Uniting Church in Australia
SYNOD OF VICTORIA AND TASMANIA

Justice and International Mission Unit
130 Little Collins Street
Melbourne Victoria 3000
Telephone: (03) 9251 5271
Facsimile: (03) 9251 5241
jim@victas.uca.org.au

Foreign Affairs, Defence and Trade Committee
Department of the Senate
PO Box 6100
Parliament House
Canberra ACT 2600

E-mail: fadt.sen@aph.gov.au

Justice and International Mission Unit
Synod of Victoria and Tasmania, Uniting Church in Australia

Submission to the Senate Standing Committee on Foreign Affairs, Defence and Trade on An inquiry into Australia's overseas aid and development assistance program.

The Justice and International Mission Unit, Synod of Victoria and Tasmania, Uniting Church in Australia, welcomes this opportunity to make a submission to the Senate Standing Committee on Foreign Affairs, Defence and Trade on its inquiry into Australia's overseas aid and development assistance program.

This submission seeks to put aid in the broader context of development and the different pathways out of poverty. We reject the simplistic ideological assertion that poverty reduction only comes from economic growth. Economic growth plays an important part in poverty reduction, but the overwhelming body of empirical research demonstrates that far more is needed that just economic growth if poverty is to be reduced. The Australian Government's own assessment has been that ten years of positive economic growth in Papua New Guinea has not resulted in significant reductions in poverty.[1] Just because aid is not the main driver of development in many cases says nothing about the effectiveness of aid itself.

We take a view that the Australian aid program should focus on assisting developing countries to be able to provide essential services sustainably. Ideally developing countries should have a level of economic activity that allows them to raise sufficient government revenues to provide essential services for their own citizens and that the revenue raised is spent responsibly and accountably to their own citizens. Aid has an important role to play where developing countries lack the ability to achieve this outcome on their own and to provide some services where the developing country lacks the domestic resource mobilization capacity to raise the necessary resources on its own. Aid also has a role to play in assisting developing countries with domestic resource mobilization and in combating

[1] Senator the Hon Bob Carr, Minister for Foreign Affairs, 'Budget. Australia's International Development Assistance Program 2013-14', 14 May 2013, p. 19.

corruption. Aid will be most effective when provided to governments or parts of governments that have the political will to work for poverty reduction.

Aid also has a vital role to play in assisting countries in times of humanitarian disasters, be they natural disasters or armed conflicts.

There is a dilemma where a developing country government is not committed to reducing poverty in its own country, especially where that poverty exists amongst minority groups that the government shows no concern for. When the government in question has the resources to provide the services and support to reduce poverty and chooses not to do so, aid can fill the gap. However, it is understandable that donor countries are reluctant to use revenue they raise through tax to provide services in a foreign country where the country in question has the resources to provide the services themselves. At the same time, it is not the fault of the people living in those countries they were born there and that their government may be corrupt or uncaring. However, this aid is not ideal in that it only papers over the underlying problems and the services only continue as long as the aid keeps flowing. Thus it is important to exert as much influence as possible towards all governments being committed to reducing poverty within their own borders.

As noted by the OECD:[2]

> *There is no substitute for strong leadership in mobilizing political will across society to tackle extreme poverty. In Africa, for example, the leadership of the late Ethiopian Prime Minister Meles Zenawi and his focus on development results, food security and poverty reduction have been exemplary. The same could be said for a number of Ghanaian presidents hailing from different political parties, but who have coincided in championing poverty reduction and food security for the poorest. This has enabled Ghana to implement a successful development strategy focused on building the private sector, developing human resources and implementing good governance.*

1. Recommendations

1. The aid budget should focus on delivering sustainable poverty reduction and development.
2. Aid for dealing with humanitarian disasters should be maintained as an important component of the aid budget.
3. The aid program should continue to ensure there is co-ordination with other donors to maximize the impact of the aid budget in poverty reduction.
4. Aid should not be diverted to primarily pursue national interest outcomes over poverty reduction.
5. The principles of the Busan Partnership for Effective Development Co-Operation should be used to guide spending within the aid budget.
6. The aid budget should avoid the imposition of performance indicators that are not consistent with the recipient country's national development strategy where possible and should strengthen the institutions of the developing country to enable them to deliver services sustainably for poverty reduction and development.
7. Greater funding should be provided to civil society organisations that are likely to be able to effectively influence reform within recipient countries and improve respect for human rights standards towards improving both poverty reduction and development outcomes.
8. The Australian Government should scale up the aid program as quickly as funding can be effectively used to reach the target of 0.7% of GNI.
9. A greater proportion of the aid budget should be targeted in assisting developing countries in combating corruption and tax evasion. This may require targeting to bodies and parts of governments that have a demonstrated will to address these problems.

[2] OECD, 'Development Co-operation Report 2013. Ending Poverty. Highlights', 2013, p. 5.

Assistance should also be provided to ensure tax laws are robust enough to combat tax dodging and that tax authorities have the skills necessary to enforce tax laws.

10. Greater funding should be provided to civil society organisations that are likely to be able to effectively influence reform within recipient countries, provide shifts towards better governance where needed and curbing of corruption.
11. Australia should seek to ensure part of its aid to Papua New Guinea is used to adequately resource the PNG Financial Intelligence Unit, to curb losses through misappropriation of government revenue.
12. A small amount of funding from the aid program should be used to establish and fund a small unit within the Australian Federal Police to investigate and seek to return any funds stolen from developing countries that are being transferred to Australia.
13. As part of targeting Australian Government aid to poverty reduction, the program should continue to assist in providing resources for reforms that will lead to sustainable reductions in inequality.
14. The Australian aid program should restore funding to ILO programs that have demonstrated effective action to protect and promote decent work for people in developing countries as an important pathway out of poverty, especially where Australia is importing goods at risk of serious human rights abuses in their production.
15. Any diversion of aid spending into new aid-for-trade programs should be proceeded by thorough analysis of how the benefits of the program will lead to sustainable poverty reduction, rather than assuming poverty reduction will automatically result.
16. Overseas aid should not be used as subsidies to Australian companies in a return to tied aid, as this undermines the efficiency of aid to reduce poverty.
17. Funding should be restored to environmental programs in the aid budget where these are important for sustainable poverty reduction.

Table of Contents

2. Aid's Role in Overcoming Poverty

Aid also has very different roles depending on the context of the recipient country. It is estimated that 70.5% of people in income poverty of US$1.25 a day now live in middle income countries[3], many of which are not aid recipients. If the poverty line is drawn at US$2

[3] OECD, 'Development Co-operation Report 2013. Ending Poverty. Highlights', 2013, p. 14.

per day, then 77.8% of those living below this level live in middle income countries.[4] Even where middle income countries are aid recipients aid is often very small compared to other revenue sources. On the flip side, many Pacific countries are examples of countries where aid plays a very significant role in the resources available to address poverty.

Poverty is a problem that can be overcome. The World Bank estimate is that poverty will decline by 8.6% by 2030, based on the assumption that each country maintains its current pace of economic growth, population growth and rate of change in inequality.[5] In our own region the Republic of Korea is held up as an example of a country that moved from being among the world's lowest-income countries to become a prosperous, modern and efficient state and a large and rising middle class.[6] The OECD notes that five African countries – Benin, Ethiopia, Gambia, Malawi and Mali – have made "striking progress" in the struggle against poverty topping the global rankings in progress against all the MDGs compared to where they started from.[7]

Brazil is an example of what can be achieved in poverty reduction when there is political will to do so. Brazil saw GDP per capita increase by 29% between 2001 and 2011, and the poorest 20% of people saw their income grow seven times as fast as the top 20%. Brazil also reduced the number of people living in poverty by half.[8] The flagship *Bolsa Famíla* (Family Stipend) programme transferred cash to low-income households in exchange for enrolling children in school and ensuring regular medical check-ups and vaccinations (conditional cash transfers).[9]

Even probably the best known neo-liberal critic of aid, Bill Easterly, admits that "foreign aid likely contributed to some notable successes on a global scale, such as dramatic improvement in health and education indicators in poor countries."[10]

Donor co-ordination is important. For example, in the area of health spending there have been 280 bilateral donor agencies, 24 development banks and 242 multilateral programmes, and about 40 UN agencies providing finance. In some instances, local officials are so occupied with meeting the demands of donors that they are unable to focus on health activities that may be much more important. In Tanzania, it was previously reported that health workers in some districts spent over 20 days per quarter writing reports for different donors.[11]

Recommendations: The aid budget should focus on delivering sustainable poverty reduction and development.

Aid for dealing with humanitarian disasters should be maintained as an important component of the aid budget, being 17% of Australia's total ODA in the 2013-2014 budget.[12]

[4] OECD, 'Development Co-operation Report 2013. Ending Poverty. Highlights', 2013, p. 14.
[5] Nobuo Yoshida, 'What Can We Learn from Projecting Poverty for 2030?', World Bank Blog, 27 January 2014.
[6] OECD, 'Development Co-operation Report 2013. Ending Poverty. Highlights', 2013, p. 4.
[7] OECD, 'Development Co-operation Report 2013. Ending Poverty. Highlights', 2013, p. 3.
[8] OECD, 'Development Co-operation Report 2013. Ending Poverty. Highlights', 2013, p. 18.
[9] OECD, 'Development Co-operation Report 2013. Ending Poverty. Highlights', 2013, p. 18.
[10] Bill Easterly, 'The White Man's Burden', p. 176.
[11] Zulfiqar A. Bhutta and Samia Aleem, 'A review of external assistance and aid effectiveness for maternal and child health. Challenges and Opportunities', UN University World Institute for Development Economics Research, Working Paper No. 2013/099, October 2013, p. 13.
[12] Senator the Hon Bob Carr, Minister for Foreign Affairs, 'Budget. Australia's International Development Assistance Program 2013-14', 14 May 2013, p. 13.

The aid program should continue to ensure there is co-ordination with other donors to maximize the impact of the aid budget in poverty reduction.

Aid should not be diverted to primarily pursue national interest outcomes over poverty reduction.

3. The Busan Partnership for Effective Development Co-Operation as a guide for the Aid Budget

We support the principles outlined the Busan Partnership for Effective Development Co-Operation, made in the Republic of Korea on 1 December 2011 and to which the Australian Government committed itself. This includes a commitment to "decent work in developing countries is paramount" and that "promoting human rights, democracy and good governance are an integral part of our development efforts". The Declaration states "Over time, we will aim to increase independence from aid, always taking into account the consequence for the poorest people and countries". The Declaration committed to:

> *Focus on results. Our investments and efforts must have a lasting impact on eradicating poverty and reducing inequality, on sustainable development, and on enhancing developing countries' capacities, aligned with the priorities and policies set out by developing countries themselves.*

The Declaration also committed to:

> *Providers of development co-operation will minimize their use of additional frameworks, refraining from requesting the introduction of performance indicators that are not consistent with countries' national development strategies….*
>
> *Use country systems as the default approach for development co-operation in support of activities managed by the public sector, working with and respecting the governance structures of both the provider of development co-operation and the developing country….*
>
> *Where the full use of country systems is not possible, the provider of development co-operation will state the reasons for non-use, and will discuss with government what would be required to move forward towards full use, including any necessary assistance or changes for the strengthening of systems.*

The important role for developing country governments in their own countries' development was further recognised:

> *Institutions fulfilling core state functions should, where necessary, be further strengthened, alongside the policies and practices of providers of development co-operation, to facilitate the leveraging of resources by developing countries. Developing countries will lead in efforts to strengthen these institutions, adapting to local context and differing stages of development.*

Providing empirical support to the principles of the Busan Declaration a recent study by the UN University World Institute for Development Economics Research into external assistance and aid effectiveness for maternal and child health concluded it is important for:[13]

---

[13] Zulfiqar A. Bhutta and Samia Aleem, 'A review of external assistance and aid effectiveness for maternal and child health. Challenges and Opportunities', UN University World Institute for Development Economics Research, Working Paper No. 2013/099, October 2013, Abstract.

> *…donors to align their programmes with government-defined priorities in order to ensure the achievement of national development objectives, long-term sustainability and success.*

The study further formed the view for aid to be effective in the health sector "The international community (bilateral agencies, multilateral organisations and donor foundations) should not be permitted to define public health strategies for a country."[14]

The study gave the example of Sri Lanka as a positive example of reducing maternal and child mortality, having reached its MDG targets well ahead of schedule. The efforts of the Sri Lankan Government have been supported by international organisations through system development, using the government's existing foundation. A notable finding is that much of Sri Lanka's policy imperatives and gains were related to indigenous policies and investments, many of which continued despite the debilitating and prolonged civil war.[15]

Ghana provided another example of where domestic efforts by the government of Ghana combined with external assistance led to a constant decline in under-five child mortality between 1967 and 2008, with a quicker decline since 2000. Ghana received significant assistance during this period from bilateral agencies, including the USAID, UKAID and the IMF. On average official development assistance represented between 5 – 6% of GNI between 2009 and 2011.[16]

The Busan Declaration also acknowledged the important role of civil society organisations:

> *Civil society organisations (CSOs) play a vital role in enabling people to claim their rights, in promoting rights-based approaches, in shaping development policies and partnerships, and in overseeing their implementation. They also provide services in areas that are complementary to those provided by states. Recognising this, we will:*
>
> *(a) Implement fully our respective commitments to enable CSOs to exercise their roles as independent development actors, with a particular focus on an enabling environment, consistent with agreed international rights, that maximizes the contributions of CSOs to development.*
>
> *(b) Encourage CSOs to implement practices that strengthen their accountability and their contribution to development effectiveness, guided by the Istanbul Principles and the International Framework for CSO Development Effectiveness.*

At the 2008 Accra High Level Forum, all donors and governments committed "to work with CSOs to provide an enabling environment that maximizes their contributions to development." Respect for CSOs as development actors requires an enabling environment that guarantees the full participation of CSOs in all stages of the development process, including the planning and formulation of development plans and strategies.[17] As acknowledged in the *International Framework for CSO Development Effectiveness:*[18]

> *A vibrant civil society, which advocates for marginalized populations, is a public good. Governments should acknowledge this important role by providing fiscal*

---

[14] Zulfiqar A. Bhutta and Samia Aleem, 'A review of external assistance and aid effectiveness for maternal and child health. Challenges and Opportunities', UN University World Institute for Development Economics Research, Working Paper No. 2013/099, October 2013, p. 14.

[15] Zulfiqar A. Bhutta and Samia Aleem, 'A review of external assistance and aid effectiveness for maternal and child health. Challenges and Opportunities', UN University World Institute for Development Economics Research, Working Paper No. 2013/099, October 2013, pp. 4-5.

[16] Zulfiqar A. Bhutta and Samia Aleem, 'A review of external assistance and aid effectiveness for maternal and child health. Challenges and Opportunities', UN University World Institute for Development Economics Research, Working Paper No. 2013/099, October 2013, p. 6.

[17] Open Forum for CSO Development Effectiveness, 'The Siem Reap CSO Consensus on The International Framework for CSO Development Effectiveness', 28-30 June 2011, p. 20.

[18] Open Forum for CSO Development Effectiveness, 'The Siem Reap CSO Consensus on The International Framework for CSO Development Effectiveness', 28-30 June 2011, p. 24.

support through taxation and other mechanisms in order to ensure the continuing operation and sustainability of civil society actors.

Recommendations The principles of the Busan Partnership for Effective Development Co-Operation should be used to guide spending within the aid budget.

This includes avoiding the imposition of performance indicators that are not consistent with the recipient country's national development strategy where possible and strengthening the institutions of the developing country to enable them to deliver services sustainably for poverty reduction and development.

Greater funding should be provided to civil society organisations that are likely to be able to effectively influence reform within recipient countries and improve respect for human rights standards towards improving both poverty reduction and development outcomes.

4. Aid Quantity

There is no shortage of worthwhile efforts aid could be spent on to reduce global poverty. The more aid provided the more that can be done with it. If there are existing inefficiencies in the current Australian aid budget, these can be corrected to improve the aid budget's impact on reducing poverty. At the same time improved efficiency and targeting in the aid budget is not an excuse for Australia not to keep scaling up its aid budget to reach 0.7% of GNI as Australia had promised to do across successive governments since 1970. On October 26, 1970, the UN General Assembly adopted Resolution 2626 on International Development Strategy for the Second United Nations Development Decade, stating that:

> *Each economically advanced country will progressively increase its official development assistance to the developing countries and will exert its best efforts to reach a minimum net amount of 0.7 per cent of its gross national product … by the middle of the Decade.*

Section 33.13 of *Agenda 21*, the document adopted by all Member States at the 1992 United Nations Conference on Environment and Development in Rio, stated that:

> *Developed countries reaffirm their commitments to reach the accepted United Nations target of 0.7 per cent of GNP for ODA and, to the extent that they have not yet achieved that target, agree to augment their aid programmes in order to reach that target as soon as possible.*

The Monterrey Consensus (2002), which stated in part:

> *We recognize that a substantial increase in ODA and other resources will be required if developing countries are to achieve the internationally agreed development goals and objectives, including those contained in the Millennium Declaration...*
>
> *In that context, we urge developed countries that have not done so to make concrete efforts towards the target of 0.7 per cent of gross national product (GNP) as ODA to developing countries... We acknowledge the efforts of all donors, commend those donors whose ODA contributions exceed, reach or are increasing towards the targets, and underline the importance of undertaking to examine the means and time frames for achieving the targets and goals.*

Australia also adopted the 2005 UN World Summit Outcome, which declared:

> *We welcome the increased resources that will become available as a result of the establishment of timetables by many developed countries to achieve the target of 0.7 per cent of gross national product for official development assistance by 2015 and to reach at least 0.5 per cent of gross national product for official development*

> *assistance by 2010,… and urge those developed countries that have not yet done so to make concrete efforts in this regard in accordance with their commitments;*

The cutting of Australia’s ODA/GNI ratio to 0.33% in the 2013-2014 financial year will mean Australia remains well behind most other OECD countries in its level of ODA, where the OECD average is 0.41%

The current government has partly used the rationale that the previous increase in aid could not be well managed by AusAID as a reason for freezing aid in real terms of $5 billion a year. However, by contrast a different standard appears to apply to military spending, with the current government planning to increase military spending by 0.41% of GDP in the next decade to reach 2% of GDP. Yet, defence economics analyst with the Australian Strategic Policy Institute, Mark Thomson, has already publicly questioned if the Defence Department will be able to effectively spend this level of increase, based on the military’s past performance.[19]

Recommendation: The Australian Government should scale up the aid program as quickly as funding can be effectively used to reach the target of 0.7% of GNI.

5. Combating Corruption and Tax Dodging

The Busan Partnership for Effective Development Co-Operation highlights the importance of combating corruption, tax evasion and illicit flows in the pursuit of poverty reduction and development:

> *Corruption is a plague that seriously undermines development globally, diverting resources that could be harnesses to finance development, damaging the quality of governance institutions, and threatening human security. It often fuels crime and contributes to conflict and fragility. We will intensify our joint efforts to fight corruption and illicit flows, consistent with the UN Convention Against Corruption and other agreements to which we are party, such as the OECD Anti-Bribery Convention. To this end, we will:*
>
> *(a) Implement fully our respective commitments to eradicate corruption, enforcing our laws and promoting a culture of zero tolerance for all corrupt practices. This includes efforts to improve fiscal transparency, strengthen independent enforcement mechanisms, and extend protection for whistleblowers.*
>
> *(b) Accelerate our individual efforts to combat illicit financial flows by strengthening anti-money laundering measures, addressing tax evasion, and strengthening national and international policies, legal frameworks and institutional arrangements for the tracing, freezing and recovery of illegal assets. This includes ensuring enactment and implementation of laws and practices that facilitate effective international co-operation.*

A recent working paper by the IMF Working Paper *Understanding Countries’ Tax Efforts* released in November 2013, found that the tax capacity of countries was significantly negatively affected by both corruption and inequality. The paper further acknowledged that corruption fed inequality. Thus, efforts towards domestic resource mobilization (such as increasing tax revenue) must also seek to address corruption.

Murney *et al* (2011) found there is a strong empirical correlation between government effectiveness and rule of law. They found no empirical examples of countries with highly

[19] Mark Thomson, ‘In a real world, Abbott faces a big challenge’, *The Weekend Australian,* Special Defence Report, 2-3 November 2013, p. 2.

effective governments and low rule of law.[20] They found the correlation between human development indices and the rule of law in countries less strong than for government effectiveness, but still significant.[21] From the empirical data they developed a model which argued that attempting to progress development to the exclusion of rule of law is likely to be less productive than traditionally assumed as the levels of state functionality and governance conditions needed to support human development are unlikely to be present or result from human development interventions alone.[22] They further raise the need to consider appropriate timeframes in which rule of law might be expected to improve and allow improvement in human development, raising the concern that progress is often expected in unrealistically short timeframes.[23]

Fragile states lose significant amounts of revenue through illicit flows. These flows exceed aid and foreign investment. Fragile states are particularly affected by illicit flows and activities, since they are more at risk from being targeted by such illegal activity, and low state legitimacy can prevent authorities from combatting the economic and financial crimes that contribute such losses.[24]

While not strictly corruption, tax dodging by multinational corporations and wealthy individuals drains developing countries of far more money than they collectively receive in foreign aid. Work by Christian Aid in 2008 estimated the loss to developing countries through transfer mispricing and false invoicing alone to be US$160 billion a year, more than developing countries collectively received in foreign aid.[25] Aid can play an important role in combating tax dodging and improving the effectiveness, efficiency and fairness of developing country tax systems. The OECD has provided compelling evidence which shows that the return on donor investment in tax systems development can be significant:[26]

- In Ethiopia, DFID, alongside other donors, supports the Public Sector Capacity Building Programme which includes capacity building support to the tax system. An objective is to increase tax revenue by 87% from 43.3 billion birr in 2010 to 81.1 billion birr in 2013. Every £1 of DFID support to tax system reform is estimated to produce additional revenue of about £20 per annum.
- USAID support worth US$5.3 million in 2004-10 to improve tax collection in El Salvador led to increased revenue of US$350 million per year.
- In Burundi, DFID support helped to establish an independent Revenue Authority in July 2010, at a time when the country's tax and customs services (then under the Ministry of Finance) topped the list of East Africa's most corrupt organisations in Transparency International's East African Bribery Index. The programme set out to transform the culture of tax collection. From January to June 2011, revenue collection was 37.4%

[20] Tony Murney, Sue-Ellen Crawford and Andie Hider, 'Transnational Policing and International Human Development – A Rule of Law Perspective', *Journal of International Peacekeeping* **15**, (2011), pp. 55-56.
[21] Tony Murney, Sue-Ellen Crawford and Andie Hider, 'Transnational Policing and International Human Development – A Rule of Law Perspective', *Journal of International Peacekeeping* **15**, (2011), pp. 59-60.
[22] Tony Murney, Sue-Ellen Crawford and Andie Hider, 'Transnational Policing and International Human Development – A Rule of Law Perspective', *Journal of International Peacekeeping* **15**, (2011), p. 64.
[23] Tony Murney, Sue-Ellen Crawford and Andie Hider, 'Transnational Policing and International Human Development – A Rule of Law Perspective', *Journal of International Peacekeeping* **15**, (2011), pp. 69-70.
[24] OECD, 'Fragile States 2014. Domestic Revenue Mobilisation in Fragile States', February 2014, p. 59.
[25] Christian Aid, 'Death and Taxes: the true toll of tax dodging', May 2008, pp. 5, 51-56.
[26] OECD, 'Draft Final Report on the Feasibility Study into the Tax Inspectors Without Borders Initiative', 17 May 2013, p. 42.

above the level for the same period the previous year. From July to September 2011 the outturn revenue exceeded the forecast by 14% (or £7million).

- DFID support to the Rwanda Revenue Authority helped to provide the laws and regulations under which the authority was established, the office building and the management systems. The 10 year period of support saw a six-fold increase in the taxes collected and in 2010, the management procedures of the authority were awarded ISO 9001 2008 accreditation – the first Rwandan institution to attain this standard. The Authority reached a point where it was collecting the full £24 million value of DFID's support programme every three weeks. Its effectiveness has been a major factor in Rwanda's impressive development performance in recent years.

The OECD is piloting a Tax Inspectors Without Borders (TIWB) initiative this year that will enable serving and former tax officials to work in tax authorities in developing countries on targeted audit-assistance programs. Developing countries will contribute to the costs of receiving assistance from the experts who will provide on-the-job, tax audit assistance to the officials in the developing country tax authority. The effectiveness of the *Tax Inspectors* program will be evaluated at the end of 2014. TIWB will uniquely concern focused assistance on current audit cases – a practical and immediate approach to combatting tax evasion and ensuring better quality tax audits. The Australian Taxation Office is already providing technical support to TIWB, although Australia has not been a donor to the current program.

The OECD has argued that donor agencies can help fragile states build their capacity to combat illicit flows. They point out that donors have made strong political commitments to helping developing countries raise revenue. Yet despite evidence that this support pays dividends, only 0.07% of ODA to fragile states actually supports their tax systems. Prioritising this support means using countries own systems.[27] Without urgent action fragile states will grow from being home to one third of people in poverty globally currently to more than half of the world's poor after 2018.[28] Progress in achieving the Millennium Development Goals has been slower in fragile states than in other developing countries. Of the seven countries that are unlikely to be able to meet any MDG by 2015, six are fragile.[29]

Of the fragile states in our region, the amount of aid received to support domestic resource mobilisation in 2010 - 2011 were:[30]

- Afghanistan – US$25.65 million
- Nepal – US$3.47 million
- Solomon Islands – US$2.24 million
- Timor Leste – US$0.27 million
- Bangladesh – US$90,000
- Sri Lanka – US$40,000
- Pakistan – US$40,000
- Marshall Islands – US$20,000
- Kiribati – US$10,000

Clearly, there is an opportunity to provide greater assistance in this area.

[27] OECD, 'Fragile States 2014. Domestic Revenue Mobilisation in Fragile States', February 2014, p. 12.
[28] OECD, 'Fragile States 2014. Domestic Revenue Mobilisation in Fragile States', February 2014, pp. 13, 15.
[29] OECD, 'Fragile States 2014. Domestic Revenue Mobilisation in Fragile States', February 2014, p. 15.
[30] OECD, 'Fragile States 2014. Domestic Revenue Mobilisation in Fragile States', February 2014, p. 66.

As a very specific anti-corruption measure within our region the Australian Government should seek to direct some of the aid provided to PNG to its Financial Intelligence Unit (PNGFIU). A World Bank and Asia/Pacific Group on Money Laundering assessment from July 2011 was highly critical of the lack of resources being allocated by the PNG Government to the PNGFIU stating:[31]

> *The FIU has minimal resources, currently the FIU has only three staff, having started out three years ago with seven. It has not been given a formal structure within the Police force. It cannot fulfil the role it should be playing in developing the national AML [anti-money laundering] system and receiving, analysing and disseminating reports.*

The assessment further stated:[32]

> *The FIU has very competent, professional and committed staff, and is receiving valuable financial reporting information from banks. This has the potential to be used to help stem the high levels of misappropriation and other corrupt practices in PNG. However, there are currently insufficient resources within the FIU for it to carry out its statutory functions.*

We would urge that Australia do much more to deter the transfer of funds to Australia where there is a high risk the funds have been stolen from developing country governments. For example, we see no reason not to automatically share information about property purchases by politically exposed persons (PEPs) from PNG in Australia. Such information is publicly available anyway, at a small cost. However, being alerted in a timely manner of such transfers may assist PNG authorities in any investigations they are undertaking or may alert them to the need for an investigation. The transfer of funds to bank accounts and money being spent at casinos and other gambling venues should also be shared with the PNG authorities, with appropriate safeguards for privacy.

Currently, even if Australian police were to become aware of corruptly or criminally obtained funds entering Australia from PNG, they would not automatically share that information with the PNG police or other bodies.[33] Such information might be shared on request from a PNG law enforcement body.

There have been a number of higher profile cases from PNG where PEPs have transferred funds to Australia or bought properties in Australia and then have been subject to legal action in PNG on offences related to misappropriation of funds from the PNG Government. Paul Tiensten, the former Foreign and Planning Minister for PNG, was recently convicted. Eremas Wartoto, Leonard Capon and Jeffery Yakopya have all been charged and are awaiting trial following investigations by PNG anti-corruption unit Taskforce Sweep. All three owned assets in Australia. Paul Paraka has been charged with 18 offences related to allegedly receiving fraudulent payments of $28.7 million from the PNG public purse, yet was able to transfer millions of dollars into Australia even after having been accused of these offences by the PNG Commission of Inquiry generally into the Department of Finance. It is not known to us if any of the funds transferred to Australia by these people were illegally sourced.

While Australian action on this front will in and of itself not stop corruption in developing countries, it is important to keep reducing the places funds stolen through corruption can be

---

[31] ‘Mutual Evaluation Report. Anti-Money Laundering and Combating the Financing of Terrorism. Papua New Guinea’, The World Bank and the Asia/Pacific Group on Money Laundering, 21 July 2011, p. 7.

[32] ‘Mutual Evaluation Report. Anti-Money Laundering and Combating the Financing of Terrorism. Papua New Guinea’, The World Bank and the Asia/Pacific Group on Money Laundering, 21 July 2011, p. 8.

[33] Senator Scott Ludlam, Senate Question Number 2391, 19 October 2012.

shifted to. This will make the remaining places willing to accept stolen funds higher risk so those stealing such funds can be less certain they will benefit from their criminal activity. It also strengthens the integrity with which Australia can seek to assist other countries in dealing with corruption, as Australia's position is somewhat undermined if it creates a perception that it is indifferent to funds stolen through corruption being transferred into Australia and only acts when such funds are directly brought to its attention.

Finally we urge that a small amount of funding from the aid program be used to establish and fund a small unit within the Australian Federal Police to investigate and seek to return any funds stolen from developing countries that are being transferred to Australia. This should be modelled on the successful units established in the UK with DIFD funding. In 2006 a Proceeds of Crime Unit was set up within the Metropolitan Police to investigate cases of PEPs money laundering in London and an Overseas Anti-Corruption Unit in the City of London Police, to investigate cases of bribes paid abroad by British companies.[34] In the case of the Proceeds of Crime Unit investigations are carried out after a suspicious activity report is received and assessed to check there is real grounds for suspicion.[35] By 2010, the Proceeds of Crime Unit had taken actions resulting in the freezing of £160 million ($296 million) of assets.[36]

Recommendation A greater proportion of the aid budget should be targeted in assisting developing countries in combating corruption and tax evasion. This may require targeting to bodies and parts of government that have a demonstrated will to address these problems. Assistance should also be provided to ensure tax laws are robust enough to combat tax dodging and that tax authorities have the skills necessary to enforce tax laws.

Greater funding should be provided to civil society organisations that are likely to be able to effectively influence reform within recipient countries, provide shifts towards better governance where needed and curbing of corruption.

Australia should seek to ensure part of its aid to Papua New Guinea is used to adequately resource the PNG Financial Intelligence Unit, to curb losses through misappropriation of government revenue.

A small amount of funding from the aid program should be used to establish and fund a small unit within the Australian Federal Police to investigate and seek to return any funds stolen from developing countries that are being transferred to Australia.

6. Economic Growth and Inequality

While economic growth is seen as a key driver of poverty reduction, the benefits of economic growth for poverty reduction are affected by the distribution of those benefits.[37] World Bank research argues that accelerating growth alone is not enough to meet a target of eliminating

[34] Alessandra Fontana, 'Making development assistance work at home: DfID's approach to clamping down on international bribery and money laundering in the UK', U4 Anti-Corruption Resource Centre, U4 Practice Insight 2011:5, p. 3.
[35] Alessandra Fontana, 'Making development assistance work at home: DfID's approach to clamping down on international bribery and money laundering in the UK', U4 Anti-Corruption Resource Centre, U4 Practice Insight 2011:5, p. 3.
[36] Alessandra Fontana, 'Making development assistance work at home: DfID's approach to clamping down on international bribery and money laundering in the UK', U4 Anti-Corruption Resource Centre, U4 Practice Insight 2011:5, p. 1.
[37] Nobuo Yoshida, 'What Can We Learn from Projecting Poverty for 2030?', World Bank Blog, 27 January 2014.

extreme poverty by 2030 and that promoting the sharing of prosperity is necessary as well.[38] This includes a sharing of prosperity across countries, as well as within countries. Aid has a critical role to play in the sharing of prosperity across countries.

The Asian Development Bank has formed the conclusion that rising inequality hampers poverty reduction.[39] The Bank compared actual poverty headcount rates (using the US$1.25-a-day poverty line in 2008) with the poverty headcount rates simulated keeping inequality unchanged from the 1990s to the 2000s. Had inequality not increased:[40]

- In India, the poverty headcount rate would have been reduced to 29.5% in 2008 instead of the actual 32.7%;
- In the People's Republic of China, extreme poverty would have declined to 4.9% instead of the actual 13.1%; and
- In Indonesia, the poverty rate would have fallen to 6.1%, instead of the actual 16.3%.

For the 11 Asian economies with rising inequality (out of 28 countries), the cost of that widening comes to 240 million more people trapped under the US$1.25-a-day poverty line, or 6.5% of the region's population. The 11 countries with widening inequality account for 82% of the population of Asia.[41] Asia's rising inequality contrasts with recent trends in other parts of the developing world, in particular Latin America, where income inequality has been on the decline since the 1990s.[42]

The Asian Development Bank also argued that not only does inequality dampen the poverty reduction impact of growth, it can also affect growth itself, through a number of economic, social and political mechanisms.[43]

The Bank also points out that widening inequality – leaving more people at the top and bottom of the ladder – can also mean a hollowing out of the middle class. They argue the middle class are important for stability and growth. Growth driven by and benefiting the middle class is more likely to be sustained – both economically and politically. Economically, the rent seeking and corruption associated with highly concentrated growth for the very wealthy are avoided. Politically, middle class driven growth makes conflict and horizontal inequalities between racial and ethnic groups easier to manage.[44]

The Bank also argues that the negative impact of inequality on institutional quality, institutional stability and property rights is well established.[45]

[38] Nobuo Yoshida, 'What Can We Learn from Projecting Poverty for 2030?', World Bank Blog, 27 January 2014.
[39] Asian Development Bank, 'Asian Development Outlook 2012. Confronting Rising Inequality in Asia', 2012, p. 41.
[40] Asian Development Bank, 'Asian Development Outlook 2012. Confronting Rising Inequality in Asia', 2012, p. 41.
[41] Asian Development Bank, 'Asian Development Outlook 2012. Confronting Rising Inequality in Asia', 2012, p. 74.
[42] Asian Development Bank, 'Asian Development Outlook 2012. Confronting Rising Inequality in Asia', 2012, p. 74.
[43] Asian Development Bank, 'Asian Development Outlook 2012. Confronting Rising Inequality in Asia', 2012, p. 41.
[44] Asian Development Bank, 'Asian Development Outlook 2012. Confronting Rising Inequality in Asia', 2012, p. 41.
[45] Asian Development Bank, 'Asian Development Outlook 2012. Confronting Rising Inequality in Asia', 2012, p. 42.

In many countries, income inequality coexists with non-income inequality in the form of unequal access to education, health and basic services among different population groups classified by gender, location and income.[46]

The Bank has recommended action in three broad areas to address the problem of growing inequality in Asian countries:[47]

- Efficient fiscal policy. Measures include increasing spending on education and health, especially for the poorer parts of society; developing better targeted social protection schemes, including conditional cash transfers that target income to the poorest but also incentivize the building of human capital; and greater revenue mobilization through broadening the tax base and improving tax administration, and switching spending from inefficient general subsidies to targeted transfers.
- Interventions to address lagging regions. Measures include improving regional connectivity; strengthening fiscal transfers for greater investment in human capital and better access to public services in lagging regions; and removing barriers to migration from poor to more prosperous areas.
- More employment-friendly growth. Policies include facilitating structural transformation and maintaining a balanced sectoral composition of growth between manufacturing, services and agriculture; supporting the development of small and medium-sized enterprises; removing factor market distortions that favour capital over labour; strengthening labour market institutions; and introducing public employment schemes as a temporary bridge to address pockets of unemployment and underemployment.

The Bank points out that it has been well documented that a key contributing factor in the recent decline in income inequality in many Latin American countries is improved access to education by those in poverty.[48]

In 2010, in 15 out of 33 Asian countries where comparative data are available, government spending on education as a share of GDP was less than 4%, including Indonesia, Pakistan, India and the Philippines. By comparison the OECD average was 5.2% of GDP spent on education. In 2009, in 20 of 41 Asian countries with comparable data, government spending on health as a share of GDP was less than 5%, compared to an OECD average of 9.4%.[49]

The ILO has shown that virtually all countries can afford basic social security.[50]

The share of government revenue as a proportion of GDP is low in many Asian countries. For example, in 2011 the share of central government revenue was about 12 – 14% of GDP in Bangladesh, Cambodia, Myanmar, Pakistan and the Philippines[51], suggesting the need for tax reform to collect more tax revenue. Strengthening governance and institutions is important in improving tax collection[52], a role that aid can assist in. The UN estimates that to

[46] Asian Development Bank, ‘Asian Development Outlook 2012. Confronting Rising Inequality in Asia’, 2012, p. 74.
[47] Asian Development Bank, ‘Asian Development Outlook 2012. Confronting Rising Inequality in Asia’, 2012, p. 75.
[48] Asian Development Bank, ‘Asian Development Outlook 2012. Confronting Rising Inequality in Asia’, 2012, p. 76.
[49] Asian Development Bank, ‘Asian Development Outlook 2012. Confronting Rising Inequality in Asia’, 2012, pp. 76-77.
[50] Asian Development Bank, ‘Asian Development Outlook 2012. Confronting Rising Inequality in Asia’, 2012, p. 79.
[51] Asian Development Bank, ‘Asian Development Outlook 2012. Confronting Rising Inequality in Asia’, 2012, p. 80.
[52] Asian Development Bank, ‘Asian Development Outlook 2012. Confronting Rising Inequality in Asia’, 2012, p. 82.

achieve the Millennium Development Goals, domestic revenue of developing countries should be at least 20% of GDP.[53] Of the 51 fragile states identified by the OECD, only two have domestic government revenues of 20% of GDP, with the average amongst fragile states being 14% of GDP.[54] According to the OECD:[55]

> *A fragile region or state has weak capacity to carry out basic governance functions, and lacks the ability to develop mutually constructive relations with society Fragile regions or states are also more vulnerable to internal and external shocks such as economic crises or natural disasters. More resilient states exhibit the capacity and legitimacy for governing a population and its territory. They can manage and adapt to changing social needs and expectations, shifts in elite and other political agreements, and growing institutional complexity. Fragility and resilience should be seen as shifting points along a spectrum.*

Within our region the OECD identifies North Korea, Nepal, Afghanistan, Pakistan, Sri Lanka, Bangladesh, Myanmar, Timor-Leste, Micronesia, Solomon Islands, Marshall Islands, Tuvalu and Kiribati as fragile states.[56]

At the moment fragile states are often highly aid dependent. The most aid dependent country being Tuvalu with 55.6% of its GNI being country programmable aid, with the next most aid dependent country being the Solomon Islands with 44.7% of the GNI in country programmable aid.[57]

The OECD argues:[58]

> *Building capacity to raise revenue through taxes is particularly crucial in fragile states, as it reduces dependence on aid and helps finance human development and recovery. At the same time, it strengthens the contract between the state and its citizens, and can fortify intra-society relationships.*

Aid has a role to play in assisting countries within our region to implement reforms to address inequality.

Given the importance of decent jobs as a significant pathway out of poverty, it is stunning that the current Government has cut funding to the ILO in the aid program. We do extensive work around forced labour and human trafficking of migrant workers in Thailand. For example, while trafficking only occurs onto a small part of the Thai fishing fleet, the abuses for those trafficked onto fishing boats are severe.

Three men tried to escape. They grabbed fishing net floats and jumped in the sea, but it was very rough and two drowned as they couldn't swim. The other was caught when he got to shore. They brought him back to the boat his face was swollen from being beaten and tortured. They called us on deck. The captain said this is what will happen if you try to escape. The man was tortured with electric shocks and was then shot in front of us all and thrown overboard.

Account by escaped trafficked fishing boat crewman[59]

---

[53] OECD, 'Fragile States 2014. Domestic Revenue Mobilisation in Fragile States', February 2014, p. 11.

[54] OECD, 'Fragile States 2014. Domestic Revenue Mobilisation in Fragile States', February 2014, p. 11.

[55] OECD, 'Fragile States 2014. Domestic Revenue Mobilisation in Fragile States', February 2014, p. 16.

[56] OECD, 'Fragile States 2014. Domestic Revenue Mobilisation in Fragile States', February 2014.

[57] OECD, 'Fragile States 2014. Domestic Revenue Mobilisation in Fragile States', February 2014, pp. 29-30.

[58] OECD, 'Fragile States 2014. Domestic Revenue Mobilisation in Fragile States', February 2014, p. 11.

A 2011 report by the International Organisation for Migration entitled *Trafficking of fishermen in Thailand*, found that men trafficked from Cambodia and Burma onto abusive Thai fishing boats may be forced to work 18 to 20 hours a day, seven days a week and not be paid for years on end. On abusive boats, men who do not perform to the expectations of the captain can face severe beatings, maiming or even murder. Crew who are injured while working may be denied any medical attention.[60]

The Global Post ran a story on 21 May 2012 in which they interviewed seven men who had been trafficked onto Thai fishing boats. Four of the seven claimed to have witnessed murders on the boats. Moeun Pich, a 32-year-old Cambodian, stated he witnessed a Thai captain stab a crewmember to death with a metal spike used to mend nets. He himself was kept in forced labour at sea for six years, being resold to captains of other boats. A 39-year-old Cambodian, Sokha, his 16-year-old son and two young nephews were sold to a Thai deep-sea trawler captain for $650 each. They were made to watch the captain carve up the face of one of the crew. He escaped after two years.

There are also reliable reports of the use of forced labour, trafficked labour and child labour in prawn shelling sheds that feed seafood processing plants. For example, *The Washington Post* published an article on 20 September 2012, ‘In a world hungry for cheap shrimp, migrants labor overtime in Thai sheds’, recounting the experience of 14-year-old Thazin Mon who worked to shell shrimp in a peeling shed. She stated she was forced to work 16 hour shifts seven days a week for less than $3 a day. She also stated she was beaten if she slowed down and when she asked for a day off to rest, her hands swollen with infection, her supervisor kicked her and threatened her with rape. Min Oo, aged 28, paid a labour broker around $500 to smuggle him into Samut Sakhon, on the promise of a job paying around $10 a day. Instead, he stated he was trafficked into a shrimp processing factory where he was forced to work 18 hours a day for no more than $20 a week.

Voice of America reported on 5 January 2013, that nine-year-old Nu Nu Wai worked 13 hours a day with her parents peeling prawns in a Thai factory, along with other children. PSB News Hour TV interviewed a trafficked Burmese migrant worker working in a prawn peeling shed on 20 September 2012 who stated they worked from 3 am to 9 pm each day for around $10.

Much of the forced labour, trafficked labour and child labour is due to the role labour brokers play in supplying workers. People are lured, mainly from Burma, with the promise of a decent job in Thailand. When they get to Thailand they are told the contract they signed will not be honoured and instead they have a debt to pay off to the labour broker for their transport. The wages they are paid are often lower than promised and deductions are made for accommodation, food, work uniforms and payments to Thai government officials and police. Their travel documents are often confiscated. The situation is made worse by Thai labour law, which requires the consent of the Thai employer for the worker to transfer employers. Abusive employers almost never voluntarily grant permission for the release of the trafficked worker, so workers who escape and seek another employer are left highly vulnerable to further abuse as they then become illegal and can be reported to the authorities, placed in a detention centre and deported back to their country of origin.

---

[59] Alastair Leithead, Burmese ‘slavery’ fisherman are trafficked and abused, available at http://www.bbc.co.uk/news/world-asia-pacific-12881982
[60] International Organisation for Migration, Trafficking of fishermen in Thailand, available at http://www.iom.int/jahia/webdav/shared/shared/mainsite/activities/countries/docs/thailand/Trafficking-of-Fishermen-Thailand.pdf

There are an estimated two to four million migrant workers in Thailand, with up to 80% coming from Burma. Up to 1.5 million of them are 'illegally' in Thailand making them extremely vulnerable to abuse by their employers and/or labour brokers.

In our experience the ILO has been at the forefront of driving effective action to end these abuses. Both the Thai industry and the Thai Government are working with the International Labour Organisation (ILO) and other UN bodies to address human trafficking, child labour and forced labour. The Thai Food Processors Association (TFPA) and Thai Frozen Food Association (TFFA) have both issued public codes forbidding their members from engaging in these abuses. The Thai Government is mapping the existence of prawn shelling sheds (for example there are about 200 unregistered shelling sheds in Samut Sakhen) and developing guides, with the assistance of the ILO, to assist employers in complying with Thai labour law. By contrast to the effective action by the ILO, we have had very little interest from the Australian Government to take any action to address the issues of forced labour, human trafficking and child labour in the production of foodstuffs from Thailand, despite significant imports of these products into Australia. Products produced with the use of forced labour and human trafficking are proceeds of crime and Australia should be funding action to stop the laundering of these proceeds of crime across borders into Australia. We have helped Australian companies identify debt bondage and other Thai labour law violations in the processing plants of their suppliers.

Recommendations: As part of targeting Australian Government aid to poverty reduction, the program should continue to assist in providing resources for reforms that will lead to sustainable reductions in inequality.

The Australian aid program should restore funding to ILO programs that have demonstrated effective action to protect and promote decent work for people in developing countries as an important pathway out of poverty, especially where Australia is importing goods at risk of serious human rights abuses in their production.

7. The role of Foreign Direct Investment (FDI)

There are those who like to champion the role of Foreign Direct Investment in reducing poverty, often using it as an argument for slashing overseas aid. Like promoting trade, the argument runs that FDI increases economic growth with automatic flow on benefits to all people in the country. However, the OECD and World Trade Organisation warn against making such assumptions and that FDI flows should be interpreted carefully. They point to studies that have urged caution in assuming that private flows are automatically positive for development. First, in terms of stability, private flows are volatile, with low predictability compared to aid. Even before the crisis, FDI in many of the 'boom sectors' was not providing sustainable benefits for growth and poverty reduction in terms of employment, budget revenue and transfer of technology and skills.[61]

8. Aid for Trade

The current Government has indicated a desire to redirect more of Australia's ODA into 'aid-for-trade' initiatives. At its most positive, such a shift is about increasing economic activity within developing countries, with a belief the benefits will flow to the whole society and poverty will be reduced. In the words of the OECD and the World Trade Organisation:[62]

[61] OECD/WTO (2013), 'Aid for Trade at a Glance 2013: Connecting to Value Chains', http://dx.doi.org/10.1787/aid_glance-2013-en, p. 59.
[62] OECD/WTO (2013), 'Aid for Trade at a Glance 2013: Connecting to Value Chains', http://dx.doi.org/10.1787/aid_glance-2013-en, p. 146.

> *…. three generalized propositions link the transmission of aid for trade to growth and poverty reduction: aid for trade leads to more rapid growth of exports and imports; more rapid growth of trade raises productivity and income growth; and incomes rising with growth lift people out of poverty. This chain of causation, while arguably robust as cross-country generalisations over long periods, does not necessarily hold for every country at any given time. For example, many factors affect the link between trade growth and income growth: conflict, indebtedness, governance, or the absence of complimentary policies in finance, education, and/or investment. Similarly, in the last link of the chain, from growth to poverty reduction, the basic structure of the economy – initial distribution of income, land or natural resource ownership, the skill of the labour force, or the labour-intensity of production – strongly affects the pace of poverty reduction and the distribution of the benefits from income growth.*

Globally aid for trade has grown by 57% since the agreed baseline for assessing progress (ie an average of aid for trade provided between 2002 and 2005). Aid for trade has maintained its share of sector allocable ODA at around 33%. These substantial increases have benefited all aid for trade categories, with increases of 61% in aid for trade policy and regulation, 58% in aid for building productive capacity and 55.5% in aid for economic infrastructure.[63] Ten countries received 35% of these disbursements, dominated by Asia, which has routinely been the largest regional recipient of commitments. India is the largest recipient with US$11 billion (6.4% of the total), followed by Vietnam with just over US$9 billion (5.3%) and Afghanistan with US$8.2 billion (4.7%). Commitments to China and Indonesia have declined, but these countries received disbursements of US$5.8 billion (3%) and US$4.4 billion (2.5%) respectively.[64]

At its most positive aid for trade plays an important role in easing the policies and trade binding constraints that prevent developing country firms from linking to or moving up value chains.[65]

Asia is now the largest aid-for-trade recipient with US$17 billion.[66]

There is now abundant evidence that aid for trade in combination with complementary policies is helping to lower trade costs – in the form of additional infrastructure, better institutions such as customs and standards authorities, as well as more trade friendly policies and regulations, or in regulatory procedures that increase competition and reduce prices.[67]

The OECD and the World Trade Organisation calculate that $1 in aid for trade is associated with an increase of nearly $8 in additional exports from all developing countries, $9 for all low and lower-middle income countries and $20 for International Development Association (IDA) countries.[68]

---

[63] OECD/WTO (2013), 'Aid for Trade at a Glance 2013: Connecting to Value Chains', http://dx.doi.org/10.1787/aid_glance-2013-en, p. 62.
[64] OECD/WTO (2013), 'Aid for Trade at a Glance 2013: Connecting to Value Chains', http://dx.doi.org/10.1787/aid_glance-2013-en, p. 71.
[65] OECD/WTO (2013), 'Aid for Trade at a Glance 2013: Connecting to Value Chains', http://dx.doi.org/10.1787/aid_glance-2013-en, p. 21.
[66] OECD/WTO (2013), 'Aid for Trade at a Glance 2013: Connecting to Value Chains', http://dx.doi.org/10.1787/aid_glance-2013-en, p. 22.
[67] OECD/WTO (2013), 'Aid for Trade at a Glance 2013: Connecting to Value Chains', http://dx.doi.org/10.1787/aid_glance-2013-en, p. 25.
[68] OECD/WTO (2013), 'Aid for Trade at a Glance 2013: Connecting to Value Chains', http://dx.doi.org/10.1787/aid_glance-2013-en, p. 26.

So far, few of the bilateral aid for trade programmes have been evaluated, but those that have report tangible results. For example, UK's interim monitoring of its value chain activities and aid-for-trade projects found improved incomes, working conditions and employment for partner country workers. The Netherlands also evaluated its value chain programmes for tea, cotton and cocoa and found an increase in household income and sustainability.[69]

However, it should not be assumed that increased trade will automatically result in poverty reduction. It is a question of how the benefits of the increased trade are distributed and what policies deliberately ensure those in poverty will benefit. A recent World Bank study evaluating aid for trade found some benefits for trade from aid for trade programs, but did not even attempt to assess what the impact was on poverty reduction.[70] Earlier World bank modelling, not based on actual impacts, suggested that aid for trade would alleviate inequality across regions[71], but this is yet to be confirmed by empirical measurement.

The establishment of economic processing zones is an example of where there may be few if any benefits to the recipient country. In some cases the investment in infrastructure by the recipient country combined with generous tax incentives to foreign companies using the economic processing zone have not necessarily led to an increase in FDI. Even where FDI has been forthcoming, value-added has often been low, and backward linkages and technology transfer quite limited. Overall, the impact of most of these zones in Africa, particularly on local economic development, has been ambiguous at best.[72]

Pacific islands have seen a number of failures in aid for trade initiatives, before being called such. A number of export ventures were begun with foreign capital in five small-island nations during the mid-1980s. Once the subsidies stopped flowing, however, these export projects (including Cook Islands orange juice and Niuean passion fruit) begun in the name of development died.[73]

Further even strong advocates for aid for trade, such as the OECD and the World Trade Organisation admit that some donor countries use aid for trade programs to benefit their companies. For example, most incentive schemes that cover up-front investment costs and address information asymmetries tend to be provided to firms in donor countries.[74] A scheme instituted by Finland, Finpartnership, offers financial seed money and advisory services for Finish companies to start and implement their business operations in developing countries. When the New Zealand Partnerships for International Development Fund was introduced, a challenge fund was established open to New Zealand organisations in the charitable, not-for-profit, private and state sectors.[75]

---

[69] OECD/WTO (2013), 'Aid for Trade at a Glance 2013: Connecting to Value Chains', http://dx.doi.org/10.1787/aid_glance-2013-en, p. 97.
[70] Olivier Cadot, Ana Fernandes, Julien Gourdon, Aaditya Mattoo and Jaime de Melo, ' Evaluating Aid for Trade. A Survey of Recent Studies', The World Bank Development Research Group, Trade and International Integration Team, Policy Research Working paper 6742, January 2014.
[71] Maria Berrittella and Jian Zhang, 'A Global Perspective on Effectiveness of Aid for Trade', The World Bank Development Economics Vice Presidency, Operations and Strategy Unit, Policy Research Working paper 6126, July 2012.
[72] OECD/WTO (2013), 'Aid for Trade at a Glance 2013: Connecting to Value Chains', http://dx.doi.org/10.1787/aid_glance-2013-en, p. 100.
[73] Francis Hezel, 'Pacific Island Nations. How Viable Are Their Economies?', Pacific Island Policy 7, East-West Centre, 2012, pp. 8-10.
[74] OECD/WTO (2013), 'Aid for Trade at a Glance 2013: Connecting to Value Chains', http://dx.doi.org/10.1787/aid_glance-2013-en, p. 46.
[75] OECD/WTO (2013), 'Aid for Trade at a Glance 2013: Connecting to Value Chains', http://dx.doi.org/10.1787/aid_glance-2013-en, p. 46.

The OECD and the WTO warn against using aid for trade to re-introduce tied aid to benefit businesses in the donor country as:[76]

> *Whether aid is disbursed on condition that partners use it to procure goods, works and services from suppliers based in a donor country has consistently been identified as a key test of donors' commitment to effective aid delivery. It has been clearly documented that tying aid raises the cost of many goods, works and services by 15 to 30 percent on average. This is a conservative estimate of the overall costs, as it does not incorporate indirect costs. Ties aid often results in higher transaction costs for partner countries and is at least partially guided by commercial considerations, which do not necessarily meet local needs and priorities.*

Schulpen and Gibbon (2002) critically reviewed private sector development policies, arguing that they were shaped mostly by the nature and interests of the private sector in donor countries themselves, incorporated a high proportion of tied aid, and failed basic tests of coherence. Most recent reviews are more positive.[77]

Recommendation: Any diversion of aid spending into new aid for trade programs should be proceeded by thorough analysis of how the benefits of the program will lead to sustainable poverty reduction, rather than assuming poverty reduction will automatically result.

Overseas aid should not be used as subsidies to Australian companies in a return to tied aid, as this undermines the efficiency of aid to reduce poverty.

9. Aid Fungibility

One of the attacks mounted against foreign aid is that it is fungible, that is the recipient government may divert funds from providing essential services because of aid being provided by donor governments. World Bank research that accounted for both on-budget and off-budget aid in the education and health sectors found that there is little evidence that aid is fully or even largely fungible.[78] The work concluded that in both sectors, technical cooperation leads to, at most, a small displacement of a recipient's own public spending.[79] No firm conclusions could be drawn with respect to the fungibility of sector program aid. However, as technical cooperation is the dominant modality in both sectors, it plays a large role in determining the overall degree of fungibility of earmarked education and health aid.[80]

The World Bank study concluded that the lack of fungibility may be a consequence of effective donor conditionality. If donors are able to monitor the spending of recipient governments, then they may be able to credibly enforce the condition that aid adds to the resources that are spent in the targeted sector.[81]

---

[76] OECD/WTO (2013), 'Aid for Trade at a Glance 2013: Connecting to Value Chains', http://dx.doi.org/10.1787/aid_glance-2013-en, p. 52.
[77] OECD/WTO (2013), 'Aid for Trade at a Glance 2013: Connecting to Value Chains', http://dx.doi.org/10.1787/aid_glance-2013-en, p. 48.
[78] Nicolas Van de Sijpe, 'Is Foreign Aid Fungible? Evidence from the Education and health Sectors', The World Bank Development Economics Vice Presidency, Partnerships, Capacity Building Unit, Policy Working Paper 6346, January 2013, p. 26.
[79] Nicolas Van de Sijpe, 'Is Foreign Aid Fungible? Evidence from the Education and health Sectors', The World Bank Development Economics Vice Presidency, Partnerships, Capacity Building Unit, Policy Working Paper 6346, January 2013, p. 26.
[80] Nicolas Van de Sijpe, 'Is Foreign Aid Fungible? Evidence from the Education and health Sectors', The World Bank Development Economics Vice Presidency, Partnerships, Capacity Building Unit, Policy Working Paper 6346, January 2013, p. 26.
[81] Nicolas Van de Sijpe, 'Is Foreign Aid Fungible? Evidence from the Education and health Sectors', The World Bank Development Economics Vice Presidency, Partnerships, Capacity Building Unit, Policy Working Paper 6346, January 2013, p. 26.

An earlier study by the UN University World Institute for Development Economics Research found three generalisations were supported by the evidence around aid fungibility: aid finances government spending; the extent to which aid is fungible is over-stated and even where it is fungible this does not appear to make the aid less effective; and there is no systematic effect of aid on tax effort. Beyond these conclusions the fiscal effects of aid are country-specific.[82]

The OECD has also argued their own research has found no compelling evidence that ODA has a consistent disincentive effect on tax collection in recipient countries. On the contrary, several recent and well-founded studies found a negligible or even positive impact of aid on tax revenue.[83]

10. The Importance of the Environment

We are deeply concerned by the current Government's decision to almost completely stop all funding for development programs within the aid budget. This seems out of step with most international thinking on development and poverty reduction.

Environmental sustainability is crucial in the struggle to reduce global poverty. In the words of the OECD:[84]

> *Today's global growth is taking a heavy toll in the form of environmental degradation and we are approaching or even overstretching our planetary boundaries. This has profound significance for both present and future generations – but particularly for the poor, who are the most dependent on nature for food, livelihoods, energy, security and health. The poor and the disadvantaged are also the most vulnerable to the negative consequences of climate change. Managing the natural resource base – soil, water, biodiversity and other precious elements – and improving well-being while preserving local ecosystems and habitats is of primordial importance for poor people. OECD countries have an obligation to deliver on their international commitments to reduce greenhouse gases and to mobilise USD 100 billion each year, starting in 2020, to counter the effects of climate change in the South.*

The Australian Government had previously committed to supporting climate change finance within the Busan Partnership for Effective Development Co-Operation through which it had committed to:

> *Continue to support national climate change policy and planning as an integral part of developing countries' overall national development plans, and ensure that – where appropriate – these measures are financed, delivered and monitored through developing countries' systems in a transparent manner.*

While it is not always easy to balance poverty reduction with environmental sustainability, important progress is being made. For example, over the past decade Brazil has greatly reduced extreme poverty and inequality while at the same time cutting deforestation by 80%.[85]

---

[82] Oliver Morrissey, 'Aid and Government Fiscal Behaviour. What Does the Evidence Say?', UN University, World Institute for Development Economics Research, Working Paper No 2012/01, January 2012.
[83] OECD, 'Fragile States 2014. Domestic Revenue Mobilisation in Fragile States', February 2014, p. 67.
[84] OECD, 'Development Co-operation Report 2013. Ending Poverty. Highlights', 2013, p. 5.
[85] OECD, 'Development Co-operation Report 2013. Ending Poverty. Highlights', 2013, p. 5.

Recommendation: Funding should be restored to environmental programs in the aid budget where these are important for sustainable poverty reduction.

11. Pacific Islands

Some Pacific countries have limited opportunities for rapid economic development, a conclusion shared by the previous Australian Government.[86] Unfortunately, this has led some of them to pursue development through the flawed model of seeking to be secrecy jurisdictions providing offshore banking services and with highly questionable adherence to international anti-money laundering standards.[87] In the 2013 Financial Secrecy Index compiled by the Tax Justice Network, Samoa was the worst country in the world for financial secrecy with a secrecy score of 88 out of 100, with Vanuatu second worst on a secrecy score of 87, Nauru was equal ninth worst with a secrecy score of 79 and the Cook Islands equal 11th worst with a secrecy score of 77. These Pacific Island states ranked far worse that traditional notorious secrecy jurisdictions like the Cayman Islands and the British Virgin Islands. It is not in Australia's interests to see the emergence of secrecy jurisdictions on its doorstep that may become growing havens for all sorts of illicit flows and may even assist Australians in laundering the proceeds of criminal activity. Vanuatu has already been used by Australians engaged in tax evasion with the Australian Taxation Office in 2008 identifying over $90 million in allegedly false deductions being siphoned through Vanuatu.[88]

This provides one reason for Australian aid to assist in the development of Pacific nations.

Hezel (2012) also argued that Tuvalu, Kiribati, Nauru, Micronesia and the Marshall Islands have low export earnings, struggling tourism and moderate remittances and thus lack any substantial source of foreign income.[89] Tuvula, Micronesia and the Marshall Islands each have over 60% of their government revenue coming from aid.[90] Kiribati and Palau have over 40% of their government revenue provided by foreign aid. Hezel concludes that notwithstanding the best efforts of all Pacific Island nations, many of them will continue to be dependent on foreign aid to make them viable as modern nation-states as they do not have other options available to them.[91]

Dr Mark Zirnsak
Director
Justice and International Mission Unit
Synod of Victoria and Tasmania
Uniting Church in Australia

[86] Francis Hezel, 'Pacific Island Nations. How Viable Are Their Economies?', Pacific Island Policy 7, East-West Centre, 2012, pp. 8-10; and Senator the Hon Bob Carr, Minister for Foreign Affairs, 'Budget. Australia's International Development Assistance Program 2013-14', 14 May 2013, p. 15.
[87] Francis Hezel, 'Pacific Island Nations. How Viable Are Their Economies?', Pacific Island Policy 7, East-West Centre, 2012, p. 15.
[88] Australian Taxation Office Media Release, 'Tax Commissioner warns against using tax evasion arrangements in Vanuatu', 7 May 2008
[89] Francis Hezel, 'Pacific Island Nations. How Viable Are Their Economies?', Pacific Island Policy 7, East-West Centre, 2012, p. 21.
[90] Francis Hezel, 'Pacific Island Nations. How Viable Are Their Economies?', Pacific Island Policy 7, East-West Centre, 2012, p. 22.
[91] Francis Hezel, 'Pacific Island Nations. How Viable Are Their Economies?', Pacific Island Policy 7, East-West Centre, 2012, p. 27.