



INSTITUTE FOR INTERNATIONAL LAW AND JUSTICE
NEW YORK UNIVERSITY SCHOOL OF LAW

International Law and Justice Working Papers

IILJ Working Paper 2008/10
“Financing Development” Project Series

**“FINANCING DEVELOPMENT” AS A FIELD OF
PRACTICE, STUDY AND INNOVATION**

Kevin E. Davis
NYU School of Law

Faculty Director: Benedict Kingsbury

Co-Directors: Philip Alston, Robert Howse and J.H.H. Weiler

Program Director: Angelina Fisher

Faculty Advisory Committee:

Philip Alston, Kevin Davis, David Golove, Robert Howse,
Benedict Kingsbury, Martti Koskenniemi, Mattias Kumm,
Linda Silberman, Richard Stewart, J.H.H. Weiler,
Katrina Wyman

"Financing Development" Project Director:

Kevin Davis

Institute for International Law and Justice

New York University School of Law
40 Washington Square South, VH 314
New York, NY 10012

Website: www.iilj.org

All rights reserved.
No part of this paper may be reproduced in any form
without permission of the author.

ISSN: 1552-6275
© KEVIN E. DAVIS

*Working Papers are issued at the responsibility of their authors, and do not
reflect views of NYU, the IILJ, or associated personnel.*

New York University School of Law
New York, NY 10012
U.S.A.



Cite as:
IILJ Working Paper 2008/10
("Financing Development" Project Series)
Finalized 10/31/2008
(www.iilj.org)

“FINANCING DEVELOPMENT” AS A FIELD OF PRACTICE, STUDY AND INNOVATION[†]

Kevin E. Davis^{*}

Abstract

Access to financial capital is an important determinant of the prospects for development of poor countries. This short essay makes the case for treating the legal aspects of financing development as an important field of study. It begins by describing the kinds of transactions that might be of interest and highlights the role that law and lawyers play in shaping the terms that govern them. The next step is to argue in favor of a holistic approach to the topic. This involves resisting efforts to fragment the field by, for example, drawing sharp distinctions between transactions that involve public as opposed to private parties, or between commercial transactions on the one hand and charity or aid on the other hand. The rest of the essay offers a somewhat speculative discussion of a possible research agenda. The discussion covers both potential research topics - ranging from the governance of international financial organizations to the loan agreements used by microfinance institutions - and methods of approaching them.

[†] *Forthcoming in Acta Juridica*

^{*} Beller Family Professor of Business Law, New York University School of Law. I thank Nikhil Dutta, Matthew Haar and Benedict Kingsbury for helpful comments on an earlier version of this paper and Heather Sims for excellent research assistance. I am also grateful for the support of the Filomen D'Agostino and Max E. Greenberg Research Fund at NYU School of Law.

I. INTRODUCTION

There is ongoing debate about the role foreign capital plays in developing countries as they strive to reduce poverty and promote development. In theory developing countries should almost always be able to put foreign capital to good use. In practice though, much depends on the terms on which the capital is provided. This holds true whether the transaction in question involves a loan from the International Monetary Fund (IMF) or bilateral aid or project financing. In each case the great challenge is to find terms that are sufficiently appealing to induce financiers to part with their funds yet still compatible with the social and economic needs of inhabitants of developing countries. In 2002 fifty world leaders acknowledged these inter-related challenges and, as part of the Monterrey Consensus, endorsed the statement that “[A] holistic approach to the interconnected national, international and systemic challenges of financing for development....in all parts of the globe is essential.”²

Although it may not be immediately obvious, law plays a significant role in defining the terms upon which financial capital flows to developing countries. In short, when it comes to financing development, law matters. Moreover, the conceptual tools that have been developed to study other areas of law can be useful in shedding light on how financing development is or ought to be practiced. Thus, both practical and conceptual considerations weigh in favour of treating the legal aspects of financing development as an important field of study.

The purpose of this essay is to justify and then examine the scholarly implications of treating the legal aspects of financing development as an integrated field of practice, study and innovation.³ The first part describes the field of practice, including some of the transactional forms used in financing development, the importance of the terms that govern those transactions, and the role that law plays in defining those terms. The second part defines the field of study and discusses the role legal concepts can play in studying it. The third part elaborates by setting out four ways of studying and stimulating innovation in the legal aspects of financing development.

II. THE PRACTICE OF FINANCING DEVELOPMENT

(1) *Financing is important*

Transnational financial transfers to developing countries take a number of forms and pass through a number of channels.

Perhaps the most high-profile category of flows is foreign aid, that is to say, financing provided on a non-commercial basis in the form of gifts, grants or debt relief. For example, the United Nations Millennium Project claims that the inhabitants of the rich world can end extreme poverty by providing Official Development Assistance (ODA) that amounts to less than 0.7 percent of their GNP. Even skeptics about the effectiveness

² United Nations *Report of the International Conference on Financing for Development* 18-22 March 2002 Monterrey Mexico A/Conf. 198/11.

³ There are also curricular implications. For an example of a course devoted to financing development see: <http://www.iilj.org/courses/FinancingDevelopmentCourse.asp> accessed 7 August 2008.

of financial aid agree that it has an important role to play in development. For example, William Easterly does not believe that foreign aid or any other type of foreign intervention can end poverty in the developing world, but he still believes that if properly channeled foreign aid can “alleviate the suffering of many desperate people.”⁴

Foreign aid flows through both the public and private sectors. In 2007 disbursements of ODA amounted to \$103.7 billion and U.S. ODA amounted to \$21.8 billion.⁵ By contrast, the recorded portion of remittances flowing from migrants to friends and families in developing countries amounted to \$251 billion and remittances from U.S. residents to the rest of the world were estimated at \$44 billion.⁶ Private donations from rich country NGOs to inhabitants of poor countries probably exceed \$10 billion annually.⁷

Financing provided on more commercial terms, such as loans offered at market rates of interest, is also perceived to play an important role in development. There is, however, ongoing debate over whether that role is positive or negative. For instance, in the sovereign debt context there is a vigorous debate over whether IMF loans have aggravated the problems of the Fund’s developing country borrowers or saved them from an even worse fate. In addition, ever since the debt crisis of the 1980s it has been understood that defaults on developing countries’ sovereign debt can cause ruinous financial crises that threaten the stability of the entire global financial system.

More recently, financial flows to the private sector have captured the attention of development experts. This is in part because for developing countries as a whole capital flows to the private sector eclipse flows to the public sector – a total of \$380 billion of FDI flowed into developing countries in 2006,⁸ dwarfing the amount of ODA. Moreover, there is an increasing sense that transactions that are ostensibly wholly private are actually matters of broader public interest. Consequently, activists and academics devote enormous amounts of energy to publicizing the social, economic and environmental consequences of financing large infrastructure projects.⁹ Similarly, though at the other end of the spectrum of flows to the private sector in terms of scale, some analysts claim that the innovations in microfinance can have far-reaching effects on the fight against poverty.¹⁰

Although the scholarly literature often attempts to isolate and focus on individual methods of financing development, it is often rather difficult, and even unhelpful, to draw

⁴ *The White Man’s Burden: Why The West’s Efforts to Aid the Rest Have Done So Much Ill and So Little Good* (2006) 383.

⁵ Both these figures include substantial amounts of aid directed to Iraq and Afghanistan. For instance, in 2007 the US devoted almost \$5.3 billion worth of aid to those two countries. Organization for Economic Cooperation and Development *Debt Relief is Down, Other ODA Rises Slightly* 4 April 2008 http://www.oecd.org/document/8/0,3343,en_2649_33721_40381960_1_1_1_1,00.html accessed 1 August 2008.

⁶ World Bank *Remittance Data* July 2008 <http://econ.worldbank.org/WBSITE/EXTERNAL/EXTDEC/EXTDECPROSPECTS/0,,contentMDK:21122856~pagePK:64165401~piPK:64165026~theSitePK:476883,00.html> accessed 1 August 2008.

⁷ D Roodman & S Standley *Tax Policies to Promote Private Charitable Giving in DAC Countries* (2006) Center for Global Development Working Paper No. 82.

⁸ *World Investment Report 2007: Transnational Corporations, Extractive Industries, & Development* UNCTAD (2007) at 251.

⁹ M Likosky *Law, Infrastructure, and Human Rights* (2006).

¹⁰ M Robinson *The Microfinance Revolution: Sustainable Finance for the Poor* (2001).

sharp distinctions of this kind. For instance, the distinction between commercial and non-commercial transactions becomes a fine one when one considers not only simple loans and grants but also interest-free loans, loans provided at below-market interest rates, loans that will predictably be forgiven in the event of a crisis, or loans that are ostensibly at market rates but are guaranteed or insured by public agencies. Similarly, it is difficult to draw a sharp distinction between public and private transactions when private actors finance public actors, as in the sovereign debt context; public actors such as the International Finance Corporation finance wholly private actors; certain actors obtain financing from both the public and the private sector; public and private entities combine to provide financing, as in the case where tax credits are given for donations to foreign charities; or financing is provided to hybrid entities such as public-private partnerships. It is also unhelpful to draw sharp distinctions between different categories of transactions to the extent that they are substitutes for one another. For instance, for any given amount of financing at commercial interest rates there should be an equivalent – albeit much smaller – grant. Perhaps more obviously, financing from public actors can often serve as a substitute for financing provided by private actors.

A fairly holistic approach to financing development is already reflected to some extent in the ways that financing development is practiced. For example, the World Bank Group uses many different sorts of financial instruments in pursuit of its mandate to finance development, ranging from market-rate loans to private sector actors to grants to governments, and gives a great deal of thought to the interaction between the various forms of financing.¹¹ It is natural to presume that recipients in developing countries are aware of the possible tradeoffs and complementarities between alternative forms of financing. Practitioners have also seized opportunities to transfer ideas initially associated with one form of financing development and apply them in other contexts. Several recent innovations in financing development involve the transplantation of terms developed for use in private sector commercial transactions to other contexts. For example, the Millennium Challenge Corporation's Compacts (grant agreements) incorporate representations and warranties that resemble those used in corporate bond offerings. The International Finance Facility allows an international NGO to raise financing for vaccines and immunization backed by donors' pledges using the same basic structure as securitizations employed by corporate actors.¹² Meanwhile, other ideas about financing development have moved from the non-profit sector to the private commercial sector. For example, innovative forms of microfinance that more or less originated in the nonprofit sector are rapidly being adopted by profit-oriented financial institutions.¹³

¹¹ World Bank *About Us – Operations* (2008) <http://go.worldbank.org/1YXPMBNDO0> accessed 1 August 2008.

¹² HM Treasury *The International Finance Facility* (2005) http://www.hm-treasury.gov.uk/media/F/B/IFF_proposal_doc_080404.pdf accessed 1 August 2008.

¹³ See, for example, the development of a commercial model by the institutional network Acción International, and the subsequent transformation of Bolivia's BancoSol from a non-profit to the first private commercial bank dedicated exclusively to microfinance. C Bruck 'Millions for Millions' (2006) 82 *The New Yorker* 62.

(2) *Terms Matter*

Occasionally one still sees analysts trying to answer questions such as “Is aid effective?” or “Does FDI stimulate growth?” However, more sophisticated treatments of these sorts of topics recognize that these categories of transactions are far too crude and that more fine-grained analysis is required to shed light on the consequences of international financial flows.

Not all capital flows to developing countries are created equal. Rather, a whole host of questions need to be asked to determine the overall impact of a particular financial transaction. For example, does the transaction (especially while it is still just a pledge) represent a binding commitment on the part of the financier? Is the recipient required to purchase goods or services from the donor’s country? Is the recipient required to purchase goods or services from local suppliers? Is the recipient required to comply with international labor or environmental standards? Is the recipient a public or a private actor? If the recipient is a public actor will the inhabitants of the recipient country be liable even if they did not benefit from the transaction? If the recipient is a private actor is it a for-profit or a non-profit entity? Under what circumstances will the recipient’s obligations be excused or modified? Et cetera.

The general point here is that the terms upon which financing for development is provided are typically of crucial importance in determining its impact. One reason is because the terms define the balance that has been struck between the potentially conflicting interests of the various actors implicated in the transaction, namely, financiers, intermediaries, ultimate recipients of funds, and other residents of developing countries. For instance, financiers’ interests may lie in being repaid with interest or in increasing exports, both tangible and intangible. At the same time intermediaries’ interests may lie in maximizing the volume of funds passing through their hands, whether to help justify their existence or to make it easier to skim a little bit off the top for themselves. Meanwhile residents may be interested in satisfying short-term consumption needs as opposed to ensuring long-term benefits for their communities. The terms upon which parties enter into a transaction can also matter because they send important signals to other actors about the parties to the transaction.¹⁴ For example, actors may go out of their way to adopt innovative terms in an effort to signal to the world that they are competent, aggressive and innovative along a number of dimensions.¹⁵

(3) *Law matters*

This of course leads to the question: How are the terms of development finance defined? The answer is that they are defined in much the same way as the terms of any other financial transaction: by some combination of the agreement of the parties to the transaction and applicable legal and non-legal norms that determine the meaning, in both symbolic and practical terms, of the agreement. Where multiple financiers or intermediaries are involved the terms may be contained in a series of agreements and norms emanating from several different sources may come into play. Moreover, the

¹⁴ M Suchman ‘The Contract as Social Artifact’ (2003) 37 *Law and Society Review* 91.

¹⁵ A Gelpert & G Gulati ‘Public Symbol in Private Contract: A Case Study’ (2007) 84 *Washington University Law Quarterly* 1627.

terms upon which some of the actors participate, and particularly organizational actors such as governments, financial institutions or charities, will be influenced by various sets of norms that determine their mandates and powers. Therefore, financing development can be analyzed as a contractual process in which the terms are set by agreements among a subset of the relevant actors as well as various forms of regulation that shape the content of, interpret, override or supplement those agreements and determine how they are enforced.

This perspective on financing development emphasizes the potential role of contracts and regulation in fixing its terms and determining its ultimate impact. In short, it highlights the role of law. This is not to imply, however, that other factors are irrelevant. In fact, a whole array of additional factors may come into play. To begin with, factors that can loosely be described as cultural norms might influence how the members of any given society behave in response to a given type of contract. For example, prevailing attitudes toward repayment of debts and the strength of social ties have proven to be important determinants of the effectiveness of microfinance techniques such as group lending.¹⁶ Geography and communications technology can also be relevant. For example, Globalgiving.com now permits individual donors worldwide to make small grants in support of specific projects in the developing world, a type of transaction that was highly impractical before the advent of the Internet. Focusing on the role of law should not mean ignoring these factors.

III. THE POTENTIAL FIELD OF STUDY

The challenge for scholars is to understand the terms upon which financing development occurs, in order both to explain and to inform practice.

(1) *The Scope of the Field*

The importance of studying specific methods of financing development is already widely accepted, particularly when it comes to techniques such as sovereign debt, foreign aid, infrastructure finance, and microfinance. The importance of developing a detailed understanding of the terms employed in those financing instruments is also becoming increasingly well recognized. In fact, astonishing amounts of effort have been devoted in recent years to analyzing topics as arcane as the role of collective action clauses in sovereign debt agreements,¹⁷ conditionality in foreign aid,¹⁸ environmental standards in project finance loans,¹⁹ and group liability in micro-lending.²⁰

¹⁶ J Lashley 'Microfinance and Poverty Alleviation in the Caribbean: A New Strategic Overview' (2004) 6 *Journal of Microfinance* 83; A Cassar, L Crowley, B Wydick 'The Effect of Social Capital on Group Loan Repayment: Evidence from Field Experiments' (2007) 117 *The Economic Journal* F85; D Karlan 'Social Connection and Group Banking' (2007) 117 *The Economic Journal* F52.

¹⁷ See S Choi & G Gulati 'Innovation in Boilerplate Contracts: An Empirical Examination of Sovereign Bonds' (2004) 53 *Emory L.J.* 929; F Weinschelbaum & J Wynne 'Negotiation, Collective Action Clauses and Sovereign Debt Markets' (2005) 67 *Journal of International Economics* 47; T Becker, A Richards, & Y Thaicharoen 'Are Collective Action Clauses Costly?' (2003) 61 *Journal of International Economics* 127.

¹⁸ J Svensson 'Why Conditional Aid Does Not Work and What Can Be Done About It?' (2003) 70 *Journal of Development Economics* 381 (arguing that most conditional aid arrangements lack any credible threat of

Though appropriate at times, this sort of piecemeal approach to the study of financing development is incompatible with key features of the phenomenon. For one thing, as we have already seen, in practice these types of transactions are difficult to distinguish from one another. Furthermore, there are also fundamental conceptual linkages. Specifically, the various methods of financing development are driven by similar economic or political factors, serve as complements or substitutes for one another and can be governed by related institutions. All of this suggests that what might at first glance appear to be distinct methods of financing development ought to be analyzed using similar conceptual tools. So for instance, the terms upon which developing country sovereigns borrow from the IMF should not be analyzed without taking into account the terms upon which they or their inhabitants receive foreign aid or the proceeds of project finance. Similarly, initiatives such as those designed to reconstruct the international financial architecture, to reinvent foreign aid, and to introduce the financiers of infrastructure projects to the concept of corporate social responsibility should not be formulated or implemented in isolation from one another. In other words, if the challenge set out by the Monterrey Consensus is to be taken seriously, financing development must be treated as an integrated field of study.

(2) *Conceptual tools*

The next topic to consider is, what sorts of conceptual tools should be brought to this field of study? The tools traditionally deployed social scientists such as economists and political scientists have a great deal to offer. But as we shall see, there is also room for some of the conceptual tools that are likely to be more familiar to lawyers.

Principal and agents

Economists often use some sort of principal-agent model to analyze the effects of adopting alternative financing terms.²¹ The standard approach in the literature is to define any actor providing financing – whether the original financier or an intermediary – as the principal and any recipient of the funds – again, whether they be an intermediary or the ultimate recipient of the funds – as the agent. This framework is thought to provide a

non-disbursement and are therefore ineffective); W Easterly ‘What Did Structural Adjustments Adjust? The Association of Policies and Growth With Repeated IMF and World Bank Adjustment Loans’ (2005) 76 *Journal of Development Economics* 1 (finding no positive effect of repeated adjustment lending on policies or growth).

¹⁹ D Hunter ‘Civil Society Networks and the Development of Environmental Standards at International Financial Institutions’ (2008) 8 *Chicago Journal of International Law* 437; B Scholtens & L Dam ‘Banking On The Equator: Are Banks That Adopted The Equator Principles Different From Non-Adopters?’ (2007) 35 *World Development* 1307; W Thomas & R Lawrence ‘Equator Principles and Project Finance: Sustainability in Practice?’ (2004) 19 *Natural Resources & Environment* 20.

²⁰ X Gineé & D Karlan ‘Group Versus Individual Liability: A Field Experiment in the Philippines’ (2006) World Bank Policy Research Working Paper 4008; M Ghatak & T Guinnane ‘The Economics of Lending With Joint Liability: Theory and Practice’ (1999) 60 *Journal of Development Economics* 195; B Armendariz de Aghion & C Gollier ‘Peer Group Formation in an Adverse Selection Model’ (2000) 110 *The Economics Journal* 632.

²¹ See, for example, F Bourguignon and M Sundberg ‘Aid Effectiveness: Opening the Black Box’ (2007) 97 *American Economics Review* 316.

useful way of analyzing financial transactions (as well as other economic transactions) because it is designed specifically to highlight the potential conflicts of interest between the various parties to a transaction and the ways in which the terms of the transaction can be structured to address those conflicts.

There are, however, fundamental problems with employing the principal-agent model as the main conceptual tool for analyzing financing development. First, implicit in the terms “principal” and “agent” is the notion that the interests of the actor labeled the principal are to be privileged over those of the actor cast in the role of agent. The problem to be solved in the principal-agent model is how to align the agent’s interests with those of the principal, not the reverse. In the development context, though, it is not so clear that the interests of financiers deserve to be privileged over those of recipients. In the eyes of some members of the development community, the source of many of the problems of the developing world has been the tendency throughout history to privilege the interests of Western financiers over the interests of inhabitants of developing countries. From this perspective the real problem to be solved when setting the terms for financing development is to re-align the interests of the financiers, not the recipients.

A second difficulty with the principal-agent model is that it tends to be associated with economic analysis and, more specifically, with economists’ presumption that actors’ basic interests (preferences) are fixed and can only be re-aligned by catering to those interests through systems of sanctions and rewards. The possibility of changing interests or preferences is typically ignored.²² Many people find this approach unduly restrictive.

The conceptual baggage associated with the principal-agent model weighs in favor of adopting an alternative framework for analyzing financing development, specifically, one that is associated with less contentious assumptions about the nature and relative importance of the parties’ interests.

Governance

Another way of characterizing financing development and the terms upon which it is conducted is as an aspect of (global) governance.²³ This perspective highlights the roles that various local and international organizations play in setting the terms upon which financing development occurs. For practical reasons, using a governance lens tends to draw attention to connections between the governance of financing transactions simpliciter and ongoing governance of the organizations or projects being financed, particularly in cases where long-term funding is being provided to large complex entities such as those that manage large infrastructure projects or the governments of sovereign nations. Moreover, many organizations that finance development – consider, for example, the IMF or a large project finance bank – have other responsibilities besides providing development finance. As a result, the governance framework seems likely to emphasize connections between the governance of financing development and

²² G Stigler & G Becker ‘De Gustibus Non Est Disputandum’ (1977) 67 *American Economic Review* 76.

²³ RJ Orr & B Metzger (2005) *The Legacy of Global Projects: A Review and Reconceptualization of the Legal Paradigm*. Proceedings of the 1st General Counsels’ Roundtable. Stanford, CA, 21 - 22 January, 2005, pp.1 – 51. Stanford: CRGP. Available at: <http://crgp.stanford.edu/news/gcr.html> accessed August 6, 2008.

governance of activity that does not necessarily have anything to do with either finance or development.

In more conceptual terms, using a governance framework allows us to bring tools developed to study other forms of governance to bear on financing development. For example, it might be useful to draw on the general literature on international relations to examine the role that state power plays in shaping the terms upon which both public and private actors participate in financing development.²⁴ Meanwhile, referring to the more specific literature on the provision of global public goods might help to identify strategic obstacles to international cooperation in financing development and ways of overcoming them.²⁵

The governance framework also puts a spotlight on the legal mechanisms that are used to implement governance. This in turn points toward the conceptual tools that have evolved to analyze the distinctively legal aspects of global governance. To cite the most notable recent example, the literature on global administrative law emphasizes the role that principles of administrative law, such as transparency, participation, and basic procedural fairness, play in global governance.²⁶ Understanding the extent to which these principles apply not only to public institutions such as the World Bank but also, perhaps, to private institutions such as project finance banks is an important part of the challenge of determining how to finance development.

Viewing financing development exclusively as a form of governance provides only limited insight though. The main reason for this is that the governance approach tends to obscure the significance of decentralized uncoordinated interactions between private actors who define the terms that will govern their interaction for themselves. The governance framework is arguably prone to view these situations as being characterized by the absence of governance and thereby overlook interesting features such as variations in the terms formulated by private actors. These sorts of terms are exactly the ones that are focus of analysis in the contractual framework discussed in the next section.

Contracts

Many forms of financing can be plausibly characterized, both legally and figuratively, as contracts. Using a contractual framework to analyze financing development has many virtues, including all of the virtues associated with the principal-agent model. Contracts are recognized as one way of aligning the interests of principals and agents and so principal-agent models are routinely used to analyze the consequences of adopting various types of contractual terms. Unlike the principal-agent model though, the contractual framework is not necessarily associated with the view that financiers' interests are paramount in any sense or that parties' interests are immutable.

²⁴ *The Globalizers: The IMF, the World Bank and Their Borrowers* N Woods (2006).

²⁵ I Kaul, I Grunberg, M Stern (eds) *Global Public Goods: International Cooperation in the 21st Century* (1999); I Kaul et al (eds) *Providing Global Public Goods: Managing Globalization* (2003).

²⁶ B Kingsbury et al (eds) 'The Emergence of Global Administrative Law' (2005) 68 *Law and Contemporary Problems* 1; B Kingsbury & N Krisch (eds) 'Symposium: Global Governance and Global Administrative Law in the International Legal Order' (2006) 17 *European Journal of International Law* 1.

Characterizing financing development as a contractual process also opens the door to transferring other conceptual tools (besides principal-agent models) from the study of contracts. For instance, looking at this phenomenon through a contractual lens naturally leads to exploring the roles that contract law and related legal doctrines play in financing development. Examples of the panoply of legal issues that might be explored include: the circumstances in which donors' pledges are legally enforceable; the role of standard contract law doctrines such as public policy or breach of authority in determining the enforceability of financing agreements; whether doctrines protecting third party beneficiaries extend to members of developing societies affected by infrastructure financing; whether financing agreements providing for resolution of disputes before foreign courts or arbitral tribunals are enforceable; whether in cases of silence or ambiguity special interpretive doctrines designed to protect or promote the interests of weaker parties apply to financing agreements; and, whether there are any restrictions upon financiers' ability to enforce their claims against the recipients' assets.²⁷

Concepts from the scholarly literature on contracting may also prove useful in the study of financing development. For example, the concept of a relational contract may be a good characterization of some complex financial transactions and so the ideas developed in the literature on relational contracting may be relevant to financing development.²⁸ Similarly, recent literature on the symbolic dimensions of contracting²⁹ or the recent flurry of writing on boilerplate contractual terms³⁰ may also provide insights that can help to understand the phenomenon of financing development.

Despite its many virtues, the contractual framework also has limitations as a method of understanding financing development. The root of the problem is the fact that characterizing a phenomenon as a contract automatically focuses attention on agreements between the parties to the exclusion of other aspects of the phenomenon. This means that events that precede or follow the life of any agreement and actors who are not parties to any agreement become peripheral rather than central to the field of study. So, for example, factors such as the regulation of financial institutions and the broader social consequences of large-scale financings may be difficult to analyze successfully using a purely contractual framework.

Hybrid frameworks

This last point suggests the value of using more than one conceptual framework, or even hybrid frameworks, to analyze financing development. The strengths of one model will often compensate for the limitations of another. So, for example, concepts from the

²⁷ Many of these issues are addressed in the recent literature on the doctrine of odious debt. See, for example, L Buchheit, M Gulati & R Thompson, 'The Dilemma of Odious Debts' (2007) 56 *Duke Law Journal* 1201.

²⁸ See, for example, I Macneil, 'Contracts: Adjustment of Long-Term Economic Relations under Classical, Neoclassical, and Relational Contract Law' (1978) 72 *Northwestern University Law Review* 854; CJ Goetz & RE Scott, 'Principles of Relational Contracts' (1981) 67 *Virginia Law Review* 1089; RE Scott, 'A Relational Theory of Secured Financing' (1986) 86 *Columbia Law Review* 901.

²⁹ M Suchman 'The Contract as Social Artifact' (2003) 37 *Law & Society Review* 91; A Gelpert & G Gulati 'Public Symbol in Private Contract: A Case Study' (2007) 84 *Washington University Law Quarterly* 1627.

³⁰ O Ben-Shahar (ed) *Boilerplate: The Foundation of Market Contracts* (2007).

literature on the provision of global public goods might usefully be combined with concepts from the literature on boilerplate contractual terms to analyze the process of creating innovative terms in the context of international finance.

IV. SPECIFIC DIRECTIONS FOR RESEARCH

There are at least four distinct purposes that might be served by studying financing development. One purpose might be to describe a particular practice or set of practices. A second purpose might be to analyze the consequences of adopting such practices. A third purpose might be to determine what causes the emergence of one practice as opposed to another. Finally, a fourth purpose might be to generate a normative assessment of a particular practice, in other words, to say whether it ought to be praised or condemned, or encouraged or discouraged. Although these scholarly purposes are conceptually distinct they are invariably tightly connected in practice because accurate description is a useful precursor to further analysis of any sort, and analysis of causes and consequences is a pre-requisite to many kinds of normative analysis.

As we shall see, regardless of the purpose of studying financing development, it is likely to be helpful to pay attention to the legal dimensions of the practice.

(1) Description

The terms upon which financing development occurs are often to be found in documents that never see the light of day. Or, if the documents are released, the important terms are buried in the fine print.

There will often – though not always – be value in simply describing the contents of those documents, if only for the purpose of making new ideas available to practitioners.³¹ Consider for example, the potential impact of showing practitioners around the world how to provide insurance against bad weather to small farmers, or how to use securitization to reduce the costs of capital for microfinance institutions. Simply creating a publicly accessible clearinghouse for documents used in financing development and applicable regulations goes a long way toward serving these purposes. More sophisticated approaches though can involve comparisons, across either time or space, between various documents. This sort of descriptive work is not only a spur to innovation but an indispensable pre-requisite to scholarly work on the causes and consequences of adopting any particular set of terms. Consider, for example, how useful it would be to know how many commercial banks both incorporate and enforce environmental standards in their project finance agreements before analyzing either the popularity or merits of the Equator Principles.

In one sense it will be difficult to avoid the legal aspects of financing development when describing its terms. Many of the terms are embodied in documents such as contracts, treaties, statutes or regulations that are intended to be legally binding. But the legal dimension of these documents is also important in another sense. Most lawyers

³¹ Disseminating information about novel terms does run the risk of discouraging innovation. As suggested below, whether and to what extent dissemination generates costs and benefits are also topics worth studying.

would insist upon recording not only variations in the operative terms of these sorts of documents, but also variations in their legal effects. So for example, they would make a distinction between an environmental covenant contained in a binding loan agreement and an identically worded covenant contained in a document styled as a ‘code of conduct.’ Collecting legal data of this sort sets the stage for thinking about why the law of development finance varies from place to place or time to time, and what difference it makes when it does.

(2) Causes

Economic, political and sociological factors undoubtedly play a role in understanding why particular methods of financing development emerge in particular times or places. However, inherently legal factors are also likely to play a role.

For instance, the literature on global administrative law is concerned in part with exploring legal mechanisms for holding organizations with transnational operations accountable to various stakeholders. It seems natural to extend this framework of analysis to organizations that provide development finance.³² An entire research program is beginning to emerge around the question of how various forms of legal accountability shape the terms on which capital is provided to developing countries by organizations such as bilateral aid agencies, project finance banks and multilateral development banks.³³ This research complements ongoing research being done on the relationship between the political accountability of organizations such as the IMF and the World Bank and the terms upon which they lend to developing countries.³⁴ Examples of the questions that fall within the scope of these closely related research programs include: What difference does it make if organizations that provide development finance are accountable to local courts, local regulatory agencies, international arbitral tribunals, new or existing international institutions, or only to internal ombudspersons? Does it matter which remedies are provided and to whom? Is it relevant to what extent any given regime can be evaded by relying on shell companies incorporated in foreign jurisdictions or choice of law clauses?

Meanwhile, ideas drawn from the literature on contract law might shed light on why the terms of individual transactions vary even when broad features of the regimes that govern development finance organizations are held constant. For instance, legal scholars have devoted a great of attention to the question of how rules that govern contractual relationships by ‘default’ – meaning that they can still be ousted by the agreement of the parties – influence the terms of the contracts that are ultimately signed.³⁵ Literature on the non-legal factors that influence the popularity of specific terms, in other words, on the

³² P Dann ‘Accountability in Development Aid Law: The World Bank, UNDP and Emerging Structures of Transnational Oversight’ (2006) 44 *Archiv für Völkerrecht* 381.

³³ Dann, id; M Likosky *Law, Infrastructure, and Human Rights* (2006); B Richardson *Socially Responsible Investment Law: Regulating the Unseen Polluters* (2008).

³⁴ N Woods *The Globalizers: The IMF, the World Bank and Their Borrowers* (2006).

³⁵ For a critical review of some of this literature see A Schwartz ‘The Default Rule Paradigm and the Limits of Contract Law’ (1994) 3 *Southern California Interdisciplinary Law Journal* 389.

diffusion of boilerplate, also seems relevant.³⁶ Taken together these bodies of literature suggest a wide range of factors that might influence the terms upon which financing development occurs. Examples of some of the directions for further research include: Do interpretive presumptions biased in favour of recipients of financing compensate for inequalities in bargaining power or are they counter-productive? How do intellectual property laws influence the costs of unauthorized copying of innovative contracts and, over time, incentives to invest in innovation? What role do NGOs play in producing socially conscious model contracts that might eventually become boilerplate? What role do individual lawyers and their training, values and predilections play in shaping the terms of transactions concluded by their clients?

(3) Consequences

A central feature of any research agenda on financing development should be analysis of the consequences of adopting specific terms. The consequences examined might be limited to the purely economic interests of the parties to the relevant agreements. But attention can also be paid to effects on the economic interests of actors who are not parties to any agreement and effects along non-economic dimensions. Typically it will make sense to compare the consequences of deploying alternative methods of financing. So for instance, analysis of project financing as a method of financing infrastructure might involve comparing the economic benefits to the parties of obtaining political risk insurance from the Multilateral Investment Guarantee Agency as opposed to a private insurer, or of obtaining principal financing from a bank as opposed to the capital markets, or adopting one set of financial covenants or another. A broader analysis would take into account the effects on the community in which the project is located, including not only economic effects but also environmental impacts and the effects on institutional capacity of channeling financing through local governmental actors as opposed to the private sector or a public-private partnership. A more elaborate analysis would try to trace causal links not only forward in time between particular transactional terms and their consequences but also backwards to the kinds of causal factors discussed in the preceding section, such as the involvement of NGOs or the potential involvement of local courts.

In some respects, implementing this research agenda should be straightforward for scholars with appropriate training. Focusing on just the legal aspects of development finance, on the theoretical side scholars can draw upon rich bodies of literature in law, economics, political science and management on how various sorts of accountability mechanisms affect organizational performance. There is also at least as much literature on how specific contractual terms – think of techniques such as representations or warranties, options or most-favoured-nation clauses – can be used to enhance the welfare of parties to financial transactions by mitigating problems such as asymmetric information, uncertainty about the future, and parties' inability to make credible commitments. Finally, there is a rapidly growing body of knowledge on how to conduct empirical work that traces causal relationships between legal phenomena on the one hand and social and economic outcomes on the other hand.

³⁶ See generally, M Kahan & M Klausner, 'Standardization and Innovation in Corporate Contracting (or "The Economics of Boilerplate")' (1997) 83 *Virginia Law Review* 713; KE Davis, 'The Role of Non-Profits in the Production of Boilerplate,' (2006) 104 *Michigan Law Review* 1075.

The greatest challenge in conducting this kind of research probably does not lie in answering questions about the consequences of adopting specific methods of financing, but rather in deciding what sorts of questions to ask. This is true in part because studying the effects of existing financing techniques is one thing, but deciding which techniques to study is quite a different matter, especially when they haven't been invented yet. The task is particularly difficult if one believes, as many reputable scholars do, that the effects of adopting legal institutions tend to be highly context-specific.³⁷ This perspective implies that the most valuable research on legal aspects of financing development will tend to be the kind that explores the consequences of innovation, whether that means creating entirely new institutions or adapting existing institutions to fit new circumstances. Typically this kind of work has to be done without being able to rely on the lessons of past experience. It is not at all clear that this kind of intellectual work is best conducted by scholars as opposed to practitioners. In fact, it might be most fruitful for scholars to focus their attention on the processes by which the law of financing development adapts and innovates rather than on specific outcomes of that process.

There is a second reason why it is difficult to formulate research questions in this area. Whether we are discussing the adoption of existing or innovative financing techniques there is always the question of which effects are worth examining. In other words, which consequences are worth caring about? For instance, should research on development aid focus on outcomes prioritized by donors or recipients? Or, in transactions that involve governmental actors, should the focus be on outcomes that matter to the government or the people they are supposed to represent? In order to be of general interest, research on the consequences of financing development will have to be related to reasonably compelling theories of what sorts of outcomes are desirable or undesirable. In other words, it should enlighten us on the relationship between finance and a form of social change that counts as development. However, there are so many competing conceptions of what counts as development and how to go about achieving it that this common-sense principle will often do little to limit the number of outcomes that qualify for consideration. This implies that scholars who seek to maximize the appeal of their work ought to assess the impacts of specific methods of financing development, or at least ways of generating those financing methods, on as broad a range as possible of social and economic outcomes.

(4) *Normative claims*

At its best, research on financing development can help lawmakers and practitioners answer questions such as: Should rich countries be encouraged to increase ODA or focus instead on boosting private donations to foreign charities? If rich country governments want to borrow against pledges of future aid in order to provide immediate funding for development projects should they borrow themselves or use an intermediary such as a development bank or the International Finance Facility? Should commercial banks be held liable when projects they finance violate environmental standards of the banks' own jurisdiction? What benchmarks should be pre-requisites to sovereign debt relief? Should

³⁷ D Rodrik *One Economics, Many Recipes: Globalization, Institutions, and Economic Growth* (2007); C Sabel 'Bootstrapping Development: Rethinking the Role of Public Intervention in Promoting Growth' in V Lee & R Swedberg (eds) *On Capitalism* (2007) 305.

non-profit micro-lenders be subject to the same forms of prudential regulation as for-profit institutions? Should financiers be encouraged to use instruments such as credit derivatives to re-allocate risks associated with financing development without fear of undermining their incentives to lend prudently? In this sense, research on financing development is likely to help define the terms upon which capital is transferred to developing countries for years to come.

As promising as they seem, however, there is no guarantee that any of these research prospects will pan out. If the course of research on other aspects of the relationship between law and development is any guide, it may prove difficult for either theoretical or empirical analysis to generate definitive and feasible prescriptions for action.³⁸ We have already discussed the ways in which lack of consensus about the outcomes desired or inability to generalize from past experience might limit the value of any given piece of research. There is also the possibility that economic or political factors may have much more influence on practice than so-called legal factors. We should be prepared for the possibility that, when all is said and done, law does not matter so much after all.

V. CONCLUSION

There is ample justification for not only treating financing development as an important and integrated field of practice, study and innovation, but also for examining the legal dimensions of the practice using conceptual tools that have been developed to study other legal phenomena. The importance of financial capital to developing countries is contingent on the terms upon which the capital is provided and those terms appear to be shaped in meaningful ways by law. The law of financing development is not co-extensive with the law of contracts or the law of global governance or any other recognized body of law, but there are significant overlaps. Those overlaps are what make the legal aspects of financing development seem like a worthwhile field to explore. It is unclear what will come of this program of research, but for the time being the outlook is promising.

³⁸ K Davis & M Trebilcock 'Optimists versus Skeptics: The Relationship between Law and Development' (2008) 56 *American Journal of Comparative Law* 895.