows occur in Africa, based on case studies of a sample of African countries and

- ensure specific recommendations of practical, realistic, short- to medium-term actions are taken both by Africa and by the rest of the world to effectively confront what is, in fact, a global challenge.[5]

The report was completed and published in 2015 and identified 15 different findings on IFFs, together with policy implications. One such finding was that, “Illicit financial flow issues should be incorporated and better coordinated under the United Nations processes and frameworks” and the “policy implication” drawn from that finding was as follows:

> “Africa needs to act in concert with its partners to ensure that the United Nations plays a more coherent and visible role in tackling IFFs. This involves ensuring that efforts to combat IFFs are included in the Post-2015 Development Agenda. Similarly, Africa needs to initiate steps for the United Nations to adopt a unified policy instrument on IFFs in order to place the matter squarely on the agenda of the world organisation.”[6]

Indeed, the HLP Report noted that the issue of IFFs was not firmly on the policy agenda of the UN system and urged more rigorous efforts in support of a unified global architecture on the issue of IFFs. Following this, the report and its recommendations were adopted by the African Union as Assembly Special Declaration on Illicit Financial Flows.[7] Paragraph 9 of the declaration noted that Member States were to:

> “Express the need to ensure that illicit financial flows and their impact on domestic resource mobilization is given the necessary attention by the 3rd International Conference on Financing for Development, and in this regard stress the need for robust international cooperation to address the problem.”[8]

Illicit financial flows were therefore a significant feature of the discussions at the 3rd International Conference on Financing for Development that was held in Addis Ababa, Ethiopia in July 2015. These conversations were subsequently reflected in the outcome – the Addis Ababa Action Agenda – which highlighted the importance of tackling multinational tax avoidance.[9] However, while the call for the establishment of a policy instrument was not adopted in the Addis Ababa Action Agenda, it did “call for more inclusiveness to ensure that these efforts [in international tax cooperation] benefit all countries”.[10]

Winds of change

Today’s global tax system is currently governed by the Organisation for Economic Co-operation and Development (OECD). It took over this role from the UN following the dissolution of the United Nations Fiscal Commission in 1946 when it suffered from a lack of support mostly from developed countries that did not see the need for a UN body to address tax issues.[11] Today, there are several institutions that play different roles within the international tax system. The G20, the International Monetary Fund (IMF) – through its Fiscal Affairs Department, the World Bank Group, the European Union and the Platform for Collaboration on Tax – a collaborative effort by the OECD, UN, IMF and World Bank.

The UN has also continued to play a role through the UN Committee of Experts on International Cooperation in Tax Matters, by largely reflecting the interests of developing countries in international tax discussions. Of all the institutions at play within the inter-

5 UN Economic Commission for Africa (2015), p. 2.
6 Ibid, p. 76.
7 AU Doc. Assembly/AU/17(XXIV) (https://au.int/sites/default/files/documents/29831-doc-assembly_declaration_on_illicit_financial_flow_-_english.pdf)
8 Ibid, para. 9.
9 UN General Assembly (2015).
10 Ibid, para. 28.
11 Owens/Ndubai (2021).

national tax system, however, the OECD is the most influential. While the OECD cannot impose binding rules or sanctions and rather depends on soft power mechanisms, it does wield significant influence over its actors. In addition, the OECD's recommendations are often considered as authoritative in the international tax field.[12]

As a result of the increasing call for more inclusive participation in the global rule-making of tax issues, the OECD established the OECD Inclusive Framework, which convened its inaugural meeting in 2016 in Kyoto, Japan.[13] This Inclusive Framework was established to allow for the increased participation of developing countries that were increasingly asking for a seat at the table when it came to making the rules. Despite the expansion of the number of countries that were now able to participate in rule-making, developing countries still raised concerns about the effectiveness of this participation.

In October 2020, the OECD proposed a Two-Pillar Solution to address the tax challenges arising from the digitalization of the economy. This proposal was part of the broader OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS). Under Pillar One, the Two-Pillar Solution sought to work on the reallocation of some taxing rights to market jurisdictions where multinational enterprises (MNEs) have users or consumers; and under Pillar Two, the proposal was to introduce a global minimum corporate tax rate to ensure that MNEs pay a minimum level of tax, regardless of where they operate. However, the African Tax Administration Forum, various civil society organizations and a number of developing countries thought the proposals fell far short of a solution that addressed the key tax issues facing Africa.

In December 2020, an Africa Union Briefing was published to inform the Extraordinary Specialised Technical Committee on Finance, Monetary Affairs, Economic Planning and Integration. It stated:

> "…developed countries are not listening to the concerns of developing countries and have no intention of redressing the balance of taxing rights in any significant way. Africa must mobilize itself at a political level if it is to change the stance of developed countries and address these key tax issues."[14]

Addressing the gaps

Led by Nigeria, the Africa Group kickstarted the process to overhaul global tax rule-making. In 2022, the group spearheaded the adoption of UN General Assembly Resolution 77/244 on "Promoting inclusive and effective international tax cooperation."[15] The resolution called on the UN Secretary-General to publish a report that served as an assessment of the current global tax landscape and to make recommendations on how to address the gaps.

Published as report A/78/235, the Secretary-General assessed the inclusiveness and effectiveness of current international tax cooperation considering both the substantive and procedural criteria of fully inclusive and more effective international tax cooperation.[16] The report flagged that:

> "the substantive rules developed through these OECD initiatives often do not adequately address the needs and priorities of developing countries and/or are beyond their capacities to implement."[17]

The report also highlighted that there was:

> "significant evidence showing that often the substantive guidance produced through these [OECD] processes […] is not implemented by developing countries. This is because they consider

12 Tychmańska (2021).

13 https://www.oecd.org/en/topics/policy-issues/base-erosion-and-profit-shifting-beps.html#:~:text=At%20its%20inaugural%20meeting%20in,jurisdictions%2C%20including%2014%20observer%20organisations

14 African Union (2020), p. 12.

15 https://documents.un.org/doc/undoc/gen/n23/004/48/pdf/n2300448.pdf

16 UN Secretary-General (2023).

17 Ibid, para. 47.

> that the guidance does not respond to their more immediate needs and priorities, and instead draws resources away from such issues, and/or that they are not capable of implementing it as a result of their tax administration capacities. The substantive aspect of inclusive and effective international tax cooperation does not, therefore, appear to be adequately met." [18]

It also added that:

> "In the publications produced by the Global Forum and the Inclusive Framework, it is consistently indicated that all members participate on 'an equal footing' in decision-making processes 'by consensus'. [...] In practice, however, it may be difficult for countries with small international tax staff to influence decision-making processes in these forums. In the case of the Inclusive Framework, a country is considered to agree to a proposal unless it raises an objection. It is not required to affirmatively 'opt-in' to be part of the consensus. Therefore, a country that cannot keep up with the pace of work and never expresses a view on a proposal is considered to agree to it." [19]

The Secretary-General's report also noted, however, that the UN did not have a sufficient platform either as the current tax committee was not fully representative. As a consequence, the Secretary-General's report proposed the establishment of a Member State-led, intergovernmental committee to "recommend actions on the options for strengthening the inclusiveness and effectiveness of international tax cooperation".[20] The report concluded by delineating three potential pathways for the reconfiguration of global tax governance, namely:

1. A multilateral convention on tax
2. A framework convention on international tax cooperation
3. A UN framework for international tax cooperation.

On behalf of the Africa Group, Nigeria proposed option two, noting that a "United Nations framework convention on international tax cooperation is needed in order to strengthen international tax cooperation and make it fully inclusive and more effective". General Assembly Resolution A/RES/78/230 was adopted in December 2023 – with 111 Member States voting in favour, 46 Member States voting against and 10 Member States abstaining.[21] All African countries and some Latin American and Asian countries – along with Russia and China – voted in favour of the resolution. Of note was that two-thirds of the members of the OECD Inclusive Framework voted in favour of the resolution, which demonstrated a shift in perspective regarding the OECD's leadership role on global tax rules.

What do we want it to achieve?

A question that is often asked is what does the Africa Group and supportive developing countries want to achieve through the UN Framework Convention? The background to the discussion on the UN Framework Convention identifies two clear issues. The first is inclusivity. Despite the repeated calls to make global tax rule-making more inclusive, it is far from surprising that developing countries are calling for a decision-making process that is more participatory. The objective of inclusivity is not an objective in and of itself, however. The primary reason why the Africa Group and developing countries are calling for inclusivity is to make the global tax system more effective. Evidence indicates an increase in IFFs over the years, as well an increase in the base erosion and profit shifting (BEPS).

The draft of the recently adopted Terms of Reference (ToRs) reflected this in the objectives of the convention that is to be deliberated from the year 2025 onwards:

18 Ibid, para. 41.
19 Ibid, para. 44.
20 Ibid, para. 67.
21 https://financing.desa.un.org/sites/default/files/2024-01/A.RES_.78.230_English.pdf

"a. Establish fully inclusive and effective international tax cooperation in terms of substance and process;

b. Establish a system of governance for international tax cooperation capable of responding to existing and future tax and tax-related challenges on an ongoing basis;

c. Establish an inclusive, fair, transparent, efficient, equitable, and effective international tax system for sustainable development, with a view to enhancing the legitimacy, certainty, resilience, and fairness of international tax rules, while addressing challenges to strengthening domestic resource mobilization." [22]

The draft ToRs were adopted on 16 August 2024 with 110 countries voting in favour.[23] While in 2022, 46 countries voted against Resolution 78/230, the negotiations of the ToRs saw only eight countries voting against the process, reflecting what one could call a shift in perspectives in favour of this process.

Where do we go from here?

At the beginning of 2025, an intergovernmental negotiating committee will be established and is due to meet in 2025, 2026 and 2027 for at least three sessions per year to develop the UN Framework Convention. It is expected to complete its work and submit the final text of the convention to the General Assembly for its consideration in the first quarter of the 82nd session in 2027. In addition to this, the intergovernmental committee is also expected to complete two early protocols that will also be submitted for early consideration. Discussion around the early protocols has already proved to be quite controversial, with various countries proposing a range of topics to be tackled by the committee. One of the points that proved to be difficult to navigate was whether the UN Framework Convention should tackle issues that have yet to be addressed as proposed by developed countries, or topics that have been addressed yet remain insufficient to address the concerns of developing countries.

Eventually, Member States agreed that one of the protocols would focus on "taxation of income derived from the provision of cross-border services in an increasingly digitalized and globalized economy".[24] However, due to the difficulty in agreeing on the second protocol, they indicated that the "[t]he subject of the second early protocol should be decided at the organizational session of the intergovernmental negotiating committee".[25]

While the proposal lists several topics, there is a hope from the African Group that this will include measures against tax-related illicit financial flows. Indeed, this was where the discussions started almost 10 years ago with the publication of the High Level Panel Report of Illicit Financial Flows.

As the Tax Justice Network Africa (TJNA), we fully support the work of the Africa Group and agree with their understanding that there is a need to establish a fully inclusive system of governance that the Framework Convention will address. The substantive component of the discussions will take place during the negotiations of the protocols. We are delighted to see that the topic of the digital economy has been prioritized and we would like to see the topic of tax-related IFFs adopted as the second early protocol. This topic was the primary reason the High Level Panel recommended the need to centralize the role of the UN on the topic of tax. The second topic that we hope will be prioritized is the fair allocation of taxing rights. This issue has been raised several times by developing countries during the negotiations and remains one that is central to African countries' ability to raise the domestic resources required to support the attainment of its developmental objectives.

22 https://financing.desa.un.org/sites/default/files/2024-08/Chair%27s%20proposal%20draft%20ToR_L.4_15%20Aug%202024____.pdf

23 https://news.un.org/en/story/2024/08/1153301

24 Ibid, para. 15.

25 Ibid, para. 16.

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5

Climate finance architecture

A climate finance architecture fit for achieving the new collective quantified goal

By Avantika Goswami and Sehr Raheja

2024 is the year of climate finance. At the Conference of the Parties 29 (COP29) in Baku, Azerbaijan, Parties to the United Nations Framework Convention on Climate Change (UNFCCC) are expected to determine a new climate finance goal. The New Collective Quantified Goal (NCQG) on climate finance is due to come into force from 2025. It is expected to be a goal that reflects the needs and priorities of developing countries, to catalyze climate action.

Although the NCQG will be an outcome of the multilateral UNFCCC process, it is situated within the broader context of the global financial system and finance architecture. Thus, to arrive at a goal that is fit for purpose and serves the needs of developing countries, it is crucial for the landscape of international finance to support its implementation. This chapter outlines the key markers that could characterize a climate finance structure capable of supporting the achievement of the NCQG.

A moral imperative

One estimate by Indian economist Utsa Patnaik finds that, over a period of 200 years, the British government may have siphoned about US$ 45 trillion out of India, which is roughly 15 times higher than the annual Gross Domestic Product (GDP) in the United Kingdom (UK) today.[1] The economic impacts of colonization stalled India's development for decades, the effects of which are likely being felt even today. India is still a growing economy and is notably better off than many of its neighbours in the Global South, but it is still working to achieve prosperity for all its citizens. Roughly 30 million Indians do not have access to electricity, and 780 million people lack access to clean fuels for cooking. Meanwhile, per capita energy consumption stands at one third of the world average.[2]

In terms of greenhouse gas (GHG) emissions, India has contributed only 3 percent of historical carbon dioxide emissions over the past century.[3] However, due to its role as the third largest greenhouse emitter, with rapidly growing energy demand, the need to decarbonize is also urgent.

There is no doubt that India will reap multiple benefits if it grows on a low-carbon, climate-resilient path. One major benefit would be avoiding being battered by the worst impacts of climate change. In 2023, India experienced extreme weather events on 318 out of 365 days – roughly one disaster every day.[4] The resulting losses and damages pile up on top of what is already a former colonized economy trying to play catch up, like much of the developing world.

1 https://www.livemint.com/Companies/HNZA71LNVNNVXQ1eaIKu6M/British-Raj-siphoned-out-45-trillion-from-India-Utsa-Patna.html
2 https://ourworldindata.org/energy-access
3 Narain/Goswami (2021).
4 https://www.downtoearth.org.in/environment/anil-agarwal-dialogue-2024-begins-cse-dte-release-2024-state-of-india-s-environment-report-94722

It is in this context that the moral imperative for adequate and high-quality climate finance to be transferred to the developing world becomes undeniable. Climate finance may lack a formal definition in political fora, but it must be viewed as reparations for the unfettered use of fossil fuels by industrialized economies. This has fuelled a crisis affecting all countries – some more severely than others – and is reversing development gains in the developing world.

The Global South is disproportionately affected by climate change

Countries that contribute the least to climate change are most vulnerable to its impacts. According to the World Bank, 74 of the lowest income countries emit only one-tenth of the world's GHG emissions.[5] However, over the last decade, they have already experienced about eight times as many natural disasters.[6]

Moreover, poorer countries are among the worst hit economically due to climate change: losses and damages from climate change have been concentrated in these countries (see Table 1).

Developing countries require finance for the transition away from fossil fuels, so that they can continue to meet development goals without significantly raising planetary GHG levels.

Climate finance needs and gaps

In 2009, developed countries committed to jointly mobilizing US$ 100 billion per year of new and additional financial resources for developing countries' climate action by 2020.[7] In 2015, this goal was extended to 2025. It was at this juncture that countries decided that a new climate finance goal would succeed this commitment, which would be decided prior to 2025.[8] This new finance goal is the so-called New Collective Quantified Goal (NCQG).

The NCQG assumes significance for many reasons. One of the most important reasons is that its precursor, the US$ 100 billion commitment mentioned above, represented a drop in the ocean compared to actual climate finance needs.[9]

Table 1:
Poorer countries are hit harder economically by climate disasters

Country/region	Impact	Damages as % of GDP
Germany	**Floods in 2021**	**0.9 %**
British Columbia, Canada	Heatwave 2021	3–5 %
Europe	Heatwaves 2003, 2010, 2015 and 2018	0.3–0.5 %
Dominica	Hurricane Maria 2017	226 %
Pakistan	Floods in 2022	9 %
Vanuatu	Tropical Cyclone Pam 2015	64 %

Source: Goswami/Rao (2023), see p. 8 for detailed sources.

5 Nishio (2021).
6 https://www.weforum.org/agenda/2023/01/climate-crisis-poor-davos2023/
7 UNFCCC (2009).
8 UNFCCC (2015).
9 Kozul-Wright (2023).

The UNFCCC Standing Committee on Finance (SCF), the nodal body within the UN climate framework for finance-related matters, authored a Needs Determination Report (NDR) in 2021.[10] The report analyses submissions made by countries about how much financing they need for implementing their climate plans under the UNFCCC and the Paris Agreement. The report found that the Nationally Determined Contributions (NDCs) of 78 developing countries estimated their costed needs to be between US$ 5.8–5.9 trillion cumulatively until 2030. Of all the needs identified by countries, not all were costed – approximately 40 percent were costed, and this was only across 78 NDCs. So, the estimate represents a fraction of all needs. An amount reflective of more countries, as well as more costed needs, is likely to be far higher. The US$ 100 billion per year commitment is a fraction of this conservative estimate.

Other estimates have also been made. A report by the Independent High-Level Expert Group on Climate Finance concluded that Emerging Markets and Developing Countries (EMDCs) other than China will need US$ 1 trillion per year in external financing alone until 2030.[11]

While the needs of developing countries are in the trillions, climate finance has not kept pace. The Organisation for Economic Co-operation and Development (OECD) has tracked the provision of climate finance from developed to developing countries under the US$ 100 billion commitment. In their 2024 update, the OECD reported that developed countries met their goal for the first time in 2022 – they provided and mobilized US$ 115.9 billion for developing countries.[12]

Apart from the fact that this delivery was too little, too late, a closer look at the quality of finance that constitutes this figure raises several questions.[13] For instance, about 70 percent of the public finance provided was in the form of loans, adding to the debt burden of recipient countries. To make matters worse, in previous years, analysis of the OECD figures by the civil society organization (CSO) Oxfam have revealed that the amounts are vast overestimates: the OECD has said that developed countries mobilized US$ 83.3 billion in 2020. However, Oxfam considers the real amount to be closer to US$ 21–24.5 billion, when considering grant-equivalent amounts and other factors.[14] This vast difference is owing to the lack of a clear, agreed-upon definition of climate finance. What gets counted as climate finance varies by entity, and those losing out are almost always economies that are already vulnerable.

Looking at data for all climate finance flows as reported by the Climate Policy Initiative (the OECD reports on flows from developed to developing countries specifically) paints a telling picture. In 2021 and 2022, the average annual climate finance flows globally were about US$ 1.3 trillion – only 1 percent of global GDP.[15] Although this is an increase compared to previous years (US$ 439 billion more), the distribution of climate finance is imbalanced. As the report highlights, the United States (USA), Europe, Brazil, Japan, India and China together received 90 percent of the increased funds. But even within these geographies, climate finance gaps remain. Crucially, the finance flowing to more climate-vulnerable countries has shown paltry progress: the ten countries that were most affected by climate change between 2000 and 2019 received just US$ 23 billion, which is less than 2 percent of total climate finance.[16]

10 UNFCCC Standing Committee on Finance (2021).

11 Songwe/Stern/Bhattacharya (2022).

12 OECD (2024).

13 https://www.downtoearth.org.in/climate-change/rich-nations-finally-delivered-on-100-billion-climate-finance-pledge-in-2022-finds-oecd-report-experts-flag-issues

14 Oxfam International (2023).

15 Climate Policy Initiative (2023).

16 The ten countries most affected from 2000 to 2019 were Puerto Rico, Myanmar, Haiti, Philippines, Mozambique, The Bahamas, Bangladesh, Pakistan, Thailand and Nepal, see Climate Policy Initiative (2023), p. 36.

Unfit for purpose: International Financial Architecture hinders climate ambition in the Global South

Given that climate finance provision is currently inadequate, as well as being unevenly distributed across regions and themes (for example, adaptation efforts receive significantly less funding),[17] there are many systemic barriers that are hindering sufficient access to climate finance for developing countries. Two key obstacles to accessing adequate climate finance include high debt burdens and the high cost of capital, particularly for green technologies.

According to Debt Service Watch, as of October 2023, the debt service of 139 countries with loans from the World Bank equaled their total spending on education, health, social protection and climate adaptation combined, while in African countries the debt amount exceeded this spending by 50 percent.[18]

In 2023, our analysis found that 16 low- and middle-income countries face higher debt servicing costs in one year than the cost of achieving their NDC.[19]

More recent analysis by the Debt Relief for a Green and Inclusive Recovery (DRGR) Project confirms the state of crisis: 47 emerging markets and developing economies (EMDE) are predicted to default on their loans if they prioritize investments in internationally agreed climate and development objectives.[20] Without adequate debt relief, the report highlights, debt burdens affect expenditures on socio-economic priorities.

Another barrier compounding the impact of inadequate climate finance flows is the unduly high cost of capital, particularly for green technologies that are essential to the energy transition. Developing countries are perceived to have a more “high-risk environment” – an assessment that is subjective, and rests mostly in the control of private credit rating agencies headquartered in the Global North. Countries in the Global South therefore face a higher cost of capital – meaning higher interest rates on loans and higher expected returns on equity are imposed on them – making the cost of investing in these regions far higher compared to their counterparts in the Global North. Financing costs for clean energy projects can be up to seven times higher in emerging and developing economies than in countries in Europe and the USA, according to the International Energy Agency (IEA).[21]

Essentially, the current climate finance target of US$ 100 billion does not reflect the developing world’s needs, and climate finance provision so far has been woefully inadequate. Even within the finance that has gone to the Global South, the distribution has been grossly uneven. Moreover, the International Financial Architecture (IFA) providing the context for today’s climate finance makes it difficult for developing countries to access such finance – by design.

The NCQG presents an opportunity not just to raise ambition and create a goal that reflects developing countries’ needs, but also one that drives a shift in the financial systems that underpin its implementation.

NCQG: A political impasse

The NCQG is due to be decided at Conference of the Parties 29 (COP29) in Baku, Azerbaijan in November 2024. However, determining a goal of such magnitude is no mean feat. Countries from around the world (those that are part of the UNFCCC and signatories to the Paris Agreement) have been working to arrive at consensus through a series of technical conversations and political engagements, as well as negotiations. However, the process has sparked immense debate and disagreement so far.

One of the most contentious issues has been that of the “contributor base” – in other words, which coun-

17 https://www.unep.org/resources/adaptation-gap-report-2023
18 Debt Service Watch (2023).
19 Goswami/Rao (2023).
20 Zucker-Marques/Gallagher/Volz et al. (2024).
21 https://www.iea.org/articles/the-cost-of-capital-in-clean-energy-transitions

tries or stakeholders must provide the money that will constitute the NCQG. Most developing countries, which are comprised primarily of low- and middle-income economies, small island states and least developed countries, have been clear about their vision for the NCQG: that this should be a goal amounting to at least US$ 1 trillion per year and that funding should be provided by developed countries to developing ones. This argument has been premised on the historical emissions that have helped today's wealthy nations achieve the economic status they enjoy now – through unbridled industrial expansion that has led them to become the largest contributors to the climate crisis and global warming.[22]

Although a standardized definition of developed and developing countries is absent from the UNFCCC or the Paris Agreement, within these climate negotiation spaces it is countries that are listed in Annex II of the UNFCCC that are typically considered "developed". These are nations that were members of the OECD at the time of adopting UNFCCC and have obligations to provide financial and technological assistance to developing countries under the Convention. However, many of these wealthier countries in the Global North today are suggesting that the responsibility for NCQG financing should be shared by newly "prosperous" developing economies, which have high annual emissions as well.

This has been a major deadlock in discussions for the new goal. Unsurprisingly, it is a lot of the same countries that indirectly wield power in the key institutions of the IFA: the governance structure of the International Monetary Fund (IMF) is known to be geared in favour of the USA, Japan and Europe in particular, and is characterized by an absence of due representation of countries from the Global South.[23] The World Bank's board also underrepresents developing countries. Its projects have long been criticized for a lack of transparency and accountability from the communities it strives to serve.[24]

This imbalance of power must be corrected urgently both from within and outside the UNFCCC for a successful and just climate finance outcome at COP29 and beyond. The NCQG is going to be both a provision and a mobilization goal. Regardless of the amount that gets decided, developing countries have been united in their demand for public finance to comprise the bulk of the goal. The provision of public finance can be either made bilaterally, through institutions of the UNFCCC financial mechanism (such as the Green Climate Fund), or through multilateral development banks – the largest of them being the World Bank.

The second, related question of how much money an NCQG must provide has also led to strong disagreements between countries – i.e., the issue of the quantum. Developing country groups have suggested figures in the range of US$ 1.1–1.3 trillion per year – an amount that is in line with conservative estimates of needs, as mentioned above. However, these numbers have not seen any constructive engagement from countries in the Global North.

Other than the contributor base and quantum, issues of sub-goals within the NCQG and the role of debt-based finance have been debated. On the latter, at COP28 in Dubai, countries took stock of progress on climate action for the first time through the results of the first Global Stocktake. Among key outcomes, the need for "non-debt creating instruments" for financing climate action in the Global South was acknowledged in the result. Given the state of the burgeoning debt crisis, and the majority of climate finance currently flowing as loans, this was a crucial outcome – one that developing countries are advocating for the NCQG to encompass as well. They have stood united in their ask for a majority of grants-based climate finance, drawn largely from public funds. Improvements in existing mechanisms addressing debt distress, namely the Common Framework of the G20 and the Paris Club and the Global Sovereign Debt Roundtable hosted by the IMF will be complementary to the call for halting the increase in the debt burden of

22 https://www.downtoearth.org.in/climate-change/bonn-climate-conference-2024-imbalanced-texts-imbalanced-outcomes-on-new-climate-finance-target

23 Bretton Woods Project (2019).

24 Bretton Woods Project (2021).

countries through NCQG climate finance provisions. The fact that money has been flowing back to providers of aid because of the use of loans is also telling.[25]

The quality of finance is thus as important as the quantity that gets sanctioned through the new climate finance target.

The road ahead: Adequate, public, concessional

Finance is one of the key enablers of climate action. It is therefore crucial that an ambitious and just outcome is negotiated on the NCQG at COP29. As the largest negotiating bloc in the UNFCCC, the G77 and China mentioned in a statement at the closing plenary at the Bonn climate conference in June 2024 that they "cannot go beyond COP29 without defining the NCQG", and there is a need to "move from conceptual to concrete discussions".[26] The following considerations must be kept in mind as the outcome of the NCQG is being determined.

To truly reflect the needs of the developing world, the level of the NCQG must be in the trillions of dollars annually. This should first be determined for a five-year period until 2030, and then revised upwards.

The statement that no government has enough money to finance trillions of dollars in climate measures is a myth. Billions of dollars are being spent on military funding and environmentally harmful subsidies. While multiple sources of finance are available to fulfill the NCQG, the emphasis must be on international public finance playing the leading role, to ensure maximum accountability, transparency and predictability. The onus cannot remain with the private sector to lead the financing of the climate transition.[27]

The NCQG must be heavily geared towards grant-based and highly concessional financing. For purposes such as adaptation and loss and damage, funding must be in the form of grants. For mitigation, it is necessary that the poorest countries are not burdened by further loans. Instead, larger emerging economies must be offered financing on highly concessional terms to account for the inequities of subjective risk perceptions and the debt crisis.

Fora outside of the UNFCCC that are debating the nuances of other funding streams, such as taxes on shipping and financial transactions and polluter fees on fossil fuel companies, must be linked to the NCQG process.

The NCQG must specify sub-goals for mitigation, adaptation and loss damage to ensure accountability and adequate finances for each climate purpose.

Finance through the NCQG must be directed from developed countries and be made available to all developing countries. Debates on the contributor and recipient base serve as distractions from the central goal of the NCQG.

Developing countries are fighting multiple battles – improving development outcomes, decarbonizing their economies and maintaining competitiveness in a changing green global economy. Simultaneously their backs are being broken by the very real impacts of climate change. And all of this is occurring in a global financial system designed to extract more from them whilst ensuring that their voices are barely heard in governance. Without an ambitious climate finance commitment from historical polluter nations, the demand for more climate "ambition" from countries in the Global South is equivalent to climate apartheid.

25 Harcourt/McNair (2024).

26 https://www.cseindia.org/distractions-and-double-speak-plague-climate-finance-talks-in-bonn-says-cse-12234

27 https://www.wri.org/insights/mdb-climate-finance-joint-report-2022

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6

Mend a broken system

How can we mend a broken system? Looking for ways to reform the international financial institutions

By Daniel Kostzer

The future of the world is being questioned on a global scale, affecting countries of all income and development levels. The agenda of the 'golden years' of capitalism has drastically shifted and the notion of a 'rising tide that lifts all boats' has proven to be an illusion, in economic terms. New risks have replaced the former status quo.

There is an urgent need to reform the International Financial Institutions (IFIs) established by the Bretton Woods Agreements of 1944. The focus should be on creating a common agenda that fosters a 'win-win' situation for all, rather than imposing values from the Global North in a 'top-down' way.

Can this be achieved within the current institutional framework? Is it simply a matter of governance or does it require additional resources?

The quest for reforms of the Bretton Woods Institutions

The story of the creation of the Bretton Woods Institutions (BWIs) – the World Bank and International Monetary Fund (IMF) – is well known: Much has been written about the differences between the waning colonial power of the United Kingdom and the rising power of the United States, on the one hand; or the developments and even gossip of 1944-46, such as the role of the Federal Bureau of Investigation (FBI) in the still unwritten rule that the President of the World Bank should be an American, while the Managing Director of the IMF should be a European.[1]

There is broad consensus on the limited effectiveness of both institutions in achieving not only the original goals set out in 1944 but also the redefined goals that have been set out since then. These include the so-called 'Twin Goals' of ending extreme poverty by 2030 and promoting shared prosperity by boosting the incomes of the poorest 40 percent of the population in each country, as defined by the World Bank in 2013, or the Marrakesh inclusion of the "World free of poverty in a livable planet".[2]

How can the new challenges of a 'just transition' be met without abandoning the prevailing urgencies of crisis prevention and recovery, debt emergencies, poverty reduction and human development expansion within the current architecture? Can a new framework be built over the existing foundations of the Bretton Woods institutions?

The aim of this chapter is to highlight several key issues that must be addressed before considering a

1 There is evidence that, after President Truman announced H. Dexter White as the head of the newly formed IMF, the FBI raised the suspicion that the latter was a Soviet spy. Then Truman offered the Europeans the post of the IMF Managing Director, keeping the WB presidency for the US. The accusation was never proved. For references see: New York Times, 18 August 1948, p. 1 (https://www.nytimes.com/1948/08/18/archives/h-d-white-accused-in-spy-inquiry-dies-former-assistant-secretary-of.html?auth=login-google1tap&login=google1tap), Benn Steil in New York Times, 8 April 2012 (https://www.nytimes.com/2012/04/09/opinion/banker-tailor-soldier-spy.html), and Boughton (2024).

2 https://timeline.worldbank.org/en/timeline/eventdetail/3331

new or reformed architecture for the complex International Financial Institutions (IFIs). This list is not exhaustive but identifies critical aspects that need to be resolved for any proposal to gain global acceptance and support. Some of these solutions are less than intuitive and, while these issues may initially appear disconnected, a deeper understanding of how these institutions operate, their governance structures, financing mechanisms and priorities will reveal the interconnections. These interlinkages are crucial for developing a comprehensive and coherent reform proposal.

Objectives: How to align the Multilateral Development Banks to the new agenda

It could be argued that there is some broad consensus on the goals, objectives and thematic areas of the expected policy interventions. The Sustainable Development Goals (SDGs), their dimensions and indicators, summarize an agreed, consistent and practical framework for the interventions that are fully incorporated into the mandate of the IFIs, in theory.

The SDGs constitute a comparatively static proposal where the starting point was 2015 and there are a number of objectives to be achieved by 2030.[3] They are not a development programme, nor are there suggested ways or paths to achieve them. In terms of dimensions for intervention, goals and indicators, the SDGs constitute a first step in a planning process, where the analysis should define the instruments to use, synergies and potential contradictions between goals, and institutional settings to design, reform or draw on to achieve these objectives.

The IFIs should adapt them recursively to their existing activities, especially those that are either new or where experience has been unsatisfactory. This cannot be done in isolation in the ivory tower of Washington D.C., but in active interaction with the multilateral institutions that are the custodians of the different goals (in other words, the United Nations (UN) in general as well as the International Labour Organization (ILO), United Nations Children's Fund (UNICEF), United Nations Environment Programme (UNEP), United Nations Educational, Scientific and Cultural Organization (UNESCO), etc.), as well as national governments and other civil society actors, in which trade unions and workers' representatives play a key and active role.

Governance: Democratic voice and vote

One of the first and key points to consider is the process of decision making in the new/reformed setting. The current system of weighted voting based on shareholding is not adequate. This system only reflects the power of richer and donor countries over the so-called customers, or implementing partners of the IFIs. The voting power is also reflected in the number of directors on the Executive Board of the IMF (24) and on the Executive Board of the World Bank (25). The Board of Directors is ultimately responsible for taking the strategic and operational decisions that govern the institutions.

It could be argued that there is a circularity in the shareholding allocation according to 'objective indicators' such as Gross Domestic Product (GDP), trade or economic openness. All these give more shares, therefore more voting power, to larger countries and more consolidated economies.[4] This system underscores the unequal international structure, which, in theory, is meant to be changed with the interventions.[5]

This system of shareholding and voting becomes highly relevant when the time comes to make some

3 Comparatively static in that there are no clear definitions regarding the path to take or intermediate steps; there is no general trend. Each goal must be achieved based on national decisions.

4 The elements of the quota formula are weighted in the following way: 0.5*GDP + 0.3* openness + 0.15*variability + 0.05*reserves (see https://www.imf.org/en/About/Factsheets/Sheets/2022/IMF-Quotas).

5 The Governors of the World Bank Group endorsed in 2015 the so-called 'Lima Shareholding Principles' that developed a 'dynamic formula' and defined a time profile of five years for the planning and revisions. For the World Bank Group, in 2015 a new 'dynamic formula' was defined, which combines 80 percent economic weight (measured by GDP, averaged over five years and using a blend of market exchange rates and PPP of 60/40), and 20 per cent Development Contributions (measured by IDA contributions with most weight given to the three most recent replenishments).

crucial decisions. For example, during the COVID-19 pandemic, the IMF took a major decision to provide additional resources to member states to address liquidity and resource constraints. A general allocation of 465.5 billion Special Drawing Rights (SDRs) in 2021, equivalent to about US$ 650 billion, was important and timely. However, it was allocated in proportion to the shareholding, and not to the needs of the countries, and the intended 'voluntary redistribution' from richer to poorer countries did not work. For some rich countries the allocation was unnecessary, while for poorer economies, it was insufficient.

Although it is true that there is a share of basic votes – votes allocated equally to all member countries – these only account for just 5.5 percent in both the IMF and the World Bank. In principle, while the contributions to the IFIs should bear some relationship to the capabilities of countries to provide resources to help others, the decision making and voting power should be equitable, as in the UN or other multilateral organizations: one country, one vote. An alternative could be two-stage voting, similar to a *two chamber system*.[6]

The process of consultations with other organizations and institutions should transcend the mere formality. Trade unions meet annually with the IFIs to discuss their workplans, critique their publications and push for the workers' agenda. However, these efforts rarely influence the actual operations or policies of the IFIs, especially the IMF.

Main approach: from projects to programmes

The IFIs tend to have a project-based approach. The units of analysis and intervention are the projects, with their own allocation of resources, objectives, procedures, operating manuals, monitoring, etc. In many cases, they are even detached from the national and sub-national structures in which they should be embedded, creating dual structures when they should be building capacity. Although many studies highlight the interactions between policy interventions, the project-oriented approach limits the contextual analysis that could take advantage of the synergies.

This becomes more evident when the World Bank Group (WBG) also compartmentalizes actions in areas defined in its internal structure, without integration.[7] This could be achieved through the SDGs and indicators as a planning context of the interventions, but would require some significant structural changes internally and also changes in the interactions with countries, as well as multidisciplinary approaches to the programmes.

In the case of the IMF, the problem is slightly different since it recommends 'programmes' in an integrated form. The IMF's approach always ends with a set of policy recommendations –common to almost all countries, independent of their productive structure, level of development and prevailing institutions. These recommendations are based on ideologically biased pre-judgements and not always on the diagnostic performed by officials. For most countries, it is sufficient to check the Article IV consultations, and a common trend can be seen in the recommendations section.

Top priority: Debt management

Foreign debt has been an issue for developing economies since the crisis of the 1980s. Although there have been times of certain calm – for example, before the global financial crisis of 2008-2009, and more recently due to the consequence of a period of almost zero interest rates – funds from the Global North maintained a reasonable flow to the Global South. Homi Kharas and Charlotte Rivard point out that "(s)ince the 2009 financial crisis and the subsequent period of extraordinary monetary policies, many developing countries accessed private credit and bond markets to supplement (and in many cases replace) domestic savings".[8]

6 A two-stage system, such as the systems of modern democracies, where one chamber is based on population size (representative) and the other on equal representation. Decision making is based on a majority of votes cast in both chambers. This system would mean at least 50 percent of direct votes and more equitable decision making.

7 There have been many attempts to better integrate areas with the development of communities of practice as well cross-cutting areas, but the results have not been satisfactory.

8 Kharas/Rivard (2024).

In the aftermath of the COVID-19 pandemic, many countries began to show signs of debt distress. The need for funds to deal with the public health emergency, respond to supply constraints and to protect the income of the population had a profound impact on the debt of emerging economies. The 'flight to quality' by private investors, taking advantage of higher interest rates from central banks in the Global North, or the demand for 'buybacks' by large companies, increased the outflow of funds from emerging markets. According to Kharas and Rivard, private lenders (banks and bondholders) withdrew over US$ 300 billion from developing economies during 2022 and 2023.

According to United Nations Development Programme (UNDP), of the 88 developing countries that have been assigned a credit rating from at least one of the major rating agencies, almost 30 percent are at substantial risk of extremely speculative conditions, or worse, in actual default.[9] Moreover, 50 percent of those developing countries are either at high risk of 'over-indebtedness' or are directly in debt distress.

Considering public debt as a percentage of GDP, in half of the countries it exceeds 55 percent. Additionally, half of these countries will face interest payments that consume 9 percent or more of their annual public revenues. Upper middle-income countries are expected to see the most significant increases in 2024, driven by persistently high global interest rates.

According to the World Bank's International Debt Report 2023, developing countries spent a record US$ 443.5 billion to service their external public and publicly guaranteed debt in 2022.[10] The 75 poorest countries, which are eligible to borrow concessional loans from the International Development Association (IDA), paid US$ 88.9 billion in debt-servicing costs in 2022, which is also an historical record. For Indermit Gill, the World Bank Group (WBG) chief economist, this is an invitation to crisis: "Every quarter that interest rates stay high results in more developing countries becoming distressed—and facing the difficult choice of servicing their public debts or investing in public health, education, and infrastructure."[11]

There are many alternatives and proposals issued in relation to solving the debt crisis. The grim scenario, with even grimmer prospects, urge sustainable debt management, based on the Basic Principles on Sovereign Debt Restructuring Processes.[12] Adopted by the UN General Assembly in 2015, they set out the conditions under which the debt of the most vulnerable economies should be discussed and restructured. The inclusion of the debt issue under the UN framework is necessary for the agenda to come.

The funding of the MDBs

While the IMF gets its funds directly from government sources plus the surplus generated by the operations (interest rates, surcharges, etc.), the WBG – as well the regional development banks – must use other practices to finance their activities. The mechanics are as follows: WBG staff define the 'envelope' to be used in the coming five years and following the 'dynamic formula' that determines how much each country should contribute. These contributions are not in cash, but rather are what is known as 'callable', which is a commitment by member countries to provide this money if the institution needs it. As of 30 June 2023, the World Bank had a total of US$ 296 billion in callable capital, accounting for 93 percent of its US$ 318 billion total subscribed capital, with the remaining 7 percent, or US$ 22 billion, in paid-in capital.[13]

With those commitments by member countries, the WBG issues bonds, after getting an AAA rating by the major credit rating agencies sold in market opera-

9 See https://data.undp.org/insights/debt-in-developing-economies. The two major rating agencies are Standard & Poor's and Moody's. Although we disagree with their methodological approaches, they profoundly affect the 'business sentiment' of investors, and the credit allocation from the development banks.

10 World Bank (2023).

11 https://www.worldbank.org/en/news/press-release/2023/12/13/developing-countries-paid-record-443-5-billion-on-public-debt-in-2022

12 UN General Assembly (2015).

13 World Bank (2024), p. 1.

tions. The WBG has borrowed "in all of the world's major capital markets, as well as directly from member governments and central banks".[14]

This dynamic of bond issuing, although seemingly effective, implies a number of constraints due to the intervention of the credit rating agencies. With limited political or social scope to assess the impact of the projects implemented, the rating agencies took an extremely conservative approach. This exerted pressure on the WBG, which restricted the exposure to some countries, even though the WBG never has faced a sovereign default.

The situation is even worse when considering regional banks. For the Inter-American Development Bank (IADB), the Asian Development Bank (ADB) or the African Development Bank (AfDB), maintaining a good credit agency rating becomes crucial. Due to geographical concentration, they are more exposed to lending to certain countries. The weight of some countries (Brazil, Indonesia, Mexico, Nigeria, the Philippines, etc.) becomes detrimental to the rating obtained by each of the banks, limiting the bond allocation in the markets, hence, impacting their lending capacity. The management of these institutions found an ingenious way of sorting out these problems, by exchanging debt from their different members to other MDBs, with the objective of reducing the exposure and limiting the lending capacity. However, this is only a mitigating tactic.

Need for new unconditional resources: Where to find the funds?

The only way of expanding the MDBs' lending capacity is by providing new funds. The discussion around how much money countries should bring to the table to finance the new agenda, without abandoning the traditional objectives, takes a lot of time and effort. Shareholding reviews took a long time, and the capital increases were quite limited. The last WBG review was performed in 2018, but not all countries fulfilled their commitment pledged to the institution. In this respect, it is imperative to look for new sources of funding that are long-term and independent of the will of individual countries. A redesigned global tax system could offer some answers.

Taxing principles: what is expected from a taxing system?

Many things have been discussed in relation to a taxing system: Equitable, fair, progressive, unavoidable, etc. Most of these principles are confined to the national space, and many of the recommendations tend to focus on the control of tax avoidance, evasion and other forms of profit shifting. Few have in mind that the generation of global resources is needed to finance transition with justice and equity, to change the productive, socio-economic and environmental landscape.

Sound tax systems include four main characteristics: Simplicity, transparency, neutrality and stability. These *'qualities'* point to different objectives, but together confirm the strength of a taxing system. The idea is to enhance the effectiveness, fairness and efficiency of taxes benefiting both taxpayers and the economy as a whole.

Financial Transaction Tax to finance development: Low-hanging fruits?

A Financial Transaction Tax (FTT) on stock, bonds and foreign exchange trades, as well as on derivative contracts, is an alternative for gathering resources for the challenges of a comprehensive and just transition.

Financial markets have expanded significantly, but this growth has come with turbulence, crises and crashes. These markets are central to the deregulated, financialized capitalist system that has transcended traditional production and distribution to generate extraordinary profits.

There are different valuations of the volume of transactions on global stock and bond markets depending on the sources; all are above US$ 100 trillion per year, with regional distribution that shows significant con-

14 https://thedocs.worldbank.org/en/doc/e384d12cfea59bdcb3adf25487894197-0340022023/original/IBRD-Information-Statement-FY23.pdf

centration: The US accounts for 42.5 percent of transactions, while the EU and China have around 11 percent each; Japan and Hong Kong are around 5 percent each. These five jurisdictions represent three quarters of total transactions in 2023.[15]

This concentration is one of the main advantages of the Financial Transaction Tax (FTT) as a global tax: it can be easily collected and controlled. The stock and bond markets of these countries have a large tradition of regulation and oversight. So how can we increase the feasibility of implementation?

Policy objectives: What can be expected from an FTT?

There are several goals of an FTT, besides the most obvious one of collecting funds for financing for development and just transition. James Tobin defined its purpose as follows: "… throw some sand in the wheels of our excessively efficient international money markets."[16] This would reduce high volatility trading (high intensity trading), which triggers risky behaviour by investors, crowding out productive investment. The restoration of the rate of profits of the productive sectors can only be achieved by the curtailing of the rate of profits of financial speculation.

On the resource side, an FTT would allow governments to diversify revenue sources, reducing reliance on traditional taxes (income, wealth, etc.) and regressive indirect taxes. This could also be an important source of income and wealth redistribution, since the revenues generated would be spent with *'progressive'* principles.

Taxing foreign exchange operations may help to reduce a prolonged swing in exchange rates caused by investors' behaviour, preventing the potentially damaging economic consequences in developing economies that is associated with the over- and under-shooting of exchange rate adjustments. When the FTT is introduced as an integral part of the overall financial architecture, it can reduce the outcomes of bad economic and financial policies.[17] This mechanism will operate by correcting the short-term operations, hence addressing exchange rate volatility.

Another factor of volatility in the world economy is the so-called 'herd trading' where investors move according to noise and news, rather than evidence, generating random movements that harm the stability of the economy. An FTT would also help to reduce the market presence of some investors that are characterised by a high volume of short-term investments causing macroeconomic volatility.

Conclusion on the reform of the BWIs: The bank should be a fund and the fund should be a bank

The economist John Maynard Keynes stated in 1944: "I will not say that the establishment of the Bank for reconstruction and development is more important than the Monetary Fund but perhaps it is more urgent".[18] In conclusion, we can argue that, as Keynes highlighted during the discussions at Bretton Woods, the structure of the IFIs should be drastically changed.

The IMF should be transformed into a bank that operates like a commercial bank, where the 'client' writes a cheque, similar to an overdraft – and, according to the qualifications and limitations assigned – from a current account when balance of payments emergencies require it. Rather than imposing conditions, perhaps it would be better to provide some guidance on specific strategies to address the emergency, but limit the advice to that. Crucially, this should be done without relying on the neoclassical framework of austerity and neoliberal policies, which consistently produce negative outcomes.

The World Bank, along with regional development banks, should be restructured into substantial, unconditional resource funds aimed at addressing

15 https://www.weforum.org/agenda/2023/04/ranked-the-largest-bond-markets-in-the-world/

16 Tobin (1978), p. 154.

17 Palley (2001).

18 Keynes (1944).

developmental disparities between countries. These funds should focus not only on the environmental dimension, but also on socio-economic development. For example, they could be replenished through the Financial Transaction Tax and other internationally coordinated taxes. Allocation of these resources should prioritize human development through democratic, participatory and programmatic methods, moving away from the paternalistic approach where policy decisions are made by those who contribute the most, rather than by those facing the greatest need.

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7

How the IMF affects healthcare

How IMF conditionalities affect healthcare in Ghana – and what to do about it

By Daniel Oberko

Austerity measures driven by the International Monetary Fund (IMF) stifle investment in public services, undermine rights to basic services such as healthcare, suppress economic growth and entrench poverty and inequality. Ghana's 2023 IMF programme is the second time the country has approached the institution in eight years, and the seventeenth time since independence. The long-term impact is less investment in public services such as healthcare. Ghana's healthcare expenditure is far below the 15 percent of national budgets recommended by the African Union.

Austerity – one of the IMF's neoliberal policy programmes – does not work for Ghana, particularly when the country is in crisis. However, there are solutions that could help to generate the much-needed revenue to invest in health. In the short term, the government should cut down on waste from political appointments, poorly targeted and election-driven social interventions, as well as confronting corruption. In the long term, the government should raise revenues by removing spurious tax incentives and closing loopholes for tax abuse. And healthcare policies should be driven by all stakeholders, including trade unions.

Introduction

Access to quality healthcare in Ghana is expensive and the out-of-pocket costs are out of reach for many Ghanaians. I have seen this with my own eyes. At the critical stage of my late mother's illness in 2022, she was admitted for more than a month to Ghana's largest teaching hospital. I recognized that I would spend a significant amount of money before she was discharged. From diagnostic tests to ambulance services and medication, every expenditure was out of our own pockets.

I called a doctor friend who works in the facility, and asked, "how would my mother survive if I did not have money to pay for all these tests and medications?" He was quiet for a moment. Then I added, "how do other families go through this?" His response was, "some families, after admitting their patients, do not step foot in the hospital again after realizing the cost of treatment".

When writer and Harvard Medical School graduate Jean Adomfeh asked whether an IMF loan killed her uncle in her article "Ghana's $3bn IMF deal: Did the fund kill my uncle?", the message she wanted to convey was that Ghana's healthcare system was not adequately funded due to loan conditionalities such as cuts to public spending, pushed forward by the IMF.[1]

Healthcare infrastructure in Ghana includes hospitals, polyclinics, community-based health facilities and other healthcare centres. There are about 11,000 of these facilities serving a population of close to 32 million. The WHO standard for doctor-to-patient ratio

1 Adomfeh (2023).

is 1:1,000. However, the Ministry of Health reports that as of 2021, the doctor-to-patient ratio in Greater Accra was 1:2,586. In the Upper East Region, it is 1:17,584. The general challenge and differences are explained by the level of poverty and differences in infrastructure in the regions.

The gap can be explained by the inadequate resources available to train and employ medical doctors to meet the demand, coupled with a backlog of graduate nurses who have been home for more than two or more years waiting to be posted to serve. There are huge deficits in the provisions of hospital beds, ambulances and other services.

The Ministry of Health budget as a proportion of the national Gross Domestic Product (GDP) in 2023 was 2.02 percent, which is far below the 5 percent recommended by the African Union (AU). It is also far below the level needed to improve healthcare delivery and the attainment of the Sustainable Development Goals (SDGs) on health.

The share of the Ghanaian government's budget dedicated to the health sector is expected to drop from a peak of 8.1 percent in 2019 to just 6.4 percent by 2025 – much lower than the 15 percent recommended by the Abuja Declaration. Ghana's National Health Insurance Scheme (NHIS) has been implemented, but still faces several obstacles, such as insufficient funding, poor quality of care, low stakeholder participation, corruption and ineffective governance.

With more than 50 percent of the population under the age of 35, according to the Ghana Statistical Service (GSS),[2] a weak healthcare system threatens the fight against child mortality and preventable and treatable illnesses associated with adolescent stages of life. This situation is also undermining the country's efforts to achieve universal health coverage (UHC). With the remaining 50 percent of the population facing their later years under a malfunctioning healthcare system, the elderly often have no access to specialized care or attention. In cases where they can access such care, it comes with a severe financial burden for patients like my mother and their families.

The lender of last resort: stifling public spending

Countries in crisis that seek an IMF loan must show their commitment to reducing fiscal spending through austerity measures. Ghana's 2023 IMF programme is the second time the country has approached the institution in eight years, and the seventeenth time since it gained independence 67 years ago.[3] On average, Ghana has enrolled in an IMF programme once every four years since 1957. Every government in its first or second term is hit by crises and therefore is forced to go to the IMF for a loan. This highlights the vulnerabilities of an economy that is heavily reliant on the export of primary commodities and the import of nearly everything, from toothpicks to plastic cutlery. It also underscores the fact that openness to global financial markets without strong regulations exposes the economy to crises.

Following the overthrow of Ghana's first Prime Minister and President, Dr. Kwame Nkrumah, subsequent governments abandoned his import substitution economic model and national industrialization drive. The global neoliberal economic policies led by the Bretton Woods institutions – the IMF and World Bank – were strongly promoted to ensure that developing countries like Ghana remained primary commodity exporters and suppliers of surplus labour. These countries were also encouraged to deregulate and privatize their economies, aligning with global market demands.

From the IMF-mandated Structural Adjustment Programmes (SAP) of the 1980s until now, Ghana has been through multiple economic crises. At each point, the country had to cut public spending, including wages, as well as introducing flexible labour laws, privatizing state-owned institutions and removing subsidies. For example, the 2015 IMF programme included an objective to cut the public sector wage bill

2 https://census2021.statsghana.gov.gh/subreport.php?readreport=MjYzOTE0MjAuMzc2NQ==&Ghana-2021-Population-and-Housing-Census-General-Report-Volume-3B#

3 Acheampong (2023).

significantly. As a result, the public wages were targeted at 5.3 percent of GDP between 2016 and 2021, according to a report by ActionAid, Public Services International and Education International.[4] This led to a considerable loss of about US$ 305.7 million for the public sector workforce, which meant constraints on the number of teachers and nurses employed in the public sector.

To make matters worse, IMF austerity measures incentivize private solutions. In some of the major public hospitals, for example, laboratory facilities are inadequate, which leads to limited tests being run. Patients are then asked to participate in these tests outside of the public healthcare facilities and end up paying even more out-of-pockets costs as a result.

Crises of debt, revenue mobilization and corruption

Debt crises reduce a government's ability to spend funds on healthcare and IMF austerity measures further stifle access to healthcare for people living in poverty. The multiple debt crises in Ghana had already curtailed public spending, including funds for the health sector, prior to the IMF agreement and the ensuing conditionalities. According to an ActionAid Ghana policy brief, as of 2020, more than 50 percent of the revenue generated in Ghana went towards servicing interest on loans.[5] The same report indicates Ghana spent US$ 1.28 billion on healthcare in 2019 – while more than three times as much money was spent paying off the country's external debt (US$ 4.1 billion). The results of the situation were well captured in the May 2023 IMF report on Ghana's request for an Extended Credit Facility (ECF):

> "The ensuing negative feedback loop of decreasing international reserves, Cedi depreciation, rising inflation and plummeting domestic investor confidence accelerated last year and eventually triggered an acute crisis."[6]

After the COVID-19 pandemic, Ghana's economy was heading towards a nosedive and public debt had risen from 63 percent of GDP in 2019 to about 93 percent of GDP in 2022. Inflation and the high cost of living had pushed some 850,000 Ghanaians into poverty in 2022, according to the World Bank's 7th Ghana Economic Update.[7] Data from the Ghana Statistical Services in June 2024 revealed that 7.3 million Ghanaians are multidimensionally poor.[8]

Revenue losses from tax abuse and Public-Private Partnerships (PPPs) are contributing factors to Ghana's ongoing crises. In recent IMF programmes for Ghana, revenue mobilization has been a key structural reform the country was expected to implement. In the 2009 to 2011 IMF programme, Ghana was expected to embark on a comprehensive review of its Value Added Tax (VAT) systems, tax exemptions and discretionary waivers. In the 2015 programme, Ghana was expected to eliminate tax exemptions to state-owned enterprises and free zone companies as well as eliminating the role of the Ghana Investment Promotion Centre (GIPC) in granting exemptions.

It was not until 2023 that the President signed the Tax Exemption Bill into law, following broad-based consultation by a parliamentary select committee. The committee reached out to various stakeholders, including affiliates of Public Services International (PSI) in Ghana, which have been campaigning to end spurious tax incentives in special economic zones over the last five years

Despite the potential of parliamentary laws like these to reduce exemptions and waivers through strong parliamentary oversight, limiting the finance minister's power to grant incentives and focusing incentives on strategic investments, the system continues to be subject to abuse. For example, three members of Ghana's parliament have sued the Ministry of Finance and the Ghana Revenue Authority (GRA) over granting tax waivers to about 42 private companies

4 ActionAid/Public Services International/Education International (2021).
5 ActionAid (2020).
6 International Monetary Fund (2023), p. 4.
7 World Bank (2023).
8 https://gna.org.gh/2024/06/poverty-report-over-7-3-million-people-multidimensionally-poor-in-ghana/

without approval or authority of parliament. In 2021, a total of more than US$ 335 million in exemptions were granted to these companies.[9]

According to research by PSI in 2019, tax exemptions provided by the government amounted to GH 2.6 billion (US$ 475 million) in 2017.[10] That was about a tenth of the year's tax income and more than six times the amount set aside for the government's flagship public education programme – Free Senior High School (FSHS) – for the same period. This amount is sufficient to employ 10,000 nurses or teachers for more than ten years and would have paid for 47 million doses of COVID-19 vaccines – more than enough to vaccinate Ghana's population of 32 million.

It is important to note, however, that while IMF loans are interest-free, they must still be repaid by the borrower, along with the implementation of any attached conditionalities. One such conditionality is privatization, which can take various forms, including Public-Private Partnerships (PPPs). PPPs are driven by private interest and profit, as compared to Public-Public Partnerships (PuPs), which have been advocated as an alternative. PuPs encourage public institutions to collaborate by sharing resources, experiences and expertise to expand and improve public services, mainly through peer-to-peer learning.

Following the COVID-19 pandemic, Ghana's government, through the Ghana Airports Company Limited (GACL), entered into a PPP agreement with Frontiers Healthcare Services (FHS) – a private company governed from the Caribbean tax haven Dominica and owned by a complex network of Ghanaian businesses. They were contracted to provide COVID testing at Ghana's international airport.

For the two years that FHS ran COVID-19 testing at Kotoka International Airport (KIA), GACL received US$ 6.4 million in compensation for the use of the airport's space and amenities, while FHS made almost US$ 87 million from providing the testing services to travellers arriving in the country.[11] In the meantime, nothing changed for Ghana's Noguchi Memorial Institute for Medical Research, a respectable state institution that leads medical research in Africa and whose systems, knowledge and facilities were also used by FHS. Rather than hiring FHS, which had no track record in healthcare, the state could have mandated Noguchi, a public institution, to fulfil this role.

In another example, the company Strategic Mobilization Ghana Limited (SML) and the government of Ghana inked a revenue assurance agreement to support the Ghana Revenue Authority's tax compliance audits of gasoline and diesel distributors. For each litre of fuel supplied, the company was entitled to 0.05 local currency units (5 GHP). That amounted to around US$ 4 million a month in 2019. The contract was extended in 2023 to cover upstream operations relating to the petroleum and mineral industries. This meant that SML would earn US$ 0.75 and 0.75 percent of all mineral profits from Ghana for each barrel of oil that Ghana exported. After investigation by The Fourth Estate, a public interest and accountability project of the Media Foundation for West Africa (MFWA), it was discovered that SML had no prior experience with revenue assurance deals in the petroleum sector. In the past, it had only served as a timber merchant. Furthermore, the National Petroleum Authority had established procedures for the work that SML was ostensibly performing. It seems that a PPP arrangement was being used as a conduit to siphon revenues from the State.

The question then is what can be done?

Conclusion: Possible solutions

Ghana must strengthen the country's revenue mobilizations systems. Ghana should implement a mapping of all tax incentives and a qualitative evaluation of how well they work to draw in actual revenues for the

9 https://citinewsroom.com/2024/05/335m-tax-waiver-request-full-list-of-42-beneficiary-companies/
10 Otoo (2019).
11 The Fourth Estate (2023).

advancement of sustainable development and expenditure in healthcare. In response to the G20/ Organisation for Economic Co-operation and Development (OECD) Pillar Two recommendation of a minimum 15 percent effective corporate tax rate, it is essential to review all company tax benefits thoroughly, including expenditure deductions and lower rates offered in export processing zones and special economic zones. Other countries will impose a top-up tax on any profits subject to less than 15 percent tax, even if Ghana chooses not to implement Pillar Two. The Ministry of Finance, responsible for enacting tax policies, should ensure that the exemptions regime maintains an effective corporate tax rate of at least 15 percent.

Ghana has transfer pricing regulations and the Ghana Revenue Authority has an office dedicated to dealing with issues of transfer pricing and other forms of tax avoidance and tax fraud. This requires adequate funding for the unit to procure the best resources needed to safeguard mechanisms for effective implementation. While it is important for Ghana to align with international tax governance proposals, it must ensure that it is also adapted to the local economy. Advanced countries and their various tax policy governing institutions have been blamed for leading the process of tax policy reforms without considering the circumstances of developing counties. Their tax policy proposals benefit advanced countries rather than developing countries. Developing countries like Ghana must find alternative routes to meet minimum tax rates and actively support the call for UN-led tax governance.

The process to generate much-needed revenue is beyond policy enactment. Citizens, trade unions, experts and other stakeholders should demand strong political will from parliament and politicians to ensure effective implementation. There should also be a call for transparency and accountability on the part of corporations. Citizens must be convinced that culprits of tax evasion, avoidance and the abuse of tax incentives will be punished.

To this end, Ghana should rethink the Agyapa deal. In 2018, the Ghana Mineral Income Investment Fund (GMIIF) (Act 978) was passed. It was set up to create and hold equity interest in a Special Purpose Vehicle (SPV) in any jurisdiction; to procure the listing on the SPV on any reputable stock exchange considered appropriate; and to assign/transfer any, or all, of its rights to the SPV.

The SPV is a private entity, Agyapa Royalties Ghana Limited. The GMIIF has a 75.5 percent share in Agyapa Royalties Ghana Limited. Agyapa Royalties Ghana Limited then set up a subsidiary, ARG in Jersey, which is a tax haven. The government of Ghana owns a 51 percent share in ARG. In the long run, ARG will float shares on the London Stock Exchange (LSE) to raise between US$ 500 million and US$ 1 billion.

In doing so, Ghana signs away over three quarters of its future gold royalties to ARG – forever. It also means that Ghana is indefinitely forfeiting up to 49 percent of its future mineral royalty income flows, in exchange for about US$ 500 million. And if there is anything untoward either in the financial market or through the activities of the directors, the government bears the cost. This is a prime example of a tax avoidance arrangement perpetrated by a government.

In a letter to the finance minister by the former Attorney General (AG) of Ghana Gloria Akuffo in 2020, she makes a strong case against the signing of the deal. She writes:

> “It freezes anything legal including judicial orders and decisions. In effect no court can pronounce any part of the agreement as being illegal, unconscionable, null and void or on any matter before the court which may or is likely to affect any part of the agreement. This will amount to executive interference of the powers of the judiciary, which is in violation of the concept of separation of powers as provided under the constitution of Ghana. Therefore, the executive

> arm of government cannot enter into an agreement that curtails the independence of both the Legislature or the Judiciary."[12]

Austerity is not a prudent policy option in times of crises because it does not yield the intended results. The IMF is all too aware of this. Austerity – also referred to as "fiscal consolidation" – stifles investment in public services, undermines rights to basic services such as healthcare, suppresses economic growth, entrenches poverty and inequality, and only causes crises to resurface in future.[13] Austerity does not address the fundamental issues of the crises. In their study of advanced and emerging economies looking at the effectiveness of austerity measures during crises, Ostry, Loungani and Furceri (all IMF staff) convey this succinctly: "Austerity policies not only generate substantial welfare costs due to supply-side channels, they also hurt demand and thus worsen employment and unemployment." They further argue that "on average, a consolidation of 1 percent of GDP increases the long-term unemployment rate by 0.6 percentage points and raises by 1.5 percent within five years the Gini measure of income inequality."[14]

The limited availability of loans by public development banks (PDBs) pushes debtors to resort to private borrowing with high interest rates that must be paid in US dollars. To address this, PDBs must increase credit facility options and the IMF should expand access to Special Drawing Rights for developing countries like Ghana.

At the national level, several pragmatic steps can be taken to ensure fiscal discipline. For example, Ghana does not need more than 100 ministers. Some experts have argued that about 50 ministers without deputies should be sufficient. In every ministry there are technical and administrative experts whose role is to support the work of the minister. Regional ministers can do their work without deputy regional ministers. The work of the regional coordinating councils, district and municipal chief executives are all to support effective administration of the regions. Sometimes, social intervention programmes, for all intents and purposes, are introduced to prop up voting numbers for politicians, especially when they are administered by political appointees. They contribute to public debt. With a decentralized administration such intervention programmes, led by existing public institutions, could be averted.

Public health policy, like every other public policy, should be driven by all stakeholders, including trade unions. High levels of corruption, poor policy decisions driven by private interests and their proximity to political power have all played a role in the dire situation in which Ghana's healthcare sector finds itself. Public health policy, just like any other policy, should not be left in the hands of politicians alone. It should be safeguarded by involving the participation of all relevant stakeholders, including trade unions. Stakeholders like these within health service delivery bring on board not only the power to negotiate for fair wages and improved living conditions for health sector workers, but they also provide a wide range of expertise in the actual functioning of the healthcare systems.

Healthcare unions like the Ghana Medical Association, Health Services Workers' Union, and the Ghana Registered Nurses and Midwives Association have been very vocal and involved in amplifying the voices of nurses and citizens, providing guidance and expertise as to how the country and its people should deal with the COVID-19 pandemic. These organizations must be supported and given the space to continue their role in the healthcare sector when it comes to defending the rights and interests of healthcare workers, advocating for laws that enhance patient care and benefit the sector and the communities it serves.

12 https://www.modernghana.com/news/1025985/agyapa-deal-unconscionable-attorney-general.html

13 Ortiz/Cummins (2019).

14 Ostry/Loungani/Furceri (2016).

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8

Reforming the financial architecture

Reforming the international financial architecture: Addressing the IMF's social legitimacy crisis

By Ohiocheoya (Ohio) Omiunu and Chioneso Samantha Kanoyangwa

This chapter critically examines the waning social legitimacy of the International Monetary Fund (IMF), focusing on its governance structure and role in the sovereign debt crisis. Despite growing calls for reform, the IMF has remained resistant to meaningful structural reforms, perpetuating an inequitable governance model dominated by a few wealthy nations. From the viewpoint that reforming the International Financial Architecture (IFA) also requires the reform of International Financial Institutions (IFIs), this imbalance marginalizes developing countries and undermines the IMF's credibility as a fair global financial institution.

The chapter also highlights how the IMF's continued reliance on austerity measures exacerbates economic hardships, particularly across several African countries that have recently defaulted or are currently experiencing debt distress, fuelling public scepticism and distrust. The IMF risks further erosion of its social legitimacy and continued irrelevance in global financial governance if it does not go beyond its minimalist approach to reforms.

Introduction

Kristalina Georgieva, Managing Director of the International Monetary Fund (IMF), and Rhoda Weeks-Brown, Director of IMF's Legal Department, wrote in 2023:

> "The [IMF] Fund's purposes and broad powers (together, the Fund's 'mandate') have not changed significantly over the past few decades. However, the substantive issues on which the IMF engages more systematically with its member countries in carrying out this mandate have evolved in important respects." [1]

To give some context to the above quote, Georgieva and Weeks-Brown admit that, while the conventional focus of the IMF is on monetary, fiscal, exchange rate and financial sector policies, along with closely related structural aspects, in recent years,

> "… the IMF's work has widened to cover a broader range of substantive topics, including governance and anti-corruption, climate change, fintech and the digitalisation of finance, inequality, social protection, and gender." [2]

According to them,

> "the IMF's work in these emerging areas with demonstrated criticality for the institution's macroeconomic and financial stability mandate is not an expansion of the IMF's mandate, but rather reflects continuing evolution in the economic understanding of what is critical for the achievement of that mandate." [3]

1 Georgieva/Weeks-Brown (2023), p. 17.

2 Ibid.

3 Ibid.

Indeed, the scope of the IMF's work has evolved beyond the conventional issues envisaged as 'macro-critical' within its original mandate as set out in its constitution. It is also true that the IMF's mandate has not changed significantly over the past few decades. The irony stems from this latter point because change is desperately needed within the IMF and the wider International Financial Architecture (IFA).[4] Admittedly, the evolution of the issues facing the global community requires international organizations to be agile and responsive to changing realities. However, Georgieva and Weeks-Brown's comments detract from the real issues and do not address the 'elephant in the room', which is the legitimacy crisis of the IMF and the wider IFA.

Conscious of the fact that much ink has flowed on these calls for reform, in this chapter we focus specifically on the waning social legitimacy of the IMF. In this context, we refer to the IMF's dwindling credibility with the audience and constituents it serves due to its reticence to acknowledge and engage with fundamental reforms to its structure. Our conceptualization of 'audience' and 'constituents' also goes beyond states and civil society organizations (CSOs), extending to voiceless ordinary citizens who bear the brunt of IMF policies. Focusing on the IMF's governance structure and its management in the sovereign debt crisis, we argue that the IMF's dogmatic insistence on maintaining the status quo not only undermines its legitimacy but also puts the future of the global financial system in jeopardy. Bradlow put this starkly, arguing that, unless the IMF and other IFIs address the fundamental structural issues, "they will never be able to fulfil their responsibilities effectively".[5]

The social legitimacy crisis of the IMF

Dellmuth and Tallberg define social legitimacy as the "acceptance of an institution within a given audience".[6] Dellmuth and Tallberg make an essential distinction between normative and sociological legitimacy. According to them, the former "refers to an institution's right to rule, based on its conformance to certain values and principles" and the latter "refers to the acceptance of an institution within a given audience".[7] Arguably, the IMF has retained the support of most states in the international system to regulate monetary policy. This normative legitimacy is derived almost entirely from its perceived efficacy and value as part of the IFA. Furthermore, given that the focus of CSO mobilization efforts has recently shifted to issues like Special Drawing Rights (SDRs) and fixing the debt architecture, one could also argue that the IMF has been adept at surviving critiques about its continued relevance as an institution.

However, the social legitimacy of the IMF is a more nebulous concept than its normative legitimacy. This is because social legitimacy is not premised on the mandate from states, derived from the IMF's efficacy as a technocratic institution focused on maintaining macro-economic stability or even predicated on the delegitimization efforts from CSO mobilization. Instead, the social legitimacy of the IMF is predicated on public perceptions (i.e., opinions by ordinary citizens) about it and the extent to which its activities are deemed embedded within the wider social fabric of society.[8] Barnett and Finnemore support this position, arguing that the "legitimacy of most modern public organisations depends on whether their procedures are viewed as proper and correct and whether they are reasonably successful at pursuing goals consistent with the values of the broader community".[9]

The attempts by global governance institutions such as the IMF to avoid scrutiny and accountability on the premise that their mandates related to issues are highly technical and are best left in the hands of an elite cadre of qualified experts no longer hold. In the 1990s, the IMF faced sustained criticism for its austerity-focused measures. However, it weathered the

4 Gathii (2023).
5 Bradlow (2000), p. 152.
6 Dellmuth/Tallberg (2015), p. 454.
7 Ibid.
8 Abdelal/Ruggie (2009).
9 Barnett/Finnemore (2004), p. 166.

storm and succeeded in blunting the delegitimization efforts of CSOs and avoiding public scrutiny for some time. However, the increasing visibility and impact of the IMF's decisions on everyday lives, especially in the immediate aftermath of the COVID-19 pandemic, have lifted the veil and rendered such justifications obsolete. The IMF's influence on ordinary citizens, particularly through the implementation of austerity measures – its preferred strategy for ensuring debt sustainability in countries in the Global South – has made the IMF a focal point of discussions. It is within this context that the IMF has gone on the charm offensive with the rhetoric expressed in the article published by Georgieva and Weeks-Brown. The attempt to justify the expanding mandate of the IMF on the so-called emerging issues without addressing the broader systemic and structural issues indicates an organization that is not yet open to change and would rather defend and justify its continued relevance.

The IMF may be doing important work in the areas mentioned above; however, this must not detract from the fact that there is widespread discontent with the current system, and for good reason. Bradlow commented along these lines in 2000, arguing that the primary cause of the unsatisfactory performance of IFIs such as the IMF "is their failure to adapt their structure and operating practices to their changing functions".[10] In effect, the problem is not necessarily about its expanding scope or functions but about the lack of corresponding changes to its governance structure to match its functions. By ignoring these agitations for systemic change, the majority shareholders of the IMF, such as the USA, are taking for granted the fact that "the social legitimacy of an International Organisation says little about the actual rightness or goodness of the organisation; [rather] it refers exclusively to the public's acceptance of and support for that organisation".[11] This underscores the urgent need for the IMF to evolve its governance structures to align with its expanded roles, ensuring greater accountability and legitimacy in the eyes of the global public.

As it stands, the view from the ground and stakeholders across different constituencies does not match the picture that the IMF seeks to portray with the aforementioned publication. The system is broken and needs fundamental reforms. United Nations Secretary-General António Guterres was categorical about this fact, stating that the International Financial Architecture is "outdated, dysfunctional and unfair".[12] This is a viewpoint that has been repeatedly made by several leaders in the Global South, including President Nana Akufo-Addo of Ghana, who argued that the current global financial system is "skewed significantly against developing and emerging economies" and in favour of rich countries,[13] and President William Ruto of Kenya, who has made calls for the "democratisation of global governance and a re-imagined multilateralism that is inclusive".[14] Mia Mottley, the Prime Minister of Barbados, has repeatedly made similar remarks calling for a "new internationalism" that is truly inclusive and reflective of the current global realities.[15] To be clear, these are not just unfair criticisms of the IMF and other IFIs. Two examples are discussed in the subsequent sections of this chapter to illustrate this point.[16]

IMF and governance

The IMF's governance structure is a primary factor in its waning social legitimacy, as its decision-making power remains concentrated among a few wealthy nations, marginalizing the voices and interests of developing countries. A closer look at the IMF's composition and power dynamics shows that the IMF is the lynchpin of the global debt and financial architecture. Given its prominent status, it is unfair that it has retained an inequitable governance structure. To put

10 Bradlow, (2000), p. 152.
11 Dellmuth/Tallberg (2015), supra note 8 at p. 454.
12 https://press.un.org/en/2023/sgsm21855.doc.htm
13 https://gadebate.un.org/en/77/ghana
14 https://www.standardmedia.co.ke/national/article/2001456275
15 https://www.kofiannanfoundation.org/news/kofi-annan-lecture-2022-mia-mottley/
16 See Dieter (2006), p. 343.

this in context, with the IMF's governance system based on weighted voting, the USA, which has 16.5 percent of the voting share, has an effective veto over any fundamental reforms of the system because 85 percent of the total voting power is required for any change in the voting structure.[17] This means that the US Treasury disproportionately influences IMF matters, particularly its role in the sovereign debt crisis. This is not only unsatisfactory but also exemplifies the uneven and undemocratic voting system based on quotas weighted by economic criteria and capital contributions, which favour a few wealthy countries over the vast majority of the world's countries. What is more evident from this dynamic is that the world's poorest economies have no power at the IMF, especially when the votes of the permanent members of the Paris Club are combined with the weighted shares of the USA.[18] The subordination of indebted countries is further enshrined in the design of the global debt and financial architecture through the requirement that the approval of Paris Club members must be sought at the start of any sovereign debt renegotiation.

Furthermore, Africa's 55 countries remain under-represented in the IMF's governance structures, with a meagre 7.2 percent of voting rights.[19] The IMF's addition of a third seat on the Executive Board for African countries illustrates a minimal approach to reforms that fails to inspire confidence in stakeholders regarding fundamental reforms. As the African Sovereign Debt Justice Network (AfSDJN) has argued, adding a new Executive Director is not enough to provide Africa with fair representation.[20] Currently, several wealthy countries each have a single Executive Director representing their interests on the Executive Board. According to the AfSDJN, this is "… an absurdity that shows that more is needed in terms of quota reform than an additional Executive Director".[21]
It is clear that African economies stand to be disadvantaged by a quota adjustment based primarily on economic weight. Even though the IMF pledges to 'protect' the quota of low-income countries, this is insufficient to increase the influence of African countries in the operations and policies of the IMF. The AfSDJN, therefore, posits that the enhancement of the IMF quotas of low-income countries to amplify their voice in its decision-making regardless of their economic weight is the more meaningful option.

To regain its social legitimacy, the IMF must undertake substantial reforms in its governance structures to reflect a more equitable distribution of power and to include the diverse perspectives of all member countries.

The IMF and the sovereign debt crisis

Another important point made by Dellmuth and Tallberg is that "the social legitimacy of an International Organisation [is not] necessarily based on a single logic but may be shaped by multiple sources that make citizens more or less supportive of an organisation".[22] In the context of the IMF, multiple sources of contention have fuelled public distrust of the system. The most apparent factors include the link between the IMF's regulation of global fiscal policy and the sovereign debt crisis. Based on the inequality in the voting structure, the critical argument is that the IMF system is perceived to be undemocratic due to the closed nature of the system, which does not accommodate a broad range of voices in its decision-making process. There is a strong correlation between this negative perception of the IMF and the declining effectiveness of the system in recent years. For example, the challenges experienced in the recent debt restructuring processes, especially the IMF's inability to get private creditors to the negotiating table, speaks to its declining credibility as the best forum for addressing the global debt crisis.

17 Ibid.

18 Ibid.

19 Gathii (2023), supra note 4.

20 African Sovereign Debt Justice Network (2023).

21 Ibid.

22 Dellmuth/Tallberg (2015), supra note 8 at p. 455.

While these regulatory International Financial Institutions (IFIs) have undergone historic proportions of stress in addressing these challenges, they are failing the test, as illustrated by today's debt crisis, particularly in the Global South. The IMF-hosted Global Sovereign Debt Roundtable (GSDR), an initiative aimed at building a greater common understanding among key stakeholders (creditors and debtors) involved in debt restructurings, is a welcome gesture. However, it is imperative to highlight that there have been several debt roundtables in the past, and creditor-centric discussions have dominated these.

The GSDR has been criticized for its continued exclusion of debtor countries, resulting in less positive impact on Africa's economies.[23] Despite the GSDR being designed to provide a platform for stakeholders to work together on the current shortcomings in debt restructuring processes, most African countries, including Zambia and Ghana, still face debt restructuring challenges. Furthermore, there has not been any positive impact on the debt sustainability challenges, making a case for reforming the Debt Sustainability Framework.

As a tool, the Debt Sustainability Assessment (DSA) should be reformed by de-emphasizing its commitment to austerity. Austerity measures are overwhelmingly associated with the need to guarantee debt service levels through a reallocation of budgetary resources otherwise allocated to public investment and services, education, healthcare and social security, typically by means of fiscal adjustment and regressive taxation. This de-emphasis would be possible through the incorporation of a human rights perspective. Currently, the DSA framework is legally and macroeconomically biased towards conducting assessments that underestimate sovereign insolvency problems. For the AfSDJN, a debt sustainability framework that does not appropriately account for sovereign insolvency problems effectively legitimizes unsustainable debt service – much to the detriment of citizens.

The G20 Common Framework, presented as the ultimate solution, has proven to be one of the many minimalist reforms to the global debt architecture favoured by the IMF. The G20's Common Framework approach to help countries seeking debt treatment has clearly failed to give Zambia, Ghana, Chad and Ethiopia the resolution these countries so badly need. Zambia has been stuck in debt restructuring negotiations for over three years and is facing the worst drought in over four decades. Having defaulted two years ago, Ghana has had to complete three major debt restructuring operations comprising domestic debt restructuring, external bilateral debt restructuring and commercial bondholders' debt restructuring. In Ethiopia's case, the process of seeking debt resolution has stretched over three years without resolution. Meanwhile, Chad became the first country to reach a Debt Treatment Agreement with official and private creditors under the G20 Common Framework, including Glencore.[24]

The IMF's role in the ongoing three restructuring processes has been very apparent, with its influence noted through its Extended Credit Facility, whose tranche-based disbursement is typically hinged on a country's ability to make progress with official and private creditors. This is a trend that the IMF has maintained over the years, with analysts flagging this as far back as 1998. Robert Barro wrote a revealing piece titled "The IMF Doesn't Put Out Fires, It Starts Them" in 1998, criticizing the IMF for encouraging bad economic policies by rewarding failure with bailouts, which increase moral hazard and financial crises.[25] Today, as a case in point, Kenya is on the brink of chaos.[26] It is critical to situate the 2024 Kenyan unrest in a context that considers both endogenous and exogenous variables. At the heart of this problem is a complex interaction of domestic challenges, such

23 https://afrodad.org/sites/default/files/statements/Reaction-to-the-Press-Released-by-IMFWB-on-the-Global-Sovereign-Debt-Roundtable-Meeting.pdf

24 https://www.afronomicslaw.org/category/african-sovereign-debt-justice-network-afsdjn/sixty-second-sovereign-debt-news-update-chad

25 Barro (1998).

26 https://www.afronomicslaw.org/index.php/category/analysis/alternatives-kenyas-austerity-and-militarized-response-genz-revolution

as government corruption and inefficient resource allocation, mixed with the frequently contested role of external actors – most notably the IMF. In 2021, Kenya agreed to a debt reduction deal with the IMF, obtaining US$ 2.34 billion in exchange for strict economic reforms.[27] These reforms, known as 'austerity measures', have sparked outrage, with critics claiming that they disproportionately burden the most vulnerable members of society while exacerbating pre-existing imbalances.

The IMF's prescription for Kenya, as with many developing countries seeking its aid, has focused on fiscal consolidation, which is frequently carried out through a combination of tax increases, subsidy cuts and public spending cuts. While the IMF warned the Kenyan government in January 2024 of the possibility of protests if the Finance Bill 2024 was passed, it urged President William Ruto's government to remain committed to changes under its programme, citing a revenue shortage. The IMF had assessed the risk of the protests as 'medium', an assessment that resulted in the loss of 39 lives. The IMF has temporarily delayed its board approval of fresh funding following the withdrawal of the Bill while it "closely monitors the situation".[28] It can be argued that, while the IMF did not necessarily write Kenya's Finance Bill, it certainly exerted influence over it. This is one of the many fires started by the IMF, and one it does not seem to be putting out any time soon.

For the IMF to restore its social legitimacy, it must shift from creditor-centric policies and instead prioritize inclusive, sustainable debt solutions that acknowledge the social and economic realities of debtor nations, ultimately fostering trust and support from the global community.

Conclusion

The persistent legitimacy crisis faced by the IMF is a direct consequence of its resistance to meaningful reform and adherence to outdated governance structures, which fail to meet modern demands for transparency, accountability and inclusivity. Ironically, the two examples that we focus on in this chapter were highlighted as far back as 2006 by Heribert Dieter, who argued that the IMF governance structure was in need of reform to address the imbalance where Organisation for Economic Co-operation and Development (OECD) countries dominate policy decisions affecting developing nations.

Heribert also argued that the IMF's outdated lending policies fail to provide a robust safety net for financial crises, prompting countries to seek alternative financial governance measures.[29] Almost two decades later, nothing meaningful has been done to resolve these systemic issues. This enduring lack of meaningful reform underscores the persistence of outdated practices, allowing institutions like the IMF to wield disproportionate power over debtor nations. The prevailing norms, regulations and mechanisms grant institutions such as the IMF the structural authority to hold debtor countries hostage, thereby perpetuating and enabling the distorted international financial system established back in 1944 to continue unabated.

What is even more worrisome is that, throughout its 80-year existence, the IMF's multiple 'restructuring' efforts have largely been cosmetic in nature, as the core paradigm has not changed significantly. Gathii warns, "The IMF and private creditors want minimalist reforms to the global financial system that are just enough to contain the pressure for more radical reform while they reap massive profits. Such minimalist reforms serve to kick the can down the road – they do not challenge the unequal governance of the IMF that is based on the assumption that the current international financial system is here to stay."[30]

27 https://www.imf.org/en/News/Articles/2021/04/02/pr2198-kenya-imf-executive-board-approves-us-billion-ecf-and-eff-arrangements
28 https://www.businessdailyafrica.com/bd/economy/imf-may-delay-approval-of-fresh-funding-to-kenya-4683254
29 Dieter (2006), p. 343.
30 Gathii (2023), p. xii.

Gathii's concerns are corroborated by Shim's study, which finds that investors react favourably if a borrowing government is credibly committed to implementing essential IMF conditionality.[31]

As was the case with the IMF's advice to Kenya over the Finance Bill 2024, Shim's study highlights how the opinions and perceptions among investors continue to have primacy in the interactions between the IMF and governments of borrowing nations. This further entrenches the perception that the IMF's conditional lending practices are primarily designed to serve the interests of private creditors by maintaining just enough reform to ensure debt repayment and economic stability, rather than addressing deeper systemic issues.

The 2005 argument of Rodrigo Rato, a former Managing Director of the IMF, that "change is held back by politics" epitomises the entrenched interests that are not ready to see the status quo change.[32] If that is the case, then plausible reform of the global debt architecture can only take place in an environment that is not monopolized by the IMF or those who stand to gain from the skewed operations of the IMF. Perhaps a more responsive and conducive environment would be under the umbrella of the United Nations, wherein a multilateral legal framework would provide for a new comprehensive, fair and effective sovereign debt restructuring mechanism that would be binding on all creditors, including commercial creditors.

In conclusion, unless the IMF embraces comprehensive reforms that address its structural imbalances and enhance its responsiveness to global challenges, it risks further erosion of its social legitimacy and continued irrelevance in the evolving landscape of international financial governance.

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31 Shim (2022), pp. 2151–2152.
32 Ibid, p. 344.

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