

# THE DUTCH GOOD GROWTH FUND

## WHO PROFITS FROM DEVELOPMENT COOPERATION?



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# 1 SUMMARY AND RECOMMENDATIONS

The Dutch Good Growth Fund (DGGF), initiated by the Dutch government, will commence in 2014. The DGGF issues export and investment financing to Dutch and local businesses for activities in developing countries. This briefing has been written in response to the recently published memorandum for the Dutch parliament, called *'Ondernemen voor ontwikkeling' (Business for Development)*, which provides detailed information about the DGGF. The starting point for evaluating this memorandum is the fact that the fund must safeguard the principles of development cooperation in all cases.

The DGGF is designed as part of the broader trend in which the Minister of Foreign Trade and Development Cooperation is constantly on the lookout for win-win situations that benefit both Dutch companies and poor people in developing countries. But although the budget for private sector development is one of the few lines within the Minister's budget to increase, the guarantees for the latter group often seem insufficient. The fund raises several questions, for instance with regard to development relevance and tied aid. It also comes with substantial risks that should be covered by proper safeguards and accountability mechanisms. With the choice of supporting its own private sector to invest in developing countries, the Netherlands is one of the first countries in Europe to abandon international agreements on untying aid.

This briefing offers concrete recommendations for improving the policy and aligning it with internationally accepted standards and best practices. This is crucial in order to enhance the chance of potential positive effects and prevent negative consequences.

## 1 Development relevance

Development relevance involves more than enhancing employment and production capacity alone, as proposed in the memorandum. Combating inequality and stimulating inclusivity, sustainable growth, local innovation and the empowerment of vulnerable groups cannot be excluded from the applied definition. Demand-drivenness and a focus on local smaller (female) entrepreneurs and inclusive business models are essential.

Exclusive support to Dutch companies which do not have development objectives does not constitute development cooperation and should not be supported by the DGGF. In addition to providing untied aid, responsiveness to local needs and demands in developing countries and consultations with stakeholders are indispensable elements in realising development relevance.

### Recommendations

Tracks 1 and 3 of the DGGF (see paragraph 2.1) should be open to companies from other countries, preferably companies from low and middle-income countries. For the DGGF to be development relevant a revision of the definition of development relevance and an increased demand-drivenness are required. Moreover, the DGGF should be monitored and evaluated for its connection to the needs of the receiving country and local communities, as well as to advancing development goals such as food security.

## 2 Export financing and debt burden

Export financing in the DGGF does not have a development goal, but is only aimed at supporting the Dutch private sector in doing business abroad. It is odd that, within the framework of the DGGF, these types of financing activities, which should be placed at a (development) bank, are assigned to an insurer such as Atradius DSB. With the lack of development goals, stimulating export via Dutch SMEs to low and middle-income countries is rarely development relevant in the current practice of Atradius DSB. Because a large part of bilateral debts of built up by developing countries results from damage covered by export credit insurance, and because when debts are cancelled they are financed by the Dutch development budget, it results in a negative development impact regarding export credit insurance.

### Recommendations

As Atradius DSB does not have a development mandate, it should not be given a managing position of development funds. The possible acquittal of debts that are built up via export financing from the DGGF should be covered by the proceeds of the fund and not by the development budget. Additionally, the development relevance of export financing should be established and made public.

### 3 CSR standards

The government should be able to provide guarantees to prevent 'doing harm' in the realisation of the DGGF by establishing and applying clear and standardised CSR criteria. The effects of these criteria should be closely monitored and evaluated. The proposed noncommittal and ambiguous application of CSR standards is not in line with this goal and provides insufficient guarantees and leads.

#### Recommendations

The IFC Performance Standards should be applied in full at the project level, and not just in the initial review. A more specific focus and guidelines are required within the framework of high-risk investments such those that affect land rights. In the realisation of the DGGF, the government and executors (plus the companies involved) should be accountable for 'due diligence'. The government should ensure transparency with regard to the taxes transferred by subsidised companies in the production country.

### 4 Transparency, stakeholder involvement and grievance mechanisms

Transparency and accountability are key issues in the proper realisation of the DGGF. Based on this idea it is a positive fact that the establishment of grievance mechanisms and transparency standards, as well as the involvement of various (local) parties are included in the memorandum. The issue requires further elaboration, however.

#### Recommendations

Both on the project level and the decision-making level, the government should aim for maximum transparency within the DGGF, inspired by the 'disclosure policy' of the IFC. Stakeholder involvement should be an integral part of the DGGF, combined with the establishment of a proactive, independent, impartial and transparent grievance mechanism for the intended government support to private sector investments, possibly as part of the NCP.

The implementation of the DGGF in early 2014 should be seen as an opportunity to start a continuing critical discussion about the functioning of the private sector in development cooperation. This briefing aims to contribute to this concept in a concrete and constructive way.



Both ENDS is an independent NGO that aims to stimulate a sustainable future for our planet. For more information, see [www.bothends.org](http://www.bothends.org).



ActionAid is an international non-profit organisation that is active in over 40 countries. It has its head office in Johannesburg.

For more information, see [www.actionaid.nl](http://www.actionaid.nl).



The Centre for Research on Multinational Corporations (SOMO) is an independent not-for-profit research and networking organisation.

For more information, see [www.somo.nl](http://www.somo.nl).

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The FGG Alliance supports civil society organisations – in developing countries and emerging economies – that support the interests of local populations and thus a socially justified and ecologically sustainable development. Additionally we aim for increased policy coherence in Dutch and European policies through research and advocacy.

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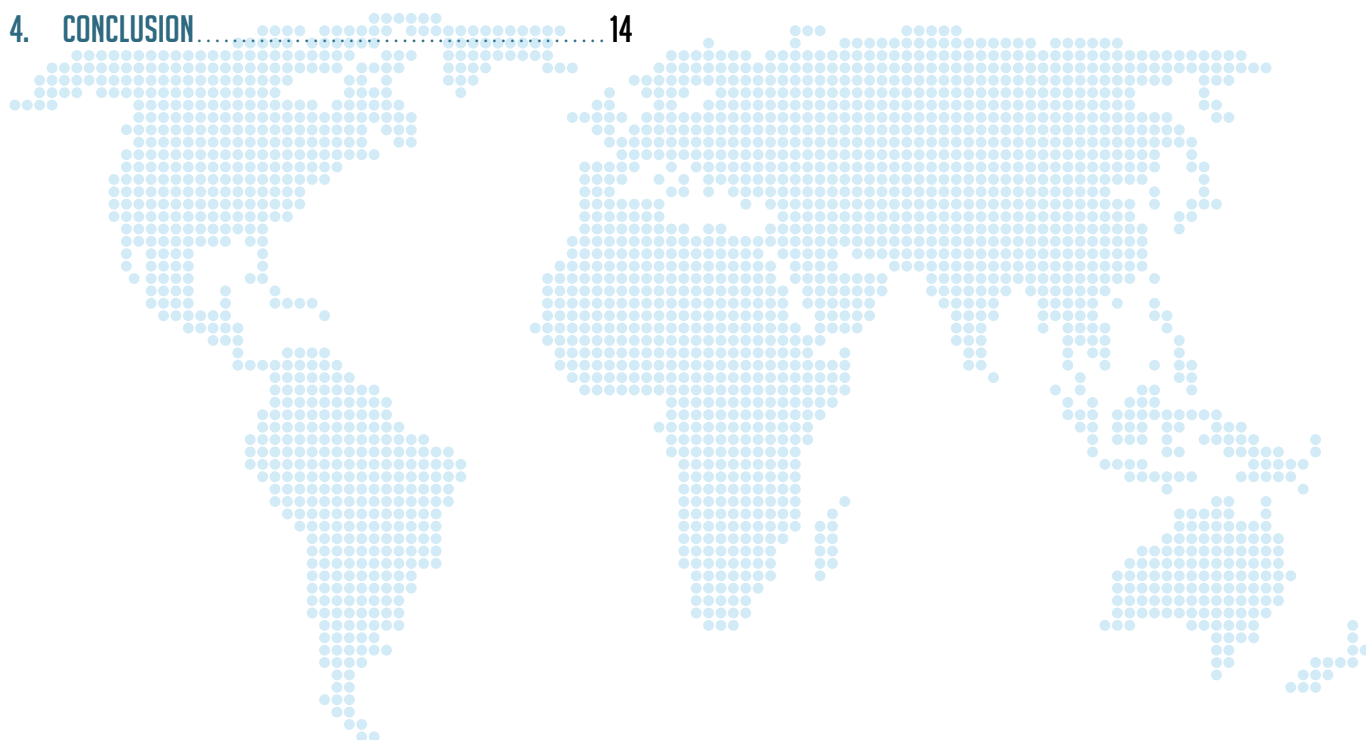
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## 2 INTRODUCTION

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The Dutch Good Growth Fund (DGGF) will commence in 2014. The DGGF issues export and investment financing to Dutch and local businesses for activities in developing countries. The fund is an important cornerstone in the development policy of the current Dutch Cabinet, which has a major focus on private sector development. Despite continuing cutbacks for nearly all segments (such as education, health care and civil society) within development cooperation, the Cabinet will be spending a substantial and growing budget on the private sector in coming years. A large part thereof is intended for the exclusive direct and indirect support of the Dutch private sector. The fund is part of the broader trend in which the Minister of Foreign Trade and Development Cooperation is constantly on the lookout for win-win situations for both Dutch companies and poor people in developing countries. The guarantees for the latter group often seem insufficient, however. The increased coherence between trade and cooperation is indeed relevant, but it is currently mainly being implemented by adjusting it to the needs of the Dutch private sector. Policy coherency for development, the systematic analysis of economic foreign policies (including all types of direct and indirect corporate support, such as trade and investment treaties) with regard to negative impact on developing countries and the adjustment thereof where necessary is not taken on board as enthusiastically.

One of the most remarkable elements of the DGGF is the implementation of export financing. The transparency regarding existing export credit insurance is extremely limited, both in the Netherlands and on a global level. Moreover, the way export credit agencies (ECAs) are administrated is actually paid for by developing countries: the majority of their bilateral debts (over 80 percent) results from export credit insurance costs that are passed on to them. Eventually, those debts are often acquitted, and the money to do so in the Netherlands is drawn from the development budget; regardless of the fact that ECAs are not required to provide any form of development relevance. Until now, it has been impossible in the Netherlands to host a public debate on this instrument, despite the fact that the public means spent on this are many times higher than the total development cooperation budget.

In this briefing we translate lessons learned from many years of experience with export credit insurance and research into the effects of investments on local communities and the environment in developing countries into recommendations for the DGGF.

This briefing was written in response to the recently published memorandum for the Dutch parliament, called 'Ondernemen voor ontwikkeling' (Business for Development),<sup>1</sup> which mainly addresses the Dutch Good Growth Fund. The starting point for evaluating this memorandum is the fact that the fund must safeguard the principles of development cooperation in all cases. In this framework, it is crucial to continue to focus on the role and added value of the (Dutch) private sector within local development processes. This also requires a more detailed definition of development relevance and the development impact of this fund and individual projects, especially for the poorest groups. Additionally, it is important to include preconditions such as a wider (economic) transformation, inclusivity, ecologic sustainability and respect for laws and regulations<sup>2</sup> as well as sufficient control mechanisms (partly as a result of a strong civil society).<sup>3</sup> The briefing was partly developed after consultation with southern organisations<sup>4</sup> and it is based on prior lessons and recommendations in the field of private sector financing.<sup>5</sup> First, we will outline the principles of the fund (1), before addressing a number of general points of interest and preconditions for private sector development, including development relevance, export financing and debt burden, CSR standards and transparency, stakeholder involvement and grievance mechanisms (2), and, finally, we present our conclusion (3).

### 2.1 THE OUTLINES OF THE DGGF

The goal of the DGGF is intensifying development relevant investments and trade in and with low and middle-income countries. The fund provides financing opportunities for this purpose to Dutch businesses, and, via financial intermediaries, to businesses in low and middle-income countries. Both small and medium-sized companies (SMEs) as well as large-scale businesses can be eligible for financing from the DGGF. The DGGF offers financing in the form of loans, guarantees and share participations, and aims for 100% repayment. The fund is powered by the Foreign Trade and Development Cooperation (BH&OS) budget at an amount of € 750 million. The government has indicated it aims to reduce the original budget for DGGF in 2014 and 2015 from € 250 million to € 100 million, and compensate it from 2016 onwards. An amount of € 175 million will be provided per fund segment. The remaining € 225 million is kept separate from the budget and will be divided over the three tracks based on an interim evaluation. Related to the fund, an additional € 75 million is available for technical support. This technical support as well

as broader accompanying policies will not be financed by the fund (despite requests from parliament) but from the regular private sector development budget.

The structure of the DGGF consists of the following three tracks:

► **Track 1**

The first track of the DGGF is focused on supporting direct investments of Dutch companies abroad. This part of the fund is managed by Agentschap NL (NL Agency).

The fund is intended to finance investments that cannot be accommodated in the private capital market due to their high risk profiles. It provides guarantees on loans from Dutch financiers. In situations where private financiers cannot support Dutch investors, the fund offers direct financing for loans or participations to the Dutch private sector. In addition to the investment capital of € 175 million a total of approximately € 18 million will be made available for technical support.

► **Track 2**

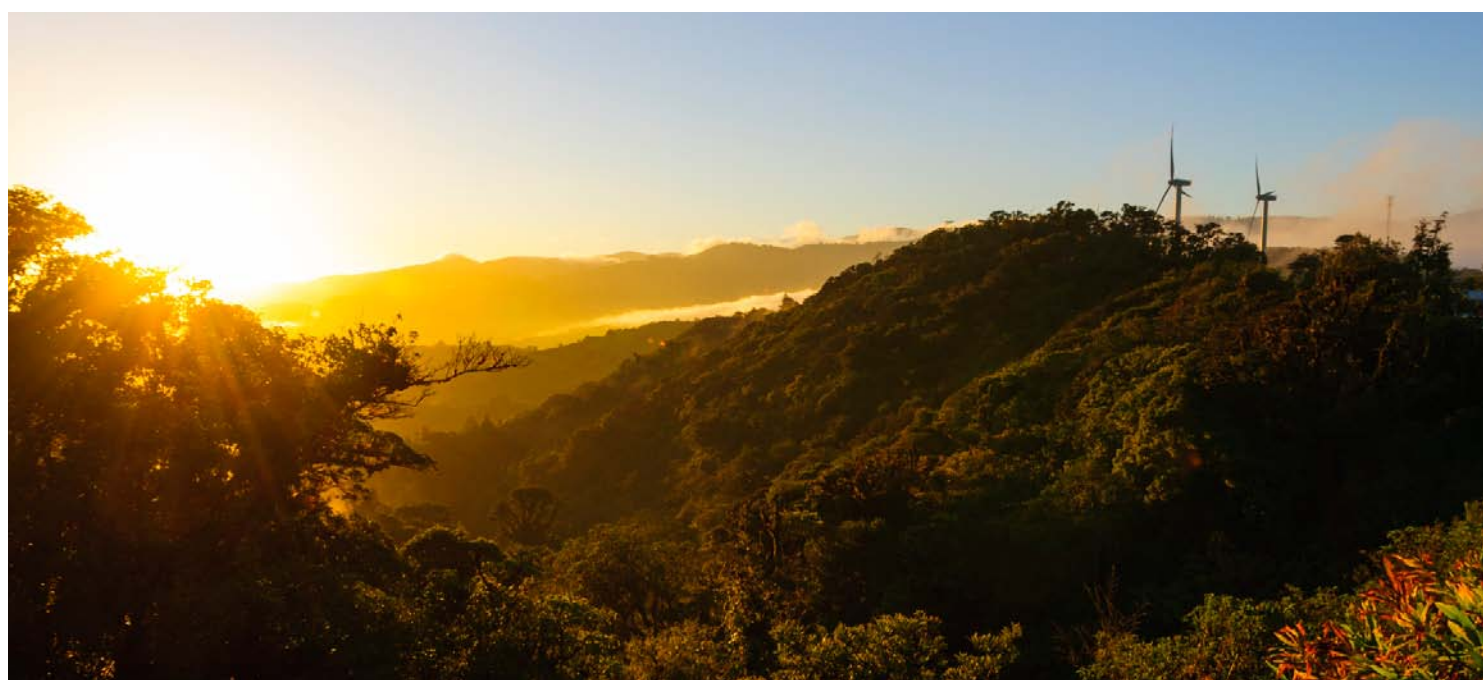
The second track aims to promote the financing of SMEs in low and middle-income countries; not directly but via private investors and financial intermediaries. A financial contribution from the DGGF always represents a minority share and is issued in various ways: as share capital, first loss protection (covering first losses), guarantees, (subordinated) loans or convertible loans. The basis is always an investment period of three to five years with a financing term up to ten years. The maximum amount per investment is ten percent of the total available investment capital for track 2. In addition to an investment capital of € 175 million, approximately € 26 million will be made available to this segment of the DGGF for technical support over

the period 2014-2017. At the time of writing, a specialised market party is being sought to manage this track.

► **Track 3**

The third track is focused on stimulating development relevant export to low and middle-income countries by Dutch SMEs. It involves risky transactions in which banks are not willing to provide financing without export credit insurance (ECI). The DGGF provides financing to companies in low and middle-income countries that are willing to purchase Dutch products. The fund focuses on export transactions up to € 15 million that are currently not supported by the market or regular governmental ECI facilities due to the geographical position, term, or nature or scope of the transaction. This segment of the fund is managed by Atradius Dutch State Business, the company that also executes existing ECI facilities. In addition to the investment capital of € 175 million, a total of approximately € 9 million is reserved for technical support for the 2014-2017 period.

The memorandum includes a number of progressive elements such as commitments in the field of sanction mechanisms and measures against tax evasion. The current effect of these issues is inadequate, however. This also applies to the (in principle admirable) commitment that fund managers will actively search for favourable initiatives for young and/or female entrepreneurs or companies in fragile countries. Unfortunately, this ambition lacks a clear goal, specific setup or budgetary earmark. Such essential (pre)conditions for development relevant private sector development should be clearly laid out in order to anchor and measure development effects.



# 3 POINTS OF INTEREST AND SHORTCOMINGS IN THE CURRENT SETUP OF THE DGGF

## 3.1. DEVELOPMENT RELEVANCE: AIMING FOR CLEAR PRIORITIES

The memorandum includes various promising prospects and goals in the field of poverty reduction and combating inequality.<sup>6</sup> Development relevance is stated as being an absolute condition. The definition and detailing of development relevance by the Minister is unfortunately very minimal. The OECD describes development relevance as the level in which an activity is in line with the priorities of the target group, the receiving country and the donor itself.<sup>7</sup> In this framework it is essential to clearly define and monitor the interests of the target group and the desired effects. Demand-drivenness and (local) stakeholder involvement are also important process conditions.<sup>8</sup> This is not included in the current setup. Despite the Staij resolution on effects on the poorest people<sup>9</sup>, there is hardly any focus on how these people benefit from the involvement of the DGGF.

### Tied aid and local risks

There is a major risk of development relevance being undermined by the large emphasis on the economic interests of the Netherlands due to the setup of the DGGF. Two of the three tracks are exclusively available to Dutch companies, a unique situation within the Dutch development policy of the past decades. This means the reintroduction of tied aid, which has been shown to be many times less effective than untied aid.<sup>10</sup> Tied aid is at odds with the goal of maximising the development relevance of investments and agreements made in Busan, Paris and Accra on the use of development funds.<sup>11</sup> In 2002, the UK regulated by law that development funds cannot be issued via tied aid.<sup>12</sup> The memorandum suggests that supporting Dutch companies with export and investment financing contributes to a sustainable economic development in developing countries. This claim, however, is not substantiated. There are major arguments against the statement that self-interest goes hand in hand with development goals. Firstly, funds that are issued to Dutch companies cannot be used for other purposes and people in developing countries. It completely ignores the increasing inequality that results from the current Dutch and international trade and investment policy, which is one of the greatest challenges of the 21st century. Secondly, there is a sizeable risk that local economic development is impeded by creating an unfair competitive position for Dutch companies.<sup>13</sup> Foreign companies do not necessarily take into account existing local companies, which

means that local companies can be forced out by foreign ones as the latter have more experience, a better access to the international market, and more means for investments.

### Definition of development relevance is too limited

Minister Ploumen defines development relevance of investments as a contribution to employment, improved production, and knowledge transfer.<sup>14</sup> Although these are relevant sub-goals, they imply a very limited definition with insufficient guarantees for positive impact on combating poverty and inequality, and contributing to sustainable social and ecological development. Recognised principles – like combating inequality, promoting inclusivity, and stimulating sustainable growth, local innovation and the empowerment of vulnerable groups – are not included among the indicators for development relevance.<sup>15</sup> An integrated analysis of both positive and negative effects on clearly defined target groups (at least gender differentiated and with a focus on the very poorest) is crucial, but lacking from the current setup. The link to and coherence with the Dutch focus areas for development cooperation such as food security and water is also lacking, which results in both risks and missed opportunities. It is important, for instance, to prevent a unilateral focus on global chains, as it acts counter to the development of inclusive local and national chains that are essential to food security.<sup>16</sup>

Proper focus: aiming for inclusivity and local small businesses SMEs commonly have a better position than large-scale businesses for ensuring CSR and inclusive business, including the establishment of equal partnerships with, say, the informal sector such as (associations of) small-scale agricultural and micro-companies<sup>17</sup>. Nevertheless, the contribution to combating poverty and increasing income equality is not automatic or guaranteed for SMEs either, and it requires additional support.<sup>18</sup> Investing in local SMEs provides the best opportunities for development relevance, especially when aiming for smaller (female) entrepreneurs and involving communities. Such a bottom up approach also reduces risks regarding elite capture; which often takes place because political elites in many countries have a direct interest in the private sector, and especially in the large and medium-scale segment.<sup>19</sup> It is a positive point that the Minister specifically demands a focus on young, female and smaller businesses, but it requires a more prominent effort and execution. There is, for example, a huge potential for associations, for small-scale female farmers, for instance, to develop into formal female-managed

## PARTNERSHIPS THAT BENEFIT SMALL-SCALE (FEMALE) FARMERS<sup>20</sup>

Although only few positive inclusive business experiences have been properly documented, an example from Mozambique is relevant to the possible application of the DGGF. Five associations with a total of 400 small-scale pineapple farmers (including 130 women) were trained and supported in a pilot project. With the aid of an NGO, the associations developed into actual businesses. They were also supported in identifying local and export markets. The first was realised through participative market research, the second through the establishment of partnerships with an SME that provided transport and refrigeration facilities as well as export capacity. By tapping into new markets in Beira and Maputo (hundreds of kilometres away) at the harvesting peak and establishing points of sale, the associations managed to receive up to 20 times as much (from 1 to 20 cent per kilo) for their 22,000-ton yield in two growth seasons. The partnership with the SME resulted in weekly sales of around 7 tons for € 0.13 per kilo in the harvesting season, and yielded as much as € 14,560 in a year and an average of € 36.40 per household. It is important that diversification was maintained: in addition to pineapples (for various markets) the households also grew their own food crops and most also had incomes from caju nuts.

The pilot project showed that by tapping into more strategic and more diverse markets, incomes increased and risks were spread more evenly. A very important aspect herein is the choice of company and the setup of an equal partnership. It helped that the company had experience with other associations, such as those involved in fair-trade litchis. If food security is guaranteed, the presence of an SME with a strong CSR policy and added values such as transport and refrigeration facilities and export capacity can contribute to development. Empowerment, technical assistance and accompanying policies are essential in ensuring success in these types of partnerships.

or gender-equal SMEs.<sup>21</sup> This does require insight into the context and obstacles for these groups, long-term support and facilitation, however – preferably by non-profit organisations or governments – as well as flanking policies for economic empowerment and sustainable company development.<sup>22</sup> In addition to increasing opportunities, it is important that the position and level playing field for small businesses and micro-companies, such as small-scale female farmers, are not undermined by (larger) financing by the fund. Possible risks for this latter group should be covered more specifically by conditions and accompanying policies.

### Recommendations

- ▶ Tracks 1 and 3 should be opened up to companies from other countries, preferably to companies from low and middle-income countries. Moreover, within the OECD/DAC framework, the Netherlands should refrain from promoting the admission of support to national businesses under the DAC criteria.
- ▶ Development relevance should be defined in a broader and more specific way, and there should be better monitoring and evaluation, including, at the very least, a focus on participation, position and wealth, and a broader cost-benefit analysis for more clearly defined target groups (with an extra focus on the poorest and

women), as well as on reducing inequality, and increasing sustainability and coherence with focus sectors such as food security and water.

- ▶ Unfair competition for local (smaller) businesses as a result of support from the DGGF should be prevented. Financing for individual companies and across the three tracks should be analysed in advance by impact assessments and afterwards by evaluations. Where necessary, policies and financing should be adapted accordingly.
- ▶ The DGGF should be demand-driven and be in line with the needs of the receiving country and local communities. This requires stakeholder involvement and the empowerment of target groups, space for the development of alternative, inclusive and community-based business models, as well as a focus on broader economic transformation.
- ▶ Recognising the importance of local smaller, female and young entrepreneurs should be defined in more detail. It is essential to increase opportunities through priority and support for the smaller segment of local SMEs through direct participation in the fund, conditions for equal partnerships with smaller businesses, and the use of accompanying policies to stimulate the transition from micro to small companies and strengthen cooperatives.



## 3.2 EXPORT FINANCING AND DEBT BURDEN

The Dutch export credit insurance facility (EKV) is in the hands of Atradius Dutch State Business (Atradius DSB). On behalf of the Dutch state, this company provides a number of insurances and guarantee products against risks faced by Dutch companies when they do business abroad. This usually involves export transactions with a credit term or implementation term of more than 12 months. In practice it often involves the export of capital goods such as machinery, trucks or vessels or the realisation of contract work. The volume of the transactions supported by Atradius DSB, which has seen substantial growth in the past few years, is a multitude of the Dutch development cooperation budget. If a demand for an export credit insurance is approved, this initially leads to a coverage commitment based on which the financing of a planned transaction can be safeguarded. An insurance policy is issued when the export transaction result in a contract.

Even in times in which many governments advocate the liberalisation of trade and markets, export credit agencies (ECAs) continue to play an undiminished important role in supporting private businesses from industrial countries. ECAs have no development goals and do not have expertise in the field of development cooperation. The loans insured by these ECAs serve the interests of exporters; the interest of receiving countries is secondary. Over 80 per cent of all bilateral debts of developing countries originates from loans supported by ECAs<sup>23</sup>. Possible cancellation of such bilateral debts are at the expense of the official development assistance (ODA) budget. For this purpose, the Dutch government makes a yearly reservation of € 150 million at the expense of the ODA budget<sup>24</sup>. While the DGGF aims to stimulate development relevant export to low and middle-income countries by Dutch SMEs in addition to the regular EKV facility, no additional measures have been provided with regard to the risk of

the build-up of extra debts in developing countries. The Netherlands presents its commitment to the debt sustainability framework of the World Bank and the IMF as a sufficient measure.

An additional concern is the legal obligation of Atradius DSB to operate cost-effectively in the long term. With an accrual accounting method that incorporates existing exposures and operating costs it calculated a total return of € 226 million over the period 1999-2012.<sup>25</sup> Nevertheless, reservations for the eventual writing off of receivables from developing countries (within the framework of debt restructuring agreements) are booked under the ODA budget. In this practice of Atradius DSB, the export interests of the Netherlands are explicitly placed above the interests of development cooperation.

In view of these facts, there are well-founded doubts about the suitability of Atradius DSB as the executor of (parts of) the DGGF. Because Atradius DSB is an insurance institution, it is furthermore remarkable that it has been provided with a fund-providing task.<sup>26</sup> Practices of Atradius DSB show that stimulating export by Dutch SMEs to low and middle-income countries is often not development relevant. The build-up of export credit debts and economic marginalisation of local populations in projects (see the Suape case in the box on the next page) are not precluded in the practices of Atradius DSB.

### Recommendations

- ▶ Because Atradius DSB does not have a development mandate it should not be given management tasks for development finance.
- ▶ The possible cancellation of debts that are built up via export financing from the DGGF should be covered by the premiums and not the development cooperation budget.
- ▶ The development relevance of export financing should be established and made public.

Key data Atradius DSB <sup>27</sup> (amounts in €)			
	2010	2011	2012
Premium	33 million	55 million	57 million
Losses	79 million	19 million	57 million
Proceeds (yield)	131 million	89 million	96 million
Number of requests	194	228	232
Issued total	5,6 billion	8,2 billion	16,6 billion



## GAP BETWEEN SUSTAINABILITY POLICY AND PRACTICE AT ATRADIUS DSB

Both ENDS has conducted research into the social and environmental effects of two dredging projects of Dutch company Van Oord in and near the port of Suape in Pernambuco, Brazil, supported by Atradius DSB<sup>28</sup>.

The dredging resulted in various negative effects, including a loss of income for many traditional fishermen, forced evictions of various families without proper compensation, and the destruction of coral reefs and (mangrove) forests.

In early September 2013 the Suape port authority was fined for violating agreements in the environmental licenses for the dredging activities and the discovery of severely endangered species in the dredging zone. Repeated requests from Both ENDS for reevaluating the project have been denied time and again. The main reasons provided are: a) the dredging activities are nearly concluded, and b) the responsibility for the social effects of the aforementioned activities rests with the local client.

In practice, the project screening by Atradius DSB does not offer any guarantees for preventing infringements of local environmental regulations or losses for the local population.

## 3.3 CSR STANDARDS

Strong standards for corporate responsibility (CSR) are essential in the implementation of the private sector policy of the Dutch government. The memorandum attaches great value to CSR. It is an 'intrinsic condition' and an 'absolute criterium' for the entire Dutch 'aid and trade policy'. In view of the Dutch Cabinet's interest in CSR, it is remarkable that the effect with regard to many aspects is noncommittal, and thus insufficient as a basis for the responsible realisation of the DGGF. The CSR principles that apply to the companies contain several good intentions, but it is unclear how supervision by the executors will be realised. Similar to (development) banks, the fund managers of the DGGF have a due diligence obligation for portfolio management. This is insufficiently recognised and operationalised.

Companies that receive funds from the DGGF are subject to ten ICSR principles, of which four are imposed on the fund managers of the DGGF instead of the companies themselves. These principles are based on the OECD Guidelines. The IFC Performance Standards are used by the fund manager in a first assessment of financing requests. It is positive that the IFC Performance Standards, which formulate clearer criteria for project evaluation than the OECD Guidelines and are more focused on issues such as land rights, are used in the risk analyses. However, it is also important that they are applied in accordance with the standards of the IFC; in the evaluation, in the realisation, and in the execution of projects, always in line with the risk categorisation. This commitment is currently lacking. Additionally it is specifically important for land-related investments that the principle of Free Prior and Informed Consent – the right of communities to take timely, well-informed decisions on projects that affect their land usage – and the 'CFS Guidelines on Land Tenure' are applied (see box on Addax on the next page).

Transparency and the due diligence process is also unjustifiably left to companies in a noncommittal way. This transparency should be a requirement, in accordance with several pre-defined guidelines. Summaries of due diligence should be made public, for instance, so affected groups can be informed of the investment considerations.

A current issue in the implementation of CSR is fair tax systems.<sup>29</sup> The current private sector instruments support companies and investment funds that evade taxes (see box on MBCDF on page 12). The memorandum lists tax evasion as an absolute exclusion criterium. Users of the DGGF are expected 'not to apply artificial constructions to reduce their profits or payable taxes in countries in which the DGGF is available'. Although this is a very positive development with regard to the current

## ADDAX BIOENERGY: THE RISKS OF LARGE-SCALE LAND ACQUISITIONS AND THE IMPORTANCE OF DUE DILIGENCE

Addax Bioenergy in Sierra Leone, partly financed by FMO and other development banks, has often been praised as an example of sustainable, large-scale agriculture for bio-fuels. The company acquired 57,000 hectares of land for a sugar cane plantation, mainly intended for bio-ethanol for the European market. Attempts to properly manage this complex process were insufficient to prevent a negative impact on the 13,000 local residents involved. Research by ActionAid (2013) and others<sup>30</sup> showed that there was no 'Free Prior and Informed Consent' (FPIC) and that the loss of land resulted in increased hunger among many people.

This project underlines the importance of a strong international CSR framework (ICSR) and adequate due diligence, especially with regard to large-scale land acquisitions that are accompanied by major risks. As long as land rights are insufficiently protected it requires restraint and a greater focus on alternatives that put less pressure on natural resources<sup>31</sup> and from which small-scale farmers can benefit. All cases of land acquisition require far-reaching due diligence, including risk analyses, impact assessments, transparency, an adequate implementation of the principle of 'Free Prior and Informed Consent' and mitigation measures and monitoring. In addition to the IFC Performance Standards the CFS guidelines (Guidelines on Land Tenure) are an important tool for protecting land rights with a specific focus on women and community rights.<sup>32</sup>

private sector development policy, the value thereof has yet to be demonstrated in the implementation and in practice. It is important, for example, to indicate clearly what these 'artificial constructions' imply and how this will be tested. Moreover, the policy should apply to all private sector instruments and not just the DGGF. Additionally, preventing tax evasion benefits from maximum transparency on the financial aspects of the transaction. It is therefore important that this commitment is linked to transparency requirements.

### Recommendations

- ▶ The IFC Performance Standards should be applied in full on the project level, in line with the risk categorisation, and not just in the initial assessment. Land investments should be approached with extra reserve and caution in line with the CFS Guidelines on Land Tenure and the principle of Free Prior and Informed Consent in particular.
- ▶ Information about the results of the due diligence process should be provided on the project level. Moreover, in the implementation of the DGGF the government and fund managers, as well as the companies involved, are accountable for due diligence, especially with regard to clearly formulating regulations and monitoring and evaluation processes. It is important that the government accepts this responsibility and provides clarity with regard to the distribution of the responsibilities this obligation entails.
- ▶ The ICSR policy of the executive organs should constantly be tested and adapted where necessary. The Ministry,

or an independent institution such as the NCP or an ombudsman, should supervise the implementation thereof in practice.

- ▶ The government should guarantee transparency with regard to the taxes paid by the financed companies in the country of production. Companies that receive government support should preferably be established in the country in which the investment is made and report on a country by country basis. Other schemes should be motivated (and published).
- ▶ In agreement with the application of the OECD Guidelines for MNEs in the financial sector, financial intermediaries should be subject to chain accountability.

## 3.4 TRANSPARENCY, STAKEHOLDER INVOLVEMENT AND GRIEVANCE MECHANISMS

### Transparency

Maximum transparency in the implementation of the DGGF is imperative, and an important condition for the proper functioning of the required accountability mechanisms within the DGGF. It also enables (local) stakeholders to participate in the decision-making process and in the realisation of activities supported by the DGGF, and allows for public scrutiny. The current private sector instruments and information policy proposed in the memorandum offer insufficient transparency. For the DGGF only already issued financing and transactions will be published on the website of the fund manager.

## MBCDF – DUTCH INVESTMENT FINANCING FOR CONTROVERSIAL PROJECT IN LAOS: THE IMPORTANCE OF CONDITIONS FOR INTERMEDIARIES

The Mekong Brahmaputra Clean Development Fund L.P. (MBCDF) is a private equity fund that is registered in Guernsey (Channel Islands), a tax haven. Established on 6 July 2010, the MBCDF claims to be the first fund aimed at the development of clean energy for the basins of the Mekong and the Brahmaputra. In its first round of fund raising, the fund was promised an amount of US\$ 45 million by leading financial institutions such as the FMO (US\$ 12.5 million), the Asian Development Bank (ADB), Finnfund and BIO. This investment provides insight into a number of important bottlenecks in investment financing by governments; for example in the field of development relevance (see 3.1), evaluation and mitigation of negative consequences on local communities and the environment, and the distribution of responsibilities with regard to due diligence (see 3.3 above).

In early 2011 the MBCDF spent US\$ 3.36 million on 6,285,000 shares in Électricité du Laos Generation PLC (EdL Gen), a company that is mainly focused on increasing the export of electricity. The MBCDF is the third largest foreign investor in EdL Gen. Due to the lack of access to energy for the local population, one could have doubts about the development relevance of this investment. According to the report *Power Surge, The impacts of rapid dam development in Laos*<sup>33</sup> by International Rivers, Laos is experiencing an unprecedented growth in dam projects, driven by the electricity demand of neighbouring countries and foreign investors. It is not directly clear whether the proceeds of these projects contribute to reducing poverty and inequality in the country itself. Lessons learned from previous dam projects in Laos tell a story of bad planning, insufficient compensation and mitigation plans, and broken promises to affected communities. Thousands of people in Laos have been forced to move due to the construction of dams, of which the majority belongs to ethnic minorities. Moreover, downstream from the dams even larger segments of the population were affected due to a substantial decline in the fish stock, flooding, erosion, and problems related to water quality.

For investments via financial intermediaries, such as private equity funds – which is also set to occur in the DGGF – there is often a lack of transparency in the process of due diligence: who is responsible for (adequate) social and environmental impact reports; and who evaluates these reports (see 3.3)? Should communities be affected by the dam projects in Laos it will be difficult to find out whom they should appeal to and which procedures they should follow. Additionally, in current practice, it is possible to avoid the CSR demands that are imposed on financiers (such as the DGGF) for direct project investments through projects that are realised via financial intermediaries.

An information disclosure policy that meets international standards<sup>34</sup> would mean that the projects would be published on the website of the DGGF or the executor 90 days prior to the decision-making moment. Strategy documents, budgets and country analyses of international financial institutions should also be part of the information policy. The public disclosure policy applied by the World Bank, for instance, states: 'Everything is public, unless.' This means that publicity is not only assured on the project level, but also on the levels of policy and decision-making processes.

### Stakeholder consultation

Involving and informing stakeholders in the design and implementation of development cooperation is an important principle in the current policy of the Minister of Foreign Trade and Development Cooperation.<sup>35</sup> It is positive that the memorandum refers to the involvement of various (local) parties, including NGOs and knowledge institutes, but adequate details are lacking. This means that in the practical realisation of projects there is no adequate description of stakeholder involvement. A lack of stakeholder involvement will undermine the potential positive effects of government-supported projects. A recognition for this role is the repeated appeal to NGOs from the Cabinet to analyse the risks and unwanted social effects of government support and take on

the role of watchdog in this process.<sup>36</sup> In the development of the DGGF there has been too little broad consultation, as referred to in the Slob resolution. A reference group was set up, but it mainly includes parties with a direct interest in the implementation of the DGGF and thus does not guarantee a sufficiently independent voice. For a development relevant policy instrument, it is incomprehensible that consultation with interested parties from the south was not included.<sup>37</sup>

### Independent grievance mechanisms

Those affected by possible negative effects of projects financed with the support of the government should be able to use an independent, impartial and transparent grievance mechanism. This is based on international agreements within the United Nations. It is positive that the memorandum of the Minister indicates that the fund managers of the DGGF should apply a grievance procedure and that there should be sanction opportunities in case of violations of ICSR regulations.<sup>38</sup> A grievance procedure can take on various forms, however, and experience has shown that they do not always lead to the opportunity of having grievances evaluated in an independent, impartial and transparent way. It is important that the Minister commits herself to a grievance mechanism that has these characteristics. FMO is currently establishing an independent grievance mechanism. Although the results thereof are as yet unclear, a similar mechanism should be accessible to all elements of the DGGF, including at the local stakeholder level. The memorandum also states that companies who make use of the DGGF should patently be involved in establishing and implementing a CSR policy. It is the government's task to ensure that maintaining an effective grievance mechanism is included in this policy.



## Recommendations

### ► Transparency

The government should aim for maximum transparency in the DGGF, both at the project level and at the decision-making level. This requires the establishment of a public disclosure policy, inspired by the disclosure policy of the IFC. Within the framework of transparency requirements, the government should also ensure that the following issues are made public for all financial support to companies:

- the direct and eventual beneficiary of the project or company;
- key data of the project, including a project summary, the scope of the financing and the physical scope (hectares);
- the way local participation is integrated in the project design and implementation;
- and the fiscal structure of a project or company. A company should be transparent with regard to paid taxes in the production country, with the OECD Guidelines as the minimum criteria.

### ► Stakeholder consultation

The government should integrate stakeholder involvement as a key condition in the DGGF, and develop opportunities for this involvement both in the Netherlands and in developing countries. A commission or project group of relevant stakeholders (companies, NGOs, governments, fund managers) could be established as an effective supervision mechanism.<sup>39</sup> In addition to the required transparency, the government should also ensure sufficient means and capacity for civil society organisations in the Netherlands, and especially in developing countries, to fulfil their role as watchdog, information source and stimulator of better laws and regulations.

### ► Grievance mechanisms

The Dutch government should ensure the development of an independent, impartial and transparent grievance mechanism for government support to private sector investments, in which accessibility to local stakeholders should be a requirement. Another requirement is that companies using the DGGF should set up a grievance mechanism that is accessible to local stakeholders.

## 4 CONCLUSION

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The DGGF aims to stimulate development relevant export and investments. The current setup in the memorandum is too noncommittal, however, and also has shortcomings with regard to ensuring and measuring development impact. The fact that financial support is provided to the Dutch private sector exclusively through the development budget and that the Netherlands is internationally advocating to include this under ODA criteria are incomprehensible choices, but not irreversible ones. In addition to offering untied aid, demand-drivenness, responsiveness to local needs and demands, and consultations with stakeholders are essential aspects in realising development relevance. Development relevance comprises more than employment and improved production alone. Combating inequality and promoting inclusivity, and stimulating sustainable growth, local innovation and the empowerment of vulnerable groups should be included in the applied definition and require serious monitoring and evaluation. Although the potential of smaller (female) entrepreneurs in developing countries is justifiably recognised, a greater focus on a level playing field for this group as well as additional support are crucial to achieve success.

Export financing is the most controversial element of the DGGF because the link to development relevance and demand-drivenness is not easy to make and has not been sufficiently established in the memorandum. Additionally,

the track record of Atradius DSB is inadequate with regard to managing development relevant projects, and to transparency and due diligence. In the field of transparency and due diligence, Atradius DSB (like other ECAs) performs far below the accepted level of development institutions.

In addition to the aforementioned 'doing good' criteria, the government should ensure the preclusion of doing harm by formulating clear, unilateral CSR criteria, including clear transparency and accountability mechanisms. It requires more than the current proposals to guarantee financing based on standards for corporate social responsibility and to prevent violations, involve and inform stakeholders in a transparent way, and manage grievances in an independent way. The proposed noncommittal and vague setup of CSR standards is not in line with this goal, and offers insufficient guarantees and leads. Even the elements that are potentially (very) positive, such as establishing sanction mechanisms and combating tax evasion, are too limited to function as essential preconditions. This briefing provides concrete recommendations to the Dutch government and the fund managers for each track to further improve the policy with regard to these issues and streamline it with internationally accepted standards and best practices. The establishment of the DGGF in early 2014 should be used as the start of a critical discussion about the functioning of the private sector in development cooperation.



## Endnotes

- 1 Ondernemen voor ontwikkeling: investeren in duurzame en inclusieve groei, <http://www.rijksoverheid.nl/documenten-en-publicaties/brieven/2013/09/30/ondernemen-voor-ontwikkeling-investeren-in-duurzame-en-inclusieve-groei.html>, parlement letter, 30 September 2013.
- 2 How this actually turns out depends on the context, but the protection of human rights, including land rights, is an absolute condition. The emphasis in the policy is now often on creating an enabling environment for investors while we prefer to speak of an enabling environment for 'responsible investments', a balance between protecting investors as well as human rights.
- 3 See Byiers, B. (2012) Common or Conflicting Interests: Reflections on the Private Sector for Development Agenda. Discussion paper 131, ECDPM (among others).
- 4 In particular the Advisory Committee van de Fair Green Global Alliance, consisting of six experts in FGG themes, involved in organisations with which the FGG collaborates in Africa, Latin America and Asia.
- 5 ActionAid, Both ENDS, SOMO (2012) 'Bijdrage private sector aan ontwikkeling niet gegarandeerd': [http://somo.nl/publications-nl/Publication\\_3874-nl](http://somo.nl/publications-nl/Publication_3874-nl).
- 6 "is it necessary to remove obstacles that impede development and create opportunities for vulnerable groups in low and middle-income countries to participate fully in economy and society." (p 4). It does not explain which obstacles for vulnerable groups are tackled or how.
- 7 <http://www.oecd.org/dac/evaluation/dacriteriaforevaluatingdevelopmentassistance.htm>
- 8 In a study for IOB, demand-drivenness is formulated as 'The extent to which decisions in the different phases of a development-instrument are based on the preferences of the intended beneficiaries' and requires at least minimum transparency, accessibility and the opportunity for the target group (beneficiaries) to influence the instrument and activities, <http://www.iob-evaluatie.nl/vraagsturing>.
- 9 See <https://zoek.officielebekendmakingen.nl/kst-33625-26.html>.
- 10 For reference see: Easterly, William. 2007. "Are Aid Agencies Improving?" Economic Policy, 22(52): 633–78.
- 11 If it were up to the commitment of the Dutch government to the OECD – where so-called development criteria are defined – this support to Dutch companies could be defined as official development aid (ODA) in the future.
- 12 Tied aid is now illegal in the UK by virtue of the International Development Act, which came into force on 17 June 2002, replacing the Overseas Development and Co-operation Act (1980), [http://en.wikipedia.org/wiki/Tied\\_aid](http://en.wikipedia.org/wiki/Tied_aid).
- 13 In 2011 the Netherlands was made aware of the excess interweaving of development cooperation (and more specifically the private sector policy therein) by promoting Dutch commercial interests by the 'OECD DAC peer review' report. According to DAC members, development goals must come first.
- 14 Wat de wereld verdient, 2013, p. 32. Elders (p 21/22) says that there will be a focus on 'socio-economic impacts, for example with regard to development relevance and CSR' but no further details are provided.
- 15 See <http://www.stakeholderforum.org/fileadmin/files/Beyond%202015%20MDG-SDG%20relationship.pdf> and OECD criteria (footnote 10) (among others). The considerations of economist Amartya Sen with regard to development as 'enlarging people's choices and enhancing human capabilities and freedoms' and the importance of 'empowerment' seems more relevant than ever – in times in which economies grow, but freedom and opportunities for many people do not, but they are completely missing here. The recognition of broad livelihood strategies that go beyond (formal) employment is also lacking while this is essential for agricultural and land related investments, among others.
- 16 Also see civil society reports with regard to the GAFSP, the food security fund of the World Bank, in which the Netherlands is a major donor.
- 17 Van Westen et al. (2013), [http://www.mvonederland.nl/sites/default/files/corporate\\_social\\_responsibility\\_in\\_the\\_agro-food\\_sector.pdf](http://www.mvonederland.nl/sites/default/files/corporate_social_responsibility_in_the_agro-food_sector.pdf); Examples in KIT, Faida MaLi, IIRR (2006), [www.mamud.com/Docs/chains.pdf](http://www.mamud.com/Docs/chains.pdf); On Empowerment in chains.
- 18 Thorsten Beck (2005), <http://www.nber.org/papers/w11224>.
- 19 The latter is often insufficiently recognised or it is ignored which undermines proper management and democratisation and thus a good business climate in the long run. It could also increase inequality, <http://www.oecd.org/dac/povertyreduction/36427804.pdf>.
- 20 Hassam and Wijnhoud (2006) in SNV/ UNDP/ MDPm (2005); Towards MDG Localisation in Africa • Options and experiences. 89-103 [http://www.snvworld.org/sites/www.snvworld.org/files/publications/towards\\_mdg\\_localisation\\_in\\_africa\\_-\\_options\\_and\\_experiences.pdf](http://www.snvworld.org/sites/www.snvworld.org/files/publications/towards_mdg_localisation_in_africa_-_options_and_experiences.pdf); KIT, FaidaMaLi, IIRR (2006), Chain Empowerment ; Supporting African Farmers to develop Markets. 56-61, [www.mamud.com/Docs/chains.pdf](http://www.mamud.com/Docs/chains.pdf).
- 21 Kaaria et al. (2008), Natural Resources Forum 32 (2008) 53–63 and Combaz (2013).
- 22 UNCTAD 'Why micro and small enterprise are not growing', <http://unctad.org/en/docs/poitetebd5.en.pdf>; Women's Economic Empowerment (OECD 2012), <http://www.oecd.org/dac/povertyreduction/50157530.pdf>; Van Westen et al. (2013), [http://www.mvonederland.nl/sites/default/files/corporate\\_social\\_responsibility\\_in\\_the\\_agro-food\\_sector.pdf](http://www.mvonederland.nl/sites/default/files/corporate_social_responsibility_in_the_agro-food_sector.pdf); Ferris et al. (2006), [http://www.crsprogramquality.org/storage/pubs/agnv/mkt\\_facilitator\\_guide.pdf](http://www.crsprogramquality.org/storage/pubs/agnv/mkt_facilitator_guide.pdf).
- 23 Exporting goods or exporting debts? Export Credit Agencies and the roots of developing country debt, December 2011, Eurodad, <http://www.eurodad.org/Entries/view/4735/2011/12/06/Exporting-goods-or-exporting-debts-Export-Credit-Agencies-and-the-roots-of-developing-country-debt>.
- 24 HGIS-nota 2014, p. 24.
- 25 See: Atradius DSB's annual review 2012: [http://www.atradiusdutchstatebusiness.nl/Images/dsben/Annual%20Review%202012%20spread\\_tcm1009-159337.pdf](http://www.atradiusdutchstatebusiness.nl/Images/dsben/Annual%20Review%202012%20spread_tcm1009-159337.pdf).
- 26 Within the framework of financial sector reforms, banking and insurance activities at private financial institutions are currently explicitly separated and placed with individual business (for example, ING).
- 27 See [http://www.atradiusdutchstatebusiness.nl/Images/Jaaroverzicht%202012%20spread\\_tcm1008-159334.pdf](http://www.atradiusdutchstatebusiness.nl/Images/Jaaroverzicht%202012%20spread_tcm1008-159334.pdf).
- 28 Compare to a case study of dredging activities by Van Oord in Suape, Brazil, supported by Atradius DSB: <http://www.bothends.org/nl/Publicaties/document/90/Rapport-Suape>.
- 29 A brief on tax and corporate responsibility, draft principles for CSR & tax van IBIS en Christian Aid, juni 2012.
- 30 ActionAid (2013): Broken Promises, <http://www.actionaid.org/nl/nederland/publications/broken-promises-impacts-addax-bioenergy-sierra-leone-hunger-and-livelihoods>. Also see Baxter 'Who is benefitting: Large scale land investments in Sierra Leone' (2013) and Silnorf Monitoring Report Addax 2013.
- 31 A recent study for CSR Netherlands (Utrecht University 2013) points out the risks of investments that consume large amounts of land and water – such as large-scale plantations for biofuels – and possible priority measures for alternatives that use fewer resources and provide many jobs. [http://www.mvonederland.nl/sites/default/files/corporate\\_social\\_responsibility\\_in\\_the\\_agro-food\\_sector.pdf](http://www.mvonederland.nl/sites/default/files/corporate_social_responsibility_in_the_agro-food_sector.pdf).
- 32 In May 2012 these guidelines for land (use) rights were accepted by the Committee on World Food Security (FAO) with wide support: <http://www.fao.org/docrep/016/i2801e/i2801e.pdf>.
- 33 <http://www.internationalrivers.org/resources/power-surge-the-impacts-of-rapid-dam-development-in-laos-3964>
- 34 For comparison, see the Information Disclosure Policy of IFC and the World Bank, e.g., [http://www.ifc.org/wps/wcm/connect/corp\\_ext\\_content/ifc\\_external\\_corporate\\_site/ifc+projects+database/projects/access+to+information+policy](http://www.ifc.org/wps/wcm/connect/corp_ext_content/ifc_external_corporate_site/ifc+projects+database/projects/access+to+information+policy).
- 35 Wat de wereld verdient, 2013
- 36 [http://www.tweedekamer.nl/ao\\_repo/buza/20120712\\_OS-bedrijfsleveninstrumentarium.pdf](http://www.tweedekamer.nl/ao_repo/buza/20120712_OS-bedrijfsleveninstrumentarium.pdf)
- 37 The Fair, Green and Global Alliance organised a conference call between southern NGOs and the responsible government officials at its own initiative, but no follow-up was given to this by the Ministry later on in the process.
- 38 <http://www.rijksoverheid.nl/documenten-en-publicaties/brieven/2013/09/30/ondernemen-voor-ontwikkeling-investeren-in-duurzame-en-inclusieve-groei.html>, p.23.
- 39 Punten op de I, Oxfam Novib, 2011.

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