Policy Briefing Paper

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No. 25 August 2010

G20 Surrenders to the Money Traders

By John Dillon

The prime ministers and presidents[i] at the Toronto G20 Summit in June acknowledged that "the recovery is uneven and fragile [and] unemployment in many countries remains at unacceptable levels." Nevertheless, they decided to turn away from stimulus spending in favour of austerity measures. With Canada taking the lead, they declared that, except for Japan, the "advanced economies"[ii] would commit to "fiscal plans that will at least halve deficits by 2013 and stabilize or reduce government debt-to-GDP ratios by 2016." [iii] (See the G20 Toronto Summit Declaration, paragraphs 4 and 10.)

By setting this course of action, the G20 leaders caved in to pressure from the same bond and derivative traders whose irresponsible actions had caused the financial crisis in the first place. Instead of reining in the power of finance capital, the summiteers avoided decisions on systemic reform. Even though government deficits are in large part the result of bank bailouts, the G20 refused to endorse taxation of financial transactions, bank profits or traders' remuneration as a source of substantial revenues.

Bruce Campbell, director of the Canadian Centre for Policy Alternatives aptly sums up the Summit outcome: "So the poor and the vulnerable will pay the price of deficit reduction via social program cuts and continued high unemployment. They are collateral damage while the perpetrators get back to business as usual"[1]

Obeying IMF commandments

Conservative commentators are celebrating the abandonment of Keynesian stimulus measures, arguing that a return to fiscal rectitude will lead to an economic revival led by the private sector. Nobel prize-winning economist Paul Krugman responds, "There is no evidence that short-run austerity in the face of a depressed economy reassures investors. On the contrary: Greece has agreed to harsh austerity, only to find its risk spreads growing ever wider; Ireland has imposed savage cuts in public spending, only to be treated by the markets as a worse risk than Spain, which has been far more reluctant to take the hard-liners' medicine."[2]

The International Monetary Fund (IMF) has advised governments on how to make the switch from stimulus to austerity. On June 24, two days before the Toronto Summit, the IMF posted a document on its web site pretentiously entitled "Ten Commandments for Fiscal Adjustment in Advanced Economies."[3] The authors, who are the Fund's research and fiscal affairs directors, do not hesitate to specify the kind of spending cuts they deem most desirable. They recommend cuts to pensions and health care, a shift from universal

[i] King Saud attended the Summit but reportedly Saudi Arabia was not an active participant.

[ii] Throughout the Declaration, the term "advanced economies" is used to differentiate those countries traditionally thought of as "developed" from the so-called "emerging economies," although neither term is precisely defined and the IMF apparently counts South Korea as an advanced economy.

[iii] The Harper government has already pledged to exceed these targets. Its 2010 budget pledges to end stimulus spending after this year, cut the deficit by two-thirds by 2013 and bring down debt to GDP ratio starting next year. Although President Obama had written to the other leaders before the Summit urging them not to abandon stimulus measures prematurely, he accepted the 2013 target as in line with his own budget plans.

to targeted social programs and the containment of public sector wages.

The IMF argues that "fiscal adjustment is key to private investment and long-term growth" despite all the evidence that this strategy failed miserably during its three-decade trial in developing countries.[4] Another IMF paper prepared for the Summit calls for making labour markets more "efficient" in order to increase employment. As Thomas Walkom explains: "In IMF-speak, labour market efficiency is code for removing any social program or regulation – from employment insurance to minimum wage statutes to laws supporting unionization – that prevent wages from being driven down."[5]

After the G20 finance ministers called for fiscal tightening in early June, the managing director of the IMF, Dominique Strauss-Kahn, said he was "totally comfortable" with deficit cuts that would cost an estimated 30 million jobs.[6] But austerity measures that reduce the purchasing power of workers, pensioners and people living on social assistance are counterproductive since they constrain effective demand for basic goods and services. So are the type of tax increases favoured by the IMF such as raising value-added taxes.

Both the IMF and the G20 Declaration ignore options for curbing fiscal deficits that would not exacerbate poverty and unemployment such as progressive taxes on speculative capital or on high-income earners or on carbon-intensive industries. The Harper government, for example, refuses to rescind corporate tax cuts that will cost the federal government almost $14 billion a year.[7] Another option would be to cut unproductive spending on armaments and military adventures. In 2008 world military spending amounted to almost US$1.5 trillion of which two-thirds was by NATO countries.

In Part One of this paper we examine how the sudden shift from stimulus to austerity is a surrender to the bond and derivative traders. Part Two recounts how the G20 failed to agree on a tax or levy to recoup some of the costs of bailing out the financial sector, with special reference to ongoing efforts to establish a Financial Transactions Tax. In Part Three we look at the G20's failure to take meaningful action on reducing subsidies to fossil fuels – something that could simultaneously reduce deficits and fight climate change. Part Four examines the failure of the G20 to address the very real danger of deflation and a prolonged recession through the use of monetary stimulus. Finally, we look briefly at the future of both the G8 and the G20 Summits.

Part One: Appeasing the Bond Traders

What caused the G20 leaders to abandon the fiscal stimulus measures credited with preventing a global depression and instead cut spending to the detriment of the poor, the vulnerable and the unemployed? The Toronto Declaration refers vaguely to "**recent events** [that] highlight the importance of sustainable public finances." (4, emphasis added) These unspecified "recent events" in fact involve a resurgence of speculation on financial markets that has driven down the value of the Euro and driven up the costs of servicing Greek and other European governments' sovereign debts.

Prime Minister Stephen Harper cited the Greek crisis in a letter to G20 leaders in May, warning that bond traders would punish countries that did not have plans for spending cuts: "We can confront our fiscal challenge with clear and realistic plans for fiscal consolidation, or we can wait for markets to dictate the terms for us."[8]

Speculators investing in the same financial derivatives that were at the heart of the 2008 financial crisis associated with the U.S. housing market have played a major role in turning sovereign debt problems into debt crises. Greece's difficulties originated partly because Goldman Sachs helped its previous government use derivative swaps to hide €2.4 billion (Cdn$3.4 billion) from its publicly-reported debt.[9] Subsequently, Greece's debt management challenge was aggravated by speculation on bond and derivative markets.[10] Speculators purchased Credit Default Swaps (CDSs) hoping to make large profits if Greece were to default on its bonds.

CDSs are a type of derivative that is similar to an insurance policy. Sellers of CDSs collect fees for taking the risk that a loan will not be repaid. If a borrower defaults, the purchaser of a CDS stands to collect a substantial profit. But unlike a normal insurance policy, speculators who have no stake in the original loans can purchase CDSs. Moreover, multiple CDSs can be taken out on a single loan or bond. CDSs played a central role in the original financial crisis when their nominal value on packages of mortgages or other similar debts ballooned to US$62 trillion even though the maximum amount of debt they insured was only US$5 trillion.[11]

Greece's debt problem was aggravated when the same speculators who had bought CDSs betting on a default then took "short" positions in the bond market, i.e., selling contracts for future delivery of Greek bonds at lower prices. These short sales have the ef-

fect of driving up the interest rates payable on the bonds. When Greece was already paying an interest rate risk premium of three percentage points above the rates paid by other European countries, billionaire financier George Soros warned that "speculation in CDSs [would] drive the risk premium higher."[12] As interest rates rise, it becomes more expensive to service sovereign debts and the likelihood of a default increases. European Central Bank President Jean-Claude Trichet acknowledged the role of speculators when he said, "By first buying the CDS and then trying to affect market sentiment by going short on the underlying bond, investors can make large profits."[13]

Failure to tame the speculation

At the April 2009 London Summit, the G20 pledged to subject credit derivative markets to effective regulation and supervision.[14] But at the June 2010 Toronto Summit, the leaders failed to take any measures that would substantially curb the power of the money traders.

Instead of taming financial market speculation through strong regulations or a Financial Transactions Tax, the G20 is making government policies subservient to market pressures. If the G20 were willing to take bold actions, it would prohibit the purchase of CDSs on sovereign debt or at least bar their purchase by investors who do not have an interest in the underlying debt. Instead, at Toronto, the G20 promised only to take future actions "to improve transparency and regulatory oversight of hedge funds, credit rating agencies and over-the-counter derivatives **in an internationally consistent and non-discriminatory way.**" (19, emphasis added)

The caution that new regulations must be internationally consistent and non-discriminatory merits special attention. It implies that new regulations must not be more binding than those adopted in the largest economy and ground zero of the financial crisis – the United States of America. The Toronto Declaration explicitly welcomed what it characterized as a "**strong** regulatory reform bill in the United States." (Annex II, 2, emphasis added) In fact, the reforms contained in the bill approved by the US Congress on the eve of the Summit are very weak.

While the 2,300 pages of legislation give the appearance of tougher new regulations, an army of some 2,000 bank lobbyists won significant concessions. Banks will be able to continue to trade most kinds of derivatives, including those involving interest rates and foreign exchange trades, but must establish separate units to handle riskier products. Banks can continue to own hedge funds and private equity trading units holding up to 3% of their core capital.[15]

Here's how *The New York Times* sums up the banks' achievements: "The financial industry won some important victories, even if they face significantly heightened regulation. They fought off some of the toughest restrictions on their ability to invest their own funds … . Industry analysts predicted that banks would most likely adapt easily to the new regulatory framework and thrive. As a result, bank stocks were mostly higher Friday [the day after the bill was passed], prompting some sceptics to question if the legislation, in fact, would be tough enough to rein in the industry and prevent future shocks to the economy as a result of bad gambling. Even architects of the bill acknowledged that it might take the next financial crisis to truly determine the effectiveness of the changes."[16]

At the end of a 20-hour, all-night negotiating session among members of Congress, a provision that would have imposed a one-time US$19 billion fee on banks to cover the costs of the bill was removed to secure the vote of Massachusetts Senator Scott Brown.

Bank lobbyists also water down Basel Agreement

The Toronto G20 Declaration implies that progress is being made on establishing new international standards forcing banks to strengthen their balance sheets by holding more capital in reserve as a safeguard against future financial crises. One reason Canadian banks survived the financial crisis better than their international peers was because they had been compelled to set aside more capital in relation to their assets (their outstanding loans and investments), than is required by the existing rules established by the Basel Committee on Banking Supervision.

The existing framework, known as Basel II, calls for internationally active banks to hold Tier One capital (shareholders equity and disclosed reserves constituting at least half of a bank's capital) equivalent to at least 4% of risk-adjusted assets and total capital amounting to 8% of risk-weighted assets, at a minimum. In Canada, the Office of Superintendent of Financial Institutions requires Canadian banks to hold higher levels of reserves – Tier One capital of 7% of risk-adjusted assets and total capital of 10%. According to the Finance Department, when the financial crisis began, "Canadian banks had average capital buffers of about 9.5 per cent of risk-adjusted assets, while many global banks had capital ratios of only 6 or 7 per cent."[17]

In the wake of the crisis, the G20 asked the Basel Committee to come up with new, uniform rules for both capital requirements and short-term liquidity requirements, i.e., the amount of liquid funds a financial institution has to have on hand to survive severe stress over a 30-day period. Annex II of the G20 Toronto Summit Declaration dealing with Financial Sector Reform states: "We took stock of the progress of the Basel Committee on Banking Supervision towards a new global regime for bank capital and liquidity and we welcome and support its work. Substantial progress has been made on reforms that will materially raise levels of resilience of our banking systems." (Annex II, 6)

This optimistic language fails to reflect how financial industry lobbyists are succeeding in watering down the new Basel rules. On the eve of the Summit, the *Financial Times* ran a story under the headline "Banks win battle for limits to Basel III" which states:

"Plans by global regulators to compel banks to set aside billions of dollars in extra capital to cope with future crises are to be pared back after intense lobbying by the industry. …The most significant change to the proposed reforms concerns the committee's recommendations on the volume of liquid funds that banks should hold to protect them against another financial crisis.

"Proposed short term emergency funding measures will go ahead. But the committee is likely to shelve the idea that banks should be forced to maintain a longer term 'net stable funding ratio' that aligns the maturity of their assets and liabilities. … Analysts had … calculated that the Basel III reforms, were they implemented in conjunction with new taxes around the world – such as the liability tax announced by the UK government – could have cut a typical bank's return on equity from 20% to 5%."[18]

Whereas the new rules were supposed to be agreed to by the end of this year and in place by the end of 2012, at Toronto the G20 said it would only "aim" to meet the 2012 target date and allow longer phase-in periods reflecting "different national starting points and circumstances." (Annex II, 8 and 9)

The longer the G20 delays putting in place new rules for capital and liquidity requirements the weaker these rules become. Research by Oxford University Professors Walter Mattli and Ngaire Woods shows that "the longer politicians wait to implement reforms after a financial crisis, the greater the chance that financial industry lobbyists and other specialists take over the process and water down reforms."[19]

Part Two: Failure to Recoup Public Support for the Financial Sector

The Toronto Summit was to take up the challenge first issued in Pittsburgh in September, 2009 to find ways for: "The financial sector to make a fair and substantial contribution towards paying for any burdens associated with government interventions … to repair the financial system or fund resolutions." (Toronto Declaration Annex II, 21 echoing the Pittsburgh Communiqué, 16)

At Pittsburgh, the G20 asked the IMF to report on a range of options for recovering some of the costs to governments of rescuing their financial systems. A survey conducted by the IMF compiled data on G20 support for rescuing the financial sector, as follows:

Amounts Announced or Pledged for Financial Sector Support by G20[20] (billions of US dollars)

	Advanced Economies	Emerging Economies
Guarantees	3,530	7
Asset swaps & purchases of assets by Treasuries and Central Banks	2,400	0
Upfront government Financing	1,610	24
Direct support pledged (includes capital injections and purchase of assets and lending by Treasuries)	1,976	108
Direct support utilized to date	1,114	43

What is striking about this table is the contrast between the US$9.5 trillion announced or pledged by advanced economies in comparison to the relatively minor backing needed by the financial sector in emerging economies. This should not be seen as an indication that the economic crisis has bypassed the developing world. On the contrary, Oxfam research shows that 56 low-income countries face a US$65 billion revenue shortfall in 2009 and 2010 due to the economic crisis.[21] The United Nations estimates it has pushed between 73 and 103 million more people into extreme poverty.[22]

The IMF does not venture to estimate what the total net cost of all this support will be once loans are repaid and governments recoup some outlays through the sale of acquired assets. It gives only a breakdown of the net costs of the direct support funds that have actually been used to date. Of the US$1,114 billion in direct support utilized so far by the advanced economies, US$237 billion has been recovered. The resulting net direct cost to advanced economies' governments to date is US$877 billion. This cost is likely to increase as the European Union struggles to stabilize its financial sector. In contrast, the net direct costs to emerging economies in the G20 is only US$43 billion.[23]

Prior to the June 2009 Pittsburgh Summit, Germany's Finance Minister, Peer Steinbruck, proposed that the best way to recover this spending would be through a Financial Transactions Tax on all trades of equities, bonds, derivatives and foreign exchange. He estimated that a tax at a rate of 0.05% applied across all G20 members would earn up to US$690 billion a year or about 1.4% of global GDP.[24] While the leaders assembled at Pittsburgh did not endorse an FTT, it was a hot topic of debate over the nine months between the two Summits. (See KAIROS Briefing Paper No. 24 "An Idea Whose Time Has Come: Adopt a Financial Transactions Tax."[25])

Three options: Financial Transaction Taxes, Bank Levies, and Financial Activities Taxes

Two reports prepared by the IMF for the G20 discuss three different, but not necessarily mutually exclusive, options for making the financial sector contribute to paying some of the costs of the crisis. While the IMF concedes that a Financial Transactions Tax "should not be dismissed on the grounds of administrative practicality," it rejects an FTT because it "does not appear well suited to the specific purposes set out in the mandate from G-20 leaders."[26] Instead the IMF recommends that G20 governments consider some combination of a levy on financial institutions' liabilities (which the IMF calls a "Financial Stability Contribution") and a Financial Activities Tax (FAT) on profits and bankers' remuneration. The reports describe in some detail various ways in which levies or FATs might be structured without recommending a specific version of either option.

In the lead up to the Toronto Summit, Prime Minister Harper undertook extraordinary efforts to mobilize opposition to any kind of levy or tax. He dispatched cabinet ministers to Mumbai, Shanghai and Washington to rally non-European G20 members against a tax. Then he travelled personally to London and Paris at the beginning of June to lobby (unsuccessfully) Prime Minister David Cameron and President Nicolas Sarkozy.

In its June 23, 2010, emergency budget, Cameron's coalition government announced a special levy of 0.04% on bank liabilities starting in 2011, rising to 0.07% in 2012. On June 21, just five days before the Summit, President Sarkozy and German Chancellor Angela Merkel wrote Harper to remind him that the European Council had agreed to call for "an international agreement to introduce a levy or tax on financial institutions to ensure fair burden sharing." Moreover, they called for "work on an international agreement on a global financial market tax, e.g., a financial transaction tax."[27]

Despite these initiatives, the Toronto Declaration says very little about bank levies or taxes. It thanks the IMF for its work without citing any of its proposals. It notes that "some countries are pursuing a financial levy." (Annex II, 22) This true of Britain, Germany, France and the United States. The Declaration then notes that "other countries are pursuing different approaches" before citing some vague principles that could apply to almost any kind of action to recoup some funds from financial firms.

This failure to agree can be attributed in part to Prime Minister Harper's efforts. It also reflects successful lobbying by bankers and by a newly constituted business coalition calling itself the "C20," representing the national Chambers of Commerce from all G20 members. Prior to the Summit, the C20 sent the G20 leaders a document explicitly rejecting both an FTT and a bank levy as inappropriate regulatory tools.[28]

However, Harper's short-term achievement has not deterred other initiatives in favour of transaction taxes. At his post-Summit news conference in Toronto, President Sarkozy once again reiterated that transaction taxes to raise money for development and fighting climate change would be on the agenda when he hosts the G20 in 2011. As described in the box on the next page, France continues to play a leading role as an advocate of transaction taxes.

Early in July 2010, the French Minister of the Economy, Christine Lagarde, and the German Finance Minister, Wolfgang Schäuble, sent a joint letter to the presidency of the European Union urging a Europe-wide FTT. The letter confirms that at the Toronto Summit, "France and Germany jointly proposed the creation of a financial transactions tax to achieve a two-fold objective of a fairer burden-sharing and of

'Leading Group' Report Advocates Currency Transaction Tax

Ever since President Jacques Chirac commissioned a report in 2003 on "innovative financing mechanisms" for development, France has been in the forefront of efforts to find additional sources of revenue for development, beyond Official Development Assistance (ODA).

Chirac teamed up with President Lula da Silva of Brazil in 2006 in founding the Leading Group on Innovative Financing for Development, an informal inter-governmental body, currently chaired by Japan, that now has 55 member countries. The Leading Group has successfully implemented an international solidarity levy, applied by 11 countries, on airline tickets that raises millions of dollars each year. This money enables UNITAID to purchase drugs for combating major pandemic diseases such as AIDS, TB and malaria in low-income countries. It has also launched an International Financing Facility for Immunization and the Advanced Market Commitment for pneumococcal vaccines.

On July 16, 2010, 12 countries from the Leading Group, members of a Task Force on International Financial Transactions and Development, released a report on various kinds of bank taxes. The report, compiled by experts in international finance, considered five different options for levies to fund global development and climate change adaptation.

While the Committee of Experts do not recommend a comprehensive FTT as their preferred option, neither do they dismiss it entirely. Instead they say that the proposals currently on the table "need further refinement." They note that the revenues from an FTT would initially be collected at the national level and therefore states would have to negotiate "a multilateral treaty and/or regional instrument" before revenues could be shared for international purposes. Rather than completely dismissing a broad FTT, the Committee of Experts concludes, "At a later stage when implementation issues are overcome, a broad FTT could be a valuable source of finance, especially for domestic purposes. Thus it could ultimately complement options more appropriate to finance global public goods."

The Committee instead recommends a global currency transaction tax that would apply to all foreign exchange trading involving four major currencies (US dollars, euros, yen and pounds). They estimate that trading in these four currencies now amounts to approximately US$3.6 trillion a day. They adopt North-South Institute economist Rodney Schmidt's proposal for a tax at a modest rate of just 0.005%. They estimate that annual revenues from such a Global Solidarity Levy (GSL) would be between US$25 billion and $34 billion a year based on trading volume reduction estimates for 2009.

One of the strengths of the proposal from the Committee of Experts is that the GSL would be collected at the point where currency trades are settled and transferred directly into a Global Solidarity Fund without passing through national treasuries. In this way all the revenues would be available for allocation by the Global Solidarity Fund for use in fighting poverty and climate change. The experts cite the Global Fund for HIV/AIDS, TB and Malaria and UNITAID where representatives from civil society, business, developed and developing countries are all involved in decision-making as examples of global governance structures governed by principles of accountability, democracy, fair representation and transparency.

While a Global Solidarity Levy that would raise some US$25 to 34 billion a year, it would only go part way towards meeting the funding gap of US$324-336 billion for climate change and development assistance. Nevertheless, it would set an important precedent. A successful GSL would also refute those critics who say that transactions taxes are not feasible. In the future, such a precedent could be expanded to a broader FTT on bond, equity, derivative and currency trades that would raise substantially more revenues for spending on global public goods.

The Report of the Committee of Experts to the Task Force on International Financial Transactions and Development. "*Globalizing Solidarity: The Case for Financial Levies.*" Paris: Leading Group on Innovative Financing for Development. 2010. is available. at http://www.leadinggroup.org/IMG/pdf_Financement_innovants_web_def.pdf

raising additional resources. Although consensus could not be reached **yet**, we are convinced that the European Union shall pursue its efforts towards the setting up of such a tax that is both feasible and necessary."[29] (emphasis added)

When reminded that UK Prime Minister Cameron might oppose a Europe-wide tax in order to protect the interest of money traders in the City of London, Schäuble replied that "the 16-member eurozone should consider introducing it if the 27-member European Union failed to agree on the tax."[30]

Revenue needs and revenue potential

According to a study by the Trade Union Advisory Committee to the Organization for Economic Cooperation and Development (OECD), US$168 billion in additional resources are needed annually from 2012 to 2014 to meet the Millennium Development Goals. Another US$156 billion is needed each year to finance climate change adaptation and mitigation in developing countries.[31] With Official Development Assistance budgets frozen or in decline, many civil society groups continue to insist that a global FTT is the best option for raising the needed funds.

The Austrian Institute for Economic Research estimates that a global FTT could yield US$286 billion annually for a tax set at a rate of 0.01% and US$917 billion a year for a 0.1% tax rate. At a mid-range tax rate of 0.05%, an FTT would raise annual revenues of approximately US$650 billion.[32]

A new study from the Institute for Policy Studies in Washington finds that an FTT would raise about US$177 billion a year in the US alone. This is nearly 20 times as much as the US$9 billion that would be raised by President Barack Obama's version of a bank levy, if it is passed by Congress, and six times as much as a Financial Activities Tax.[33]

Absent from the G20 Declaration, and largely ignored in the public debate until now, is the IMF's endorsement of a Financial Activities Tax (FAT) on bank profits and bankers' remuneration as a complement to a bank levy. The IMF claims a FAT would not only raise substantially more revenues than a bank levy alone but also mitigate excessive risk-taking and "like an FTT … tend to reduce the size of the financial sector."[34] Moreover, the IMF points out that the financial sector is in fact under taxed since its services generally are not subject to value-added taxes. A FAT would bring taxation of the financial activities more in line with other sectors of the economy.

The political appeal of taxing bank profits and money traders' high incomes at a time when bank profits are soaring and working people are struggling to find or hold on to jobs should not be underestimated. Goldman Sachs "posted a US$13.4 billion profit in 2009, a Wall Street record. … Goldman proceeded to pay its employees more than $16 billion."[35] Linda McQuaig notes that with "the top 25 hedge fund managers earning a combined $25.3 billion last year, Wall Street's bailed-out financiers are clearly back."[36]

One scenario discussed by the IMF would be for a Financial Activities Tax at a rate of 5% applied to financial institutions' profits, capital formation and wages. Such a FAT would raise about US$93 billion a year if applied across the 22 OECD countries. [37] In Britain the potential revenue from this version of a FAT would amount to £4 billion (US$6 billion) a year or double the £2 billion (US$3 billion) the UK expects to earn from its bank levy. In North America the potential annual revenue from a 5% FAT would be around US$3.4 billion in Canada and about US$44 billion in the US. This is considerably less than the US$261 billion that would be raised each year by an FTT at a rate of 0.05% on all transactions in equities, bonds, derivatives and foreign exchange trades on North American markets.[38]

Part Three: Inaction on Subsidies to Fossil Fuels and Renewable Energy

One measure that could reduce government deficits (or enable spending to be redirected to more environmentally and socially useful endeavours) would be to cut subsidies to fossil fuels. The Toronto summiteers received the "Report to Leaders on the G20 Commitment to Rationalize and Phase Out Inefficient Fossil Fuel Subsidies" as requested at the Pittsburgh Summit. The report was nominally prepared by the International Energy Agency (IEA), the OECD, the World Bank and the Organization of Petroleum Exporting Countries. However OPEC appears to have been at odds with the views of the other three organizations, controlled by the advanced economies.

While the Toronto Declaration acknowledges receipt of the report, it does not set any collective target or mutually agreed timeline for subsidy cuts. The report cites an IEA estimate that global subsidies to consumers of fossil fuels were worth about US$500 billion in 2008. [i] It estimates that if these consumption subsidies were phased out by 2020, global energy-related carbon-dioxide emissions would be reduced by 6.9% as compared to what would happen if subsidies were left untouched. What the report fails to emphasize is that most of these consumer subsidies benefit poor people in low-income countries, although it does say that their removal should be accompanied by policies to protect the poorest.

The report estimates subsidies to fossil fuel producers at US$100 billion a year. It says production subsidies are more difficult to quantify and promises further work to identify their true extent. After citing an estimate by the Global Subsidies Initiative that another "US$100 billion per year is spent to subsidize alternatives to fossil fuels" the report comes to a rather dubious conclusion: "Based on this, OPEC estimates that renewable energy sources and biofuels are subsidized at a much higher rate than fossil fuels."[39] This assertion, clearly attributed to OPEC, is at odds with other estimates of the relationship between subsidies to fossil fuels and to renewable forms of energy. For example, the 2006 Stern review conducted for the British government estimated that subsidies to fossil fuels were 20 times greater than subsidies to renewables.

After Pittsburgh, G20 members were asked to submit national plans for subsidy reductions which were published in an Annex to the report. Six countries, including Saudi Arabia, claim that they have no

[i] OPEC disputes the IEA's methodology for estimating these subsidies.

inefficient fossil fuel subsidies. The United States tabled a promise to eliminate 12 tax provisions that give preferential treatment to the coal, oil and natural gas industries. Canada's submission is particularly disappointing as it offers no new commitments to phase out any of its estimated $2 billion in annual subsidies to oil and gas production. It simply restates pre-existing plans to phase out gradually the accelerated capital cost allowance that provides, on average, subsidies of $300 million a year to tar sands operators.[40]

Before the Summit, Finance Department officials had suggested ways in which Canada could lead by example by announcing plans to phase out some of the tax breaks given each year to fossil fuel companies. But as the Canadian Press reported, "Harper rejected advice from his officials to eliminate tax incentives for the oil patch over a weekend that saw the world's most powerful leaders disdain fresh attempts to combat climate change in favour of fighting deepening deficits."[41]

Although drafts of the Toronto Declaration contained language stating the leaders' resolve to address climate change in part through investments in clean energy, these references were removed from the final text. Kim Carstensen of WWF International sums up the dismay felt by many: "They went through this document with a vacuum cleaner to remove any reference to clean energy. In the Pittsburgh G20 Summit, there were eight references to 'clean energy' – in this one, there is zero. This is demonstrative of the host country's lack of drive and ambition on empowering a shift to renewable energy."[42]

Copenhagen Accord promoted

Instead of taking bold action on the urgent issue of climate change, the Toronto G20 Summit merely endorsed the controversial Copenhagen Accord reached by 26 countries in unofficial closed-door meetings during the 15th Conference of the Parties to the UN Framework Convention on Climate Change (UNFCCC) held last year in the Danish capital. For a thorough critique of the deficiencies and problems associated with the Accord, see KAIROS Briefing Paper No. 23 "Copenhagen Accord or Discord?"[43]

Whereas the G8 Muskoka Declaration gives full support to the Copenhagen Accord, the Toronto Declaration is more reserved. It says: "Those of us who have associated with the Copenhagen Accord reaffirm our support for it and its implementation and call on others to associate with it." (41) This difference reflects the fact that three G20 countries – Argentina, Saudi Arabia and Turkey – have not associated themselves with the initiative which many countries in the global South oppose as a perversion of the UNFCCC process involving all 192 members of the United Nations.

At Pittsburgh, the G20 leaders had asked their Finance Ministers to "report back at their next meeting [scheduled for November 7 in Scotland] with a range of possible options for climate change financing to be provided as a resource to be considered in the UNFCCC negotiations at Copenhagen." (33) But no progress was made at that meeting, leaving the issues unresolved prior to the December Copenhagen conference. In an effort to appease critics from the global South and to entice developing countries into signing on, the Copenhagen Accord made a commitment that developed countries would provide US$30 billion in "new and additional" financing for adaptation and mitigation measures undertaken by developing countries over the years 2010 to 2012. It also promised an additional US$ 100 billion a year by 2020 to address the needs of developing countries.

Unlike other countries, Canada made no financial commitment at the time of the UNFCCC conference. However, in the run up to the Toronto Summit, Minister for the Environment Jim Prentice announced a $400 million annual contribution over three years to the "Copenhagen Green Climate Fund" launched under the auspices of the Copenhagen Accord. This contribution will likely come out of Canada's overall Official Development Assistance budget. Many in civil society fear that this will be at the expense of other urgent needs, especially since Canadian ODA will be frozen at current levels over the next four years.

While the Canadian commitment is in line with Canada's 4% share of other global funds, the total pledged by adherents to the Copenhagen Accord is far from adequate. After the initial three-year period, during which donor countries have pledged to allocate US$10 billion a year, there is no firm plan for how to raise the promised US$100 billion a year by 2020. Moreover this amount is itself inadequate since developing counties need at least US$156 billion a year to finance climate change adaptation and mitigation.

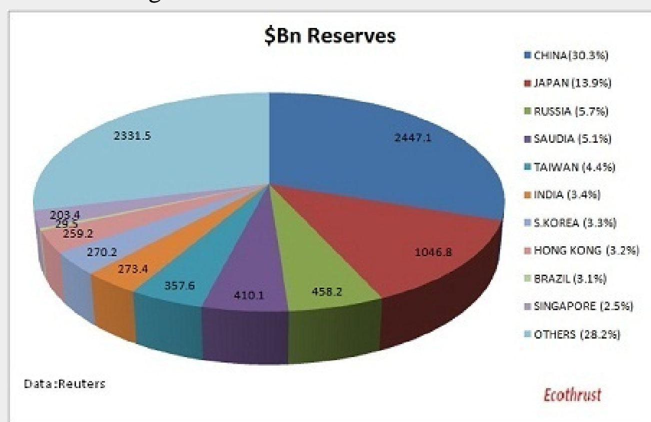
Where will the needed funding come from? The G20 Declaration hints that it left the issue up to the United Nations: "We look forward to the outcome of the UN Secretary General's High-Level Advisory Group on Climate Change Financing which is, *inter alia*, exploring innovative finance." (Toronto Declaration, 41) This group is due to report later in 2010, prior to the November-December UNFCCC conference in Mexico. While the group is looking at a variety of options, one of its sub-groups, chaired by France, is ex-

amining the feasibility of raising revenues through some form of Financial Transactions Tax.

Emerging economies finance advanced economies' debts
The IMF's Ten Commandments for fiscal austerity refer to how advanced economies need "a little help from their emerging market friends" in order to manage their deficits. The IMF wants emerging countries to put less emphasis on promoting exports and pay more attention to expanding their internal markets. The IMF hopes that such a shift would result in bigger markets for advanced economies' exports and thus sustain demand that will otherwise decline due to austerity measures. Hence the IMF welcomes China's decision to allow some increase in the value of its currency as a step towards rebalancing the world economy.

But there is another way in which the emerging economies help the advanced economies to cope with their deficits. That occurs when these countries use their substantial foreign exchange reserves to finance the debts of the advanced economies at very low interest rates. Some advanced economies, particularly the United States, have become very dependent on borrowing from emerging countries to finance government debts.

The chart shows how emerging countries, with the exception of Japan, are the dominant holders of foreign exchange reserves. A central reason why the industrialized countries invited emerging countries into the G20 leaders club in the first place was to persuade them to lend more of their foreign exchange reserves, particularly to the IMF (see KAIROS Briefing Paper No. 16). At their April 2009 Summit in London, the G20 agreed to triple the resources available to the IMF to US$750 billion. At Seoul next November they will consider adding another US$250 billion to the IMF's lending resources.



Part Four: Role of Central Banks Ignored

While the G20 seems mostly concerned with fiscal policies, the potential role that central banks could play in overcoming deficits is ignored. This is doubly strange when one considers how much central banks contributed to bailing out financial institutions. Indeed at the height of the financial crisis, central banks were literally creating money out of nothing to lend to faltering banks.

In technical terms, the central banks engaged in what is known as "quantitative easing," that is measures that increase the money supply when interest rates are near zero and unavailable as a stimulus tool. Central banks can and do at times literally create money from nothing. During 2008, the US Federal Reserve purchased private debt from troubled firms with US$1.2 trillion it created through accounting entries on its books.[44]

This practice is particularly useful when economies are threatened by deflation, that is falling instead of rising prices, the scourge of the Great Depression of the 1930s. Many economists, including Paul Krugman, believe that the US economy is in danger of falling into deflation within the next year. Krugman is highly critical of US Federal Reserve chairman Ben Bernanke for not taking action to prevent deflation by, for example, buying long-term US government debt or private-sector debt.[45]

Quantitative easing could also be used to reduce the cost of servicing Canadian deficits. Since the federal government owns the Bank of Canada, any interest payments it collects revert back to the federal treasury each year net of the Bank's expenses. As long as inflation remains low, the Bank of Canada could safely lend more money to federal or provincial governments for spending on needed goods and services. In fact, for much of the last century the Bank of Canada held a large share of the federal government's debt without causing inflation.[46]

If Bank of Canada purchases of government debt did coincide with rising prices, Michael Bradfield, a Dalhousie University economist, shows how the Bank "could offset any inflationary effect by raising the reserve requirement on deposits held by [private] financial institutions. Higher reserves would have the effect of reducing the money supply by an equivalent amount to what is added when the Bank monetizes government debt."[47] The refusal of central bankers to consider this option is yet another way in which states have ceded power to private banks that themselves create money out of nothing through their lending.[48]

The refusal of governments to consider borrowing from central banks to sustain employment and provide essential services while allowing the same monetary authorities to create money out of nothing to bail out failing banks is yet another indication of a failure to rein in private finance at the expense of peoples' wellbeing.

What is the Future of the G8 and G20?

Although the G8 will meet again next June in France, it is not clear whether it will continue at the leaders level much longer afterwards. In 2012, the G8 would return to the United States and the White House has signalled that President Obama is experiencing "summit fatigue" and wants to cut down on the number of such meetings. Although the official communiqué wrapping up the last "three amigos" summit in Guadalajara in August 2009 said that the North American leaders would meet in Canada in 2010, so far no date has been announced. In the meantime President Calderon has made bilateral visits to both Ottawa and Washington.

One reason why Prime Minister Harper put so much effort into his Muskoka Initiative for maternal and child health was to demonstrate that the G8 is still committed to dealing with development issues. However, the G8's own Accountability Report revealed a shortfall of US$18 billion (in 2005 dollars) on its Gleneagles pledge to increase ODA by US$50 billion by 2010. Similarly, the G8 leaders only advanced two-fifths of the way towards meeting their 2005 Gleneagles promise to deliver universal access to treatment for HIV/AIDS by 2010. At Muskoka the G8 "reaffirmed" their commitment to the goal of universal access but failed to specify a time-frame. Dr. Julio Montaner, president of the International AIDS Society, called this failure "morally and ethically wrong." He added, "There can be no substantial gain in maternal and child health if we fail to deliver universal access to care, treatment and prevention of HIV/AIDS."[49]

While the G8 Declaration says, "We fully anticipate that, over the period 2010-2015 … the Muskoka Initiative will mobilize significantly greater than $10 billion," it adds a caveat – "subject to our respective budgetary processes." (G8 Muskoka Declaration, 11) G8 members themselves only offer a "catalytic … $5 billion of additional funding for disbursement over the next five years" for maternal and child health. The end notes attached to the Declaration say that the US commitment is only for two years and the British government has yet to determine its plans beyond 2011. International aid agencies note that "the G8 countries share of a $30 billion shortfall in international spending promised in 2000 to improve maternal and child health is $24 billion over the next five years, not $5 billion."[50]

Part of the funding gap is to be made up from US$2.3 billion pledged by non-G8 governments and foundations. Australia, the Netherlands, Norway, New Zealand, South Korea, Spain and Switzerland will contribute "subject to their respective budgetary processes." Moreover, the success of the initiative is dependent on additional financial support from six private foundations led by the Bill and Melinda Gates Foundation.

Although the Harper government presented the Muskoka Initiative as "new money" for child and maternal health, "in those countries like the UK honest enough to answer the question clearly, this turned out to mean money not previously labelled as assistance for maternal health. There was no guarantee of a net addition to overall aid budgets."[51] The $220 million pledged by Canada for each of the next five years will initially take up most of the $384 million increase in this year's ODA spending. In the future, it may come at the expense of other aid programs since the Harper government froze future contributions to International Assistance for each of the next four years without even allowing for increments to account for inflation. One quarter of the Harper government's planned expenditure reductions to bring down the deficit over the next four years are to come from shrinking the International Assistance envelope by a total of $4.4 billion.

G20 picking up development issues

While the G8 Declaration refers briefly to convening a group of experts to consider further steps for assisting Haiti, it says nothing about debt relief – a traditional concern of the G7/G8. Instead debt relief for Haiti is announced in the G20 Declaration: "To ensure that Haiti's recovery efforts can focus on its reconstruction action plan, rather than the debt obligations of its past, our Finance Ministers agreed last April to support full cancellation of Haiti's debts to all IFIs, including through burden sharing of the associated costs, where necessary. We are pleased that an agreement on a framework for cancelling such debt has been reached at the IMF, the World Bank, the International Fund for Agriculture Development and soon at the Inter-American Development Bank." (Annex III, 12)

What the G20 fails to acknowledge is that these same institutions are saddling Haiti with new debts. According to Gender Action, 56% of the amounts approved by the World Bank, Inter-American Development Bank and IMF for post-earthquake reconstruction in Haiti are loans, not grants.[52] Moreover, the G20 is silent on whether new lending to Haiti will involve the usual conditions. When IMF directors met on January 27 to approve a new concessional loan to Haiti, the news release said the new loan is not subject to any **additional** policy conditions, implying that existing policy conditions remain in place.

Some commentators believe that shifting concern for development issues from the G8 to the G20 will defuse debates over whether past commitments like those made at the Gleneagles Summit are being fulfilled. Former Canadian Diplomat Jeremy Kinsman, writing in the journal *Policy Options*, questions the assumption that "the G20 will be content to assume accountability for past decisions of the G8. … Obviously, the somewhat resentful leaders of the major emerging countries are looking to decision-making on the real and future major issues, not to a past in which they were not participants."[53]

The South Korean government has promised to make development a major focus at the November Summit in Seoul. Just prior to the Toronto Summit the Koreans released a "Development Issue Paper" which states: "As the premier global economic forum, the G20's development approach flows naturally from its core mandate of international economic cooperation. We therefore believe the G20 should focus on the economic aspects of development, especially the economic growth of low-income countries. After all, economic growth is a necessary (though not sufficient) condition to achieve sustained and self-sufficient poverty reduction and is thus a critical component in closing the development gap." Korean civil society organizations warn that their government's approach to development has a distinctly pro-corporate and neoliberal orientation.

If development issues do indeed become central to the agenda of the G20, there would be one less reason for the G8 to continue meeting at the leaders level although it might continue as a gathering of Foreign Ministers. Certainly the G7 grouping of Finance Ministers (who have always excluded Russia from their gatherings) is likely to continue to meet on the occasions of World Bank and IMF meetings.

The Korean government has pledged to put these issues back on the table as they take over the chair from Canada. A leading Korean newspaper quotes Chin Dong-soo, Chairman of Korea's Financial Services Commission, as saying: "Seoul is hoping to mediate and bring to conclusion the raging global debates on taxing financial institutions around the world to pay for future bailouts by November's G-20 Summit. … We're very cautious expressing our own stance since we're the G-20 chair country responsible for streamlining and coordinating all the other countries' views."[54]

The Koreans have also portrayed themselves as honest brokers, able to mediate between the G7 and the emerging countries without forgetting the needs of the other 173 members of the UN. South Korean officials see themselves as best placed to mediate between the US and China. In the words of one Korean official, "If you tell China to do something directly about its currency, China can do nothing without losing face. We have a good relationship with Chinese economy officials and can engage more on fundamental [issues that impact the] currency, like promoting domestic consumption."[55]

The Koreans are also well situated to bring leadership to bear on the issue of how to make the transition away from dependency on fossil fuels to more climate friendly economic policies. South Korea has led by example, putting more than $30 billion, or 80% of its economic stimulus package, into investments to improve energy efficiency of buildings, expand mass transit and restore forests.[56] In contrast, only 8% of Canada's stimulus package was devoted to green projects and most of that was set aside for dubious carbon capture and storage projects. (See KAIROS Policy Briefing Paper No. 21. "The Costs and Risks of Carbon Capture and Storage."[57])

France has also said that it wants development issues on the agenda when it chairs the G20 in 2011. Between the Koreans' commitment to bring a more civil tone to debates on issues like bank taxes and the French government's ongoing support for innovative financing for development perhaps progress can be made at future Summits on issues like a global financial transaction tax that could not be achieved in Toronto.

For more information, please contact John Dillon, Program Coordinator for Economic Justice, jdillon@kairoscanada.org
KAIROS: Canadian Ecumenical Justice Initiatives unites eleven churches and religious institutions in work for social justice in Canada and around the globe.

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