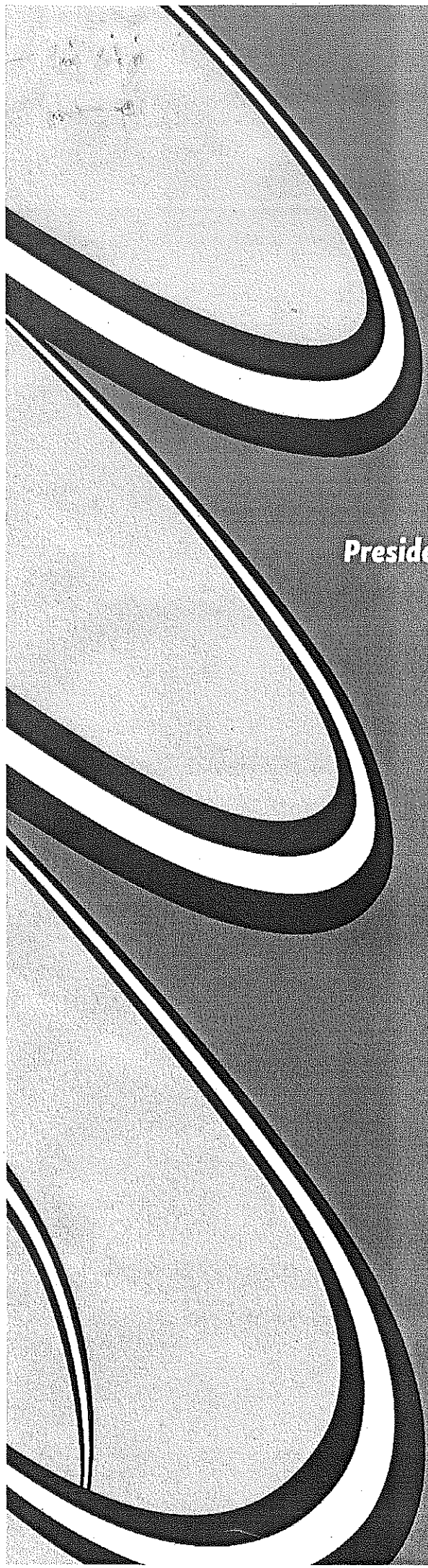

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Governance of the aid system and the role of the EU

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Contents

0. Introduction

This paper is about governance of the aid system, with specific reference to the European Union. The EU makes a good case study, because all the global questions about governance of international aid also apply at the level of the EU. Is this a coherent and planned system, or more random and chaotic in nature? Is it capable of being governed and planned? Should it be governed and planned in its entirety? And assuming governance or architectural interventions are possible, should the aim be consolidation into fewer entities or cooperation among many?

Within the world of official aid, two views currently dominate the debate. The first celebrates diversity and concentrates on the coordination of collaborative networks. It focuses attention on shared goals, harmonisation of approaches, and better coordination of who does what. It finds its highest expression in the UN's work on the Millennium Development Goals (MDGs), and in the aid effectiveness initiatives of the Development Assistance Committee of the OECD. In the European Union, the key instruments are the European Consensus on Development of 2005[1] and the Code of Conduct on Division of Labour,[2] agreed in 2007.

The second view seeks reform of the aid 'architecture' in order to reduce the number of actors and rationalise the supply of aid. It focuses on the allocation of aid between institutions, transactions costs, multilateral effectiveness, and issues like governance reform of the Bretton Woods Institutions. Its ideal is captured in the phrase 'don't just harmonise, multilateralise'. In the European Union, a key issue is the share of EU aid channelled through the European Commission, currently only just over 20%.[3]

Outside the official world, some have taken the idea of collaboration further, advocating market or network approaches, within a largely self-organising framework.

We begin (Section 2) by reviewing different concepts of governance and 'good governance' and by providing a framework within which to assess the governance of the aid system as it currently stands. We focus on five criteria of good governance: effectiveness; efficiency; legitimacy; accountability; and adaptability.

In Section 3, we describe the aid system as it currently exists: growing and diversifying, variously governed, and often described as an aid 'non-system'.

In Section 4, we assess the governance of aid, finding that none of the DAC, UNDCF, High Level Forums, ad-hoc country-level coordination or multilateralism achieve full marks on our score-card (though multilateralism comes close and will score higher as a result of recent reform of Bretton Woods governance).

In Section 5, we turn to the EU. We summarise the role of the EU in global context and assess the current governance of EU aid, with special reference to the European Consensus on Development and the Code of Conduct on Division of Labour. The European Commission (EC) scores reasonably well on governance, not least because of the accountability

[1] See: http://ec.europa.eu/development/policies/consensus_en.cfm
[2] See: http://europa.eu/legislation_summaries/development/general_development_framework/r13003_en.htm
[3] OECD-DAC data for 2009

mechanisms built into the Cotonou Convention with countries in Africa, the Caribbean and the Pacific.

Finally, we conclude with two paradoxes and four recommendations specifically for the European Union and the European Commission. The first paradox is that that although the system as a whole would work better if most aid was given through multilateral institutions, there are coordination failures which leave many countries preferring a large bilateral programme. The second paradox is that there is a familiar trade-off between effectiveness and accountability with regard to some aspects of aid governance: the DAC, for example, scores highly for its work on statistics and reporting, but remains essentially a rich country club and, partly as a consequence, is largely ineffective in driving change rather than merely keeping score.

Multilateral space is competitive. The EU and the EC can boost their position by: maintaining the mutual accountability provisions of the Cotonou Convention, and widening their geographical reach; increasing transparency; Member States holding each other to account for existing and more demanding targets related to the Code of Conduct on Division of Labour; introducing new instruments, like the Vulnerability Flex (V-FLEX) and the Food Facility; continuing to strengthen collaboration in international fora like the UN, G8, G20 and the United Nations Framework Convention on Climate Change (UNFCC).

1. What is meant by 'governance'?

In the case of nation states, there are different views of what constitutes good governance, but a number of common themes emerge – and these can be applied to the governance of aid.[4] A typical summary is given by Julius Court and Goran Hyden:

> "The *Making Sense of Governance* book identifies six core principles that are widely accepted by researchers and governance stakeholders in developing and transitional societies around the world:
>
> a. Participation: the degree of involvement by affected stakeholders
>
> b. Fairness: the degree to which rules apply equally to everyone in society
>
> c. Decency: the degree to which the formation and stewardship of the rules is undertaken without humiliating or harming people
>
> d. Accountability: the extent to which political actors are responsible to society for what they say and do
>
> e. Transparency: the degree of clarity and openness with which decisions are made
>
> f. Efficiency: the extent to which limited human and financial resources are applied without unnecessary waste, delay or corruption." [5]

Governance of the international aid system is not exactly the same as governance of a nation, but many of these principles translate well into desirable characteristics of a governance system for international aid. Drawing from the governance literature, we suggest the following five dimensions against which a governance system should be assessed:

a. Effective
The governance of the aid system should improve the effectiveness of the aid system as a whole. This means it has to address issues which improve collective outcomes, while leaving to the discretion of developing countries and their development partners those questions which are best resolved individually.

b. Efficient
The governance arrangements should be efficient as well as effective, avoiding unnecessary cost for donors or recipients.

c. Legitimate, fair and decent
The governance system must be legitimate, representing all affected stakeholders, setting rules that apply equally to everyone, treating every stakeholder with respect. It should respect the rights of nation states, both as recipients and donors, while achieving better collective outcomes than could be achieved without governance.

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[4] These are helpfully summarized in Table 1, p.14 of Merilee Grindle's paper (2005), 'Good Enough Governance'. See: http://www.odi.org.uk/events/states_06/29thMar/Grindle%20Paper%20gegredux2005.pdf

[5] Hyden, G., Court, J. & Mease, K. (2004), *Making Sense of Governance: Empirical Evidence from 16 Developing Countries,* London: Lynne Rienner.

d. Transparent and accountable

Good governance must be transparent and accountable to stakeholders. These qualities underpin effectiveness and legitimacy, as well as the ability of the system to adapt.

e. Adaptive

Finally, the governance of aid must not only address the world as it finds it today, but also ensure that it is fit for purpose in the future. As the environment continues to change, so the aid system should evolve with it. The aid system has been handicapped by institutional arrangements that have been hard to change. The response to rapid changes in context – most notably the arrival of new kinds of donors – has been to add complexity rather than to simplify and evolve. The aid system must be organized in a way that allows, and indeed forces, it to adapt more quickly as circumstances change.

These qualities correspond closely to commonly used frameworks for government – for example, the UK Department for International Development refers to governments which are "capable, accountable and responsive".[6]

[6] See, for example: http://www.dfid.gov.uk/Global-Issues/How-we-fight-Poverty/Government/

2. Aid – where have we come from, where are we, and where are we likely to go?

The system of development assistance has its origins in the end of the Second World War, with the establishment of the Bretton Woods institutions. These institutional structures have remained largely unchanged despite very substantial changes in the context in which they operate.

Since the Second World War, the political environment for foreign assistance has changed considerably:

- The Marshall Plan, in which the United States contributed to the rebuilding of post-war Europe, gave respectability to the idea that rich nations could, in the interests of peace and trade, contribute to economic development. The perceived success of the Marshall Plan became a major impetus behind the emergence of aid programmes to developing countries.

- Decolonisation was accompanied in western countries by a growing sense of obligation to their former colonies, and so conventional foreign assistance programmes began in the 1960s, partly modeled on the Marshall Plan.

- The Cold War played out in the developing world as well as in Europe, with the great powers using development assistance in pursuit of their global strategic interests. Huge amounts of aid were given to regimes like those of Mobuto in Zaire and Mengistu in Ethiopia, with the aim of shoring up allies and with little regard to the effects on poverty.

- The first oil shock in the 1970s led to the recycling of surpluses to developing countries, many of whom needed additional funds to cope with rising oil prices; this recycling of surpluses laid the foundation for the subsequent debt crises, and eventually large-scale debt relief in the 1990s.

- From the collapse of the Berlin Wall to the fall of the Twin Towers, donors were able to move away from using aid for geopolitical purposes; and at the same time, the shift in industrialized countries to floating exchange rates reduced their obsession with the balance of payments, allowing development policy-makers to focus on longer-term and broader objectives of reducing poverty and global inequality. It is not a coincidence that this was the period when the International Development Targets, later the MDGs, were established.

- Since 9/11, and the subsequent wars in Afghanistan and Iraq, donors have used more of their development assistance in support of shorter-term political and security objectives, and in support of post-conflict reconstruction and not only on acute poverty. The threat of terrorism has both created a heightened sense of global interdependency, and focused attention on the need to create the conditions in which violent extremism is less likely to be perpetuated.

- Increasing environmental insecurity is becoming a new driver of a changing development relationship. Developing countries face the greatest costs of global warming, despite having contributed little to the problem. In the short term, the challenge is to reach an agreement on addressing global warming that does not slow down development and which compensates developing countries for the damage caused to them by industrialized nations; in the longer run, developing countries may benefit from changes in economic systems which put a higher value on natural resources, so reflecting part of the wealth of developing nations that is undervalued in today's markets.

The changing role of foreign assistance

Against the backdrop of broad geopolitical changes, there has also been an evolution in perceptions about the role of foreign assistance. Following the Second World War, it was argued that long-run welfare depended on capital investment, and that helping countries raise savings through a 'Big Push'[7] would launch them into self-sustaining growth or take-off. As a result, donors funded infrastructure, such as dams and roads. However, by the 1980s the development community had concluded that capital accumulation and technological progress depended not only on the level of investment, but also on a better economic policy environment. The combination of policies that were thought desirable was subsequently dubbed *The Washington Consensus*. By the 1990s, this approach too was in doubt, and it was argued that these policies could only have the impact intended if they were accompanied by more fundamental institutional reforms. A decade later, attention has shifted to even more fundamental causes of poverty such as conflict, rivalry between different social and economic groups, competition for scarce natural resources, and lack of political accountability.
We can characterise this evolution as a search for the underlying causes of poverty. In part this has been motivated by an insistence that aid must be purely temporary, creating the imperative to find a way to catalyze permanent changes in developing countries. This evolution in thinking about the role of aid has inevitably changed the nature of the aid relationship, as it has placed the politics and institutions of developing countries centre stage. As the objective of aid has increasingly been redefined as nothing short of social and political transformation, so it has been increasingly difficult to relate aid to the ambitions held for it.

Aid volumes

The target for rich countries to give aid of 0.7% of national income was first formulated by the Pearson Commission in their report of 1969, although it had its origins in the first meeting of the United Nations Conference on Trade and Development (UNCTAD) in 1964. Reflecting its time, the target was based on an estimate of the amount of capital from abroad that would be needed to increase investment and so accelerate growth in developing countries, though subsequent estimates of the amount of money needed to meet the MDGs have arrived at broadly the same orders of magnitude.

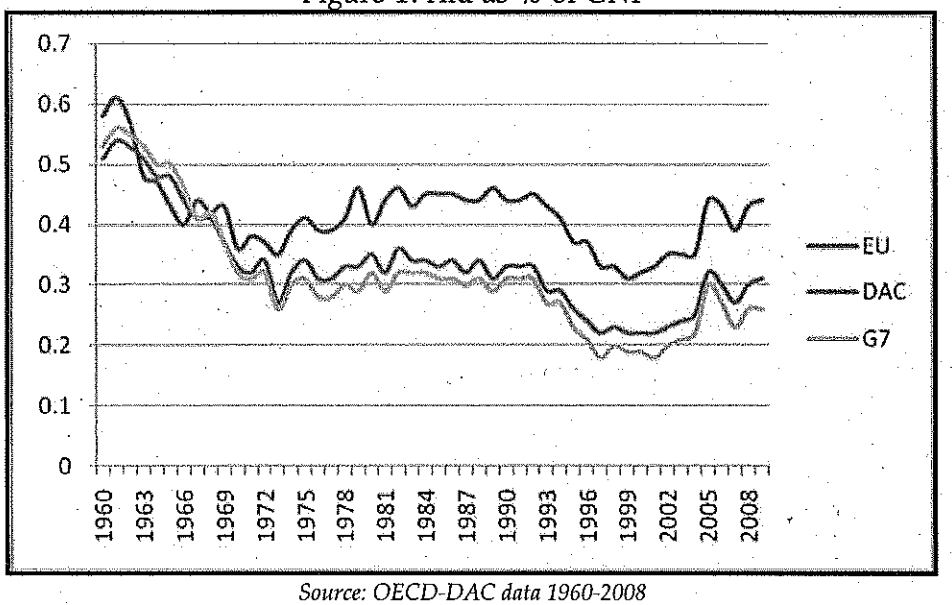
Until 2005, each industrialised country was committed to "exert its best efforts to reach"[8] the target of 0.7% of GNI. Five nations met it: Denmark, Luxembourg, Netherlands, Norway

[7] The idea of the 'Big Push' first came to prominence in Paul Rosenstein Rodan's article 'Problems of Industrialization of Eastern and South-eastern Europe' (1943). The concept of 'take-off' was popularised by Walt Rostow in *The Stages of Economic Growth* (1960)
[8] See: http://www.unmillenniumproject.org/reports/costs_benefits2.htm

and Sweden, and two futher countries (Belgium and France) were committed to doing so. In 2005, all EU-15 countries committed themselves to reaching the 0.7% of GNI target by 2015.[9]

Since the pledges in 2005 to increase it, aid has increased sharply, by 35 percent in real terms from 2004 to 2009. While substantial, this increase falls considerably short of what was promised in 2005. Over 60% of the increase from 2004-2009 has been from EU countries.

Figure 1: Aid as % of GNI



Source: OECD-DAC data 1960-2008

New actors in the aid system

Despite these significant changes over time in the purposes and ideology in development assistance, there was, until the 1990s, very little change in the organisation of the development system. About 70% of aid is given bilaterally, and 30% through multilateral channels, and this has remained broadly constant.

Over time, the EU has become a more important donor, rising from a third of official aid in the 1960s to 56% in 2009.[10] Although a growing proportion of official aid is given by European donors, they are not becoming dominant actors in the development system. Instead, they are faced with a rapidly proliferating environment of new donors and new agencies. The main characteristics of these changes are:

- The number of government donors, and donor agencies, has increased. The DAC now includes 23 nations plus the European Commission, which have between them more than 120 bilateral agencies providing aid to developing countries.

[9] http://www.entwicklung.at/uploads/media/European_Consensus_01.pdf

[10] OECD-DAC data for 2009

- There are now more countries which give official aid outside the DAC than within it, including China, Turkey, Russia, Brazil, India, Venezuela and South Africa. These countries mainly operate in their spheres of influence. The oil-producing states also give large amounts of aid, mainly to Islamic states. These donors typically do not attach much value to the standards and norms set by the DAC, and because they do not report to the DAC, we do not know exactly how much aid is being given. Estimates suggest that China is giving perhaps US$5 billion a year,[11] a little less than the Gates Foundation; and about as much again is given by the other non-DAC government donors.

- There are more than 260 multilateral aid organisations, ranging in size from the World Bank to The Schistosomiasis Control Initiative. Although the overall share of aid going through the multilateral system has remained constant, at about 30% of ODA, for the last 30 years, within that the share going through the UN system has fallen and multilateral spending is now spent through a much larger number of smaller multilateral agencies.

- International philanthropy has taken off over the last decade. This is a predominantly American phenomenon. The Gates Foundation is in a class of its own in terms of size, but the most spectacular growth is among large numbers of smaller foundations.

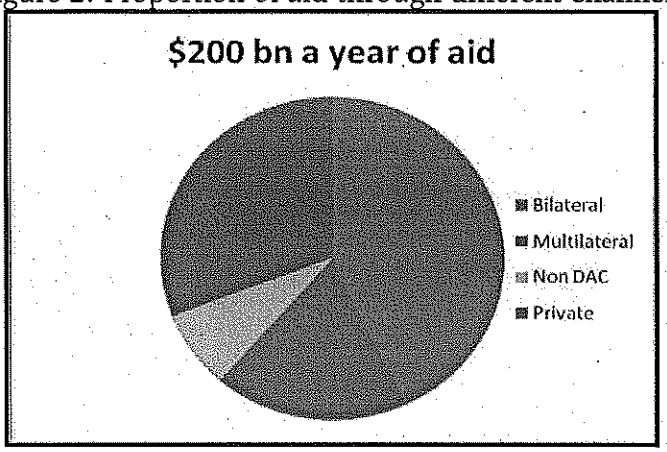
- International NGOs, like World Vision, Oxfam and CARE have also grown rapidly, and are increasingly funded by private individuals rather than governments. International NGOs raise more money for development assistance than the entire UN system.

- Total private development assistance – including foundations, NGOs, educational organizations, churches and private companies – comes to about US$60 billion a year, about half of official development assistance.[12] This exceeds aid through the multilateral system, and may soon overtake bilateral aid.

- The private sector is increasingly involved in development, not only through (relatively modest) giving under the banner of corporate social responsibility, but more fundamentally by changing business models to take account of their customers' growing preference for more ethical and sustainable behaviour.

[11] Kharas, H. (2009), *Development Assistance in the 21st Century.* See: http://www.brookings.edu/papers/2009/11_development_aid_kharas.aspx
[12] *Ibid.*

Figure 2: Proportion of aid through different channels



Source: OECD-DAC data 2009

Total aid to developing countries was about US$200 billion in 2009 (this is an estimate with a wide margin of error, given the difficulty of establishing precise numbers for private giving and giving by non-DAC donors).

Competition and diversity: good news or bad?

The growing array of development actors, and the diversity of their approaches, represents both a challenge and an opportunity. They bring new money and ways of working which could make a substantial contribution to development.

New philanthropic donors bring more money to development, but more importantly they bring new attitudes and ways of working. Large foundations are less dependent on public support for future funding, so they may be willing to support unpopular or un-photogenic causes (e.g. supporting statistical systems in developing countries). Foundations are frequently founded by successful entrepreneurs, so they may be more inclined to operate along business principles, such as making decisions based on evidence, tightly controlling overheads, adopting new technologies, and focusing more sharply on results. They may be willing to take more risks and accept more failures in return for bigger success. They tend to select projects according to the characteristics of the project rather than the country. Foundations may be more able and inclined to work closely with the private sector, which plays a key role in development, but with which official agencies have not found it easy to work.

The rise of new official donors, in particular China, has caused concern among traditional donors, who worry that their implicit cartel is undermined by a donor that is less concerned about governance and human rights, and that is prepared to be more open about its desire for access to raw materials and minerals. China has not been stuck with the DAC development model, and in many ways developing countries prefer China's approach. They rarely poach skilled staff; they provide turnkey infrastructure projects that do not overstretch developing country governments with meetings, reports and workshops. They appear more genuine in respecting local ownership, they operate very differently in different countries, and they seem to be genuinely interested in learning about what works. They are willing to invest in infrastructure, irrigation and university scholarships – all sectors that DAC donors have moved away from. They avoid embezzlement and corruption by rarely using cash: there is

almost no budget support or policy loans, as aid is disbursed to Chinese companies who do the projects.

Private aid through charities tends to focus on supporting communities and individuals rather than developing countries. It tends to be more opportunistic and closer to the ground. People who give money this way value the sense that they can work with local civil society organisations rather than governments, which can bring about results more directly although it is harder to bring about systemic change this way.

Specialised multilateral global organizations are growing in number. They can bring apply skills and expertise, they can learn more systematically and spread knowledge more quickly, they can bring together a number of different donors, the public and the private sector to work in a more joined-up way on a particular issue, and they can raise money from the public because they can be more specific about what they do.

On the one hand, this diversity of development actors could be a growing strength of international aid. Foundations could act like venture capitalists: taking bigger risks but leaving long-term financing of scaled up successes to official aid donors. Private aid could focus on achieving community and individual level results. Specialised global organizations could provide particular expertise not available through generalist support. The diversity of official donors could provide innovation rather than a monoculture of ideas. Official aid agencies could focus on long term funding and resource transfer, and support for institutional change. If these actors could all focus on their strengths, and if the aid system enables them to work together well, the changing development landscape might substantially improve the effectiveness of development assistance.

On the other hand, this proliferation can present huge challenges for everyone involved. Developing countries are forced to deal with a vast, growing number of partners, each with separate agendas, priorities, and requirements. Meetings, reports, milestones and systems multiply. Skilled staff are hired away to serve in local agency offices or NGOs. Funding is fragmented and unpredictable, with developing countries unable to bring together the scale of long-term, predictable finance needed to undertake significant institutional reform and service delivery. Donors lose leverage and influence, because they undermine each other; and yet developing countries are not able to keep track of, let alone exercise sufficient ownership and control over, an increasingly fragmented system of aid delivery. Public accountability is impossible, since nobody has a clear view of what resources are being used, by whom, or for what purpose. Long-term strategy has to be sacrificed to short-term, measurable outputs to meet the immediate needs of individual stakeholders. Donors face rising costs, as administrative costs multiply when agencies proliferate, and the costs of coordination and harmonization rise exponentially with the number of aid agencies. Donor missions, offices and staff proliferate and duplicate.

According to the 2008 survey monitoring the Paris Indicators,

"More than 14,000 donor missions were fielded to the 54 countries that took part in this survey (Indicator 10a). In Vietnam alone, this amounted to 752 donor missions in 2007 —

more than three missions per working day! Of these missions, less than one in five was co-ordinated with another donor".[13]

The effects of this proliferation and lack of coordination substantially reduce the value of aid. A recent study by the European Commission[14] finds that:

- EU Member States have designated a total of 400-500 priority country partners. Increased consolidation of programmes and projects, use of joint financing arrangements, an agreed division of labour and delegated cooperation would save €200-500 million a year;

- EU Member States accounted for 40-50,000 entries in the OECD Creditor Reporting System (CRS) database, an increase from 30,000 in 2003. About 22,000 new commitments were made in 2007 alone by EU countries, with an average budget of €0.7-1 million. The total costs of preparing these projects are estimated at between €2-3 billion per year;

- Increased predictability of EU bilateral aid commitments could increase the value of country programmable aid by between €2 and €4 billion a year.

In Vietnam, it took 18 months and the involvement of 150 government workers to purchase five vehicles for a donor-funded project, because of differences in procurement policies among aid agencies.

It is not just official aid agencies that have to be better coordinated:

"In the aftermath of the tsunami disaster a local doctor in Banda Aceh, one of the most affected areas, wrote: "In February, in Riga (close to Calang) we had a case of measles, a little girl. Immediately, all epidemiologists of Banda Aceh came in, because they were afraid of a propagation of measles among displaced people, but the little girl recovered very fast. Then, we realized that this was not a normal case of measles and we discovered that this girl has received the same vaccine three times, from three different organizations. The measles symptoms were a result of the three vaccines she received."[15]

Although the costs of proliferation are well known, and donors have committed themselves to coordinate, harmonise, and to make more use of country systems, in fact the number of projects is continuing to rise and the average project size is continuing to fall.

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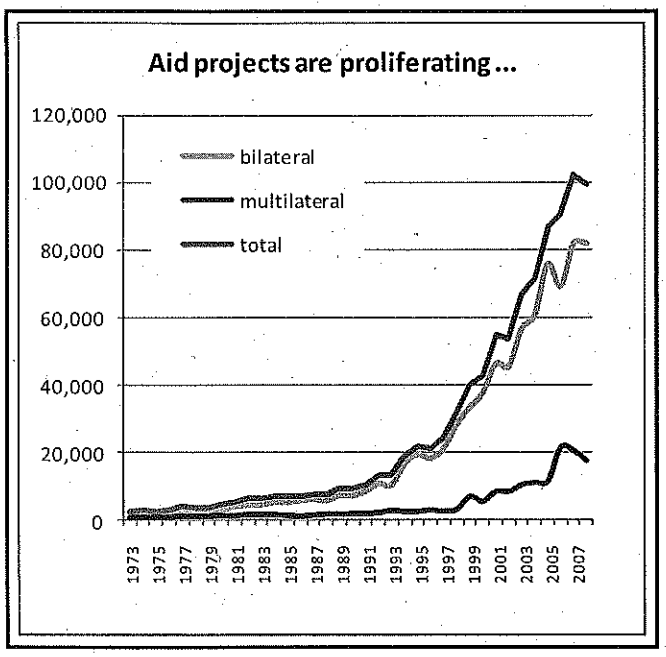
[13] OECD (2008), *Better Aid: 2008 Survey on Monitoring the Paris Declaration, Making Aid More Effective by 2015*, p.15. See: http://www.oecd.org/dataoecd/58/41/41202121.pdf

[14] European Commission (2010), *Aid Effectiveness Agenda: Benefits of a European Approach.* See: http://ec.europa.eu/development/icenter/repository/AE_Full_Final_Report_20091023.pdf

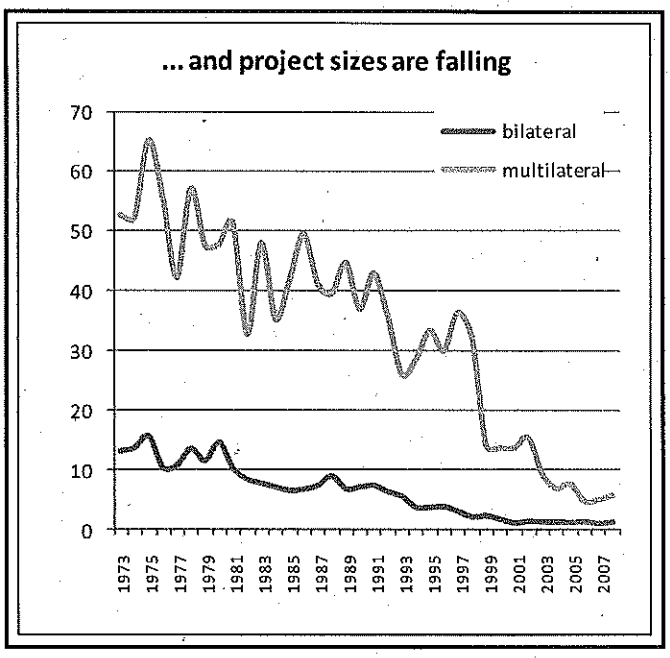
[15] El Pais, April 13, 2005, p.2. Quoted in Djankov, S., J. García Montalvo & M. Reynal Querol (2009), 'Aid with multiple personalities', *Journal of Comparative Economics* 37(2), p.217-229

Figure 3: The proliferation of aid projects projects



Source: AidData http://www.aiddata.org/home/index

Figure 4: The decreasing size of aid



Source: AidData http://www.aiddata.org/home/index

3. The governance of aid

Why do we need any sort of international governance of aid?

What determines whether the benefits of diversity are secured, and the challenges of proliferation avoided? Success and failure are divided by a knife edge. If diverse actors can each play their part, and the parts link together well, then this diverse, competitive, noisy development system can be a coherent whole, greater than the sum of its parts. This requires different actors to pursue their interests within shared rules of the game, with appropriate mechanisms to limit negative spill-overs and ensure the collective provision of public goods within the system. But if the governance of the system fails, the result will be that developing countries bear many of the costs of proliferation, but with many fewer benefits.

Sometimes, the lightest governance is all that is needed. One of the most transformative social changes of our generation has been the spread of the internet, and the enormous range of uses to which it has been put. This revolution has occurred in the presence of very light governance arrangements. The internet is largely self-governing and self-correcting. Where it has thrown up problems – such as email spam – it has also found ways to work around those problems. (Interestingly, the philosophy of working round problems is so much part of the internet culture that it is built in a fundamental way into the technical specifications of the internet: if the shortest possible path for data to move is blocked, the system automatically looks for another path.)

The thought leaders of the internet have generally taken the view that the internet is better off without government interference: it can solve its own problems, while retaining the freedom and individualism that enables it to innovate, adapt and grow.[16]

Analogously, it is reasonable to ask why the international aid system needs any sort of governance. As with the internet, there is a danger that any sort of governance arrangements will slow innovation and stifle change and add to costs. Given that aid consists of arrangements freely entered into between sovereign nation states, and between consenting adults, what is the case for any kind of governance arrangements?

Aid needs governance arrangements for the same reasons that intervention is warranted in other sectors: there are some results that can only be achieved collectively, and individuals will tend to underinvest in these public goods; the actions of some individuals can have negative impacts on others, which need either to regulated or at least priced. Suitable governance arrangements can, in these circumstances, make the aid system more effective. For the money that is spent on development, better outcomes can be achieved if these public goods are provided and spillover effects are properly managed.

Working from the principles of good governance laid out in Section 2, it is possible to imagine ten ways in which a system of collective governance could make the aid system more effective. These are described below and summarised in Box 1.

[16] See, for example: Perry Barlow, J. (2006), *A Declaration of the Independence of Cyberspace.*

(a) Encouraging positive spillovers

There is strong evidence of positive synergies between aid activities: one donor's investment in agriculture is more productive as a result of another donor's investment in feeder roads. Millennium Villages are an example of efforts to bring about many different changes at the same time. Some development assistance is inherently collective – such as designing and implementing a reform programme, or filling a financing gap – and requires donors to work towards a shared goal.

(b) Reducing negative spillovers

The activities of on aid agency can adversely affect the impact of another. An aid agency that recruits a specialist from a government department undermines the efforts of another agency to build capacity. Aid agencies that require meetings with Ministers, or monitoring and review meetings with officials, slow down broader progress (this is analogous to a form of 'aid pollution'). The prices of scarce resources needed by aid agencies – offices, houses, and vehicles – can be driven up by the presence of multiple aid agencies. Incentives created by one aid agency can dull the carefully constructed incentives created by another.

Box 1: Benefits of better governance of the aid system

- Encourage positive spillovers
- Reduce negative spillovers
- Coordination
- Prevent free-riding
- Information sharing and learning
- Division of labour and cost-effectiveness
- Secure investment in public goods
- Align incentives to development objectives
- Protect long-term goals from short-term pressures
- Voice and accountability

(c) Coordination

The optimal behaviour for one agency may depend on the behaviour of others. A clear example is aid allocation, in which the optimal choice by one donor of where to work, and on what, depends directly on the choices being made by other donors. This is necessary in order to avoid some countries becoming 'aid orphans' or 'donor darlings', for example. Optimal decisions about the allocation of research funding similarly depend on what other donors are doing. Complex institutional change programmes requiring sequenced reforms will work best if donors are making their contribution to a coordinated overall programme.

(d) Preventing free-riding

Everyone benefits from a more just, safer world, with prosperous trading partners. But some countries may be tempted to 'free-ride' on the generosity of others. For example, a

country could give relatively little aid, in the expectation that others will give more, so benefitting from economic development without paying for it. A country may benefit from the fact that other donors 'untie' their aid, so its firms can compete for other donors' contracts, while choosing not to untie their own aid. One of the original motivations for establishing the OECD-DAC was to monitor volumes of aid given by each donor. Countries that have provided debt relief are concerned by the possibility that this has opened the way for other countries to take advantage of this by making new loans to those countries in return for mineral concessions. If these fears are realised, it will reduce their willingness to give debt relief in future.

(e) Information sharing and learning

Aid agencies increasingly see themselves as organisations whose value is not *administration* but *knowledge*. Project administration is important, but it is also fairly straightforward; more complicated is learning what works, adapting it to different circumstances, influencing policies, sharing ideas, building capacity and shared commitment. This learning and knowledge sharing is needed across aid agencies as well as within them. The DAC networks (eg. GovNet) and the peer review mechanism are examples of this kind of role. Aid agencies also need a way to share basic aid information, which they do through in-country aid management systems, the two DAC databases, and the Financial Tracking Service (FTS) of the Office for the Coordination of Humanitarian Affairs. All of this contributes to reduced information asymmetries and a lower risk of principal-agent problems in administering aid.

(f) Division of labour

The overall effectiveness of the aid system is increased if organisations focus on the activities in which they have a comparative advantage. In market-based systems, concentration of comparative advantage is a *result* of profit maximising behavior, rather than a *mechanism* for making choices. Firms are driven towards the activities in which they can make the most profit: the forces of price, supply and demand help to ensure an optimal use of resources. In the absence of a market mechanism, some kind of mechanism is needed to push aid agencies into concentrating on the countries and activities where their opportunity cost is lowest, sometimes in the face of countervailing political pressures to spread themselves more thinly.

(g) Investing in public goods

Public goods tend to attract too little investment because, by definition, the benefits are widespread, so individual countries and agencies do not have a strong incentive to spend money on them. For example, the knowledge created by research and development is a public good, with benefits that spread far beyond the country that paid for it. There is significant global under-investment in development public goods such as reducing climate change, financial stability, norms and standards, evaluation, and knowledge. Nation states address the need for investment in public goods by a combination of government spending and regulation; there is no equivalent of either in the development system.

(h) Keep incentives aligned to development objectives (prisoners' dilemma)

Donors invest in foreign assistance for a variety of reasons. Some of these are shared global objectives: for example, reducing absolute poverty is a shared moral endeavour. All nations benefit when the world is less unequal, when world trade increases, and the risks of conflict, organised crime, drugs and disease are reduced by economic

advancement. But donors are also willing to invest in foreign assistance in pursuit of their own national interest to the disadvantage of other countries: for example, to win commercial contracts, gain geopolitical strategic advantage over rivals, or to stake a claim to oil or mineral resources. The aid system is more effective at reducing poverty to the extent that the shared goals are pursued in preference to the competitive interests of donors. This is a prisoners' dilemma problem – everyone is better off when aid is untied from commercial interests, for example; but each individual agency has an incentive to tie their own aid. A system of coordination among donors is needed to ensure that their actions are aligned with their collective interest in poverty reduction, and that this is not undermined by pursuit of individual national interests.

(i) Protecting long-term goals from short-term pressures

Most democracies have evolved governance institutions to protect the nation's long-term interests from immediate political pressures. Examples include written constitutions, an independent judiciary and independent central banks. In development, long-term interests are frequently sacrificed to short-term expediency. For example, imported food aid may reduce hunger immediately, but at the expense of undermining domestic agriculture production in the long run. Donor-managed projects may provide services to the poor with lower risk of corruption and theft, but at the expense of undermining the capacity of the country's institutions to manage their own services. A good system of governance ensures that long-term needs are not ignored in the interests of short-term pressures.

(j) Voice and accountability

Finally, governance mechanisms are required to assure voice and accountability for all stakeholders in aid, including especially developing countries themselves.

These themes constitute a compelling case for effective governance of the aid system. They demonstrate why it is not sufficient simply for donors each to pursue their own immediate interests; because the result will be lack of investment in public goods, failures of coordination and behaviors which have negative spillover effects on others. There are examples in the aid system of all the reasons why nation states establish their own governance arrangements.

What kinds of governance do we already have?

The aid system already has some types of governance in place. The main components are:

(a) The Development Assistance Committee (DAC) of the OECD

A 'donor club' of 24 donors.[17] It collects comparable information from donors, shares information and ideas through regular meetings of officials, sets implicit standards, and reviews them through peer review. The Working Party on Aid Effectiveness, technically a committee of the DAC, has broader representation than the DAC, but fewer instruments at its disposal.

[17] The EU-15 and the European Commission, plus Australia, Canada, Japan, South Korea, New Zealand, Norway, Switzerland and the United States.

(b) The UN Development Cooperation Forum (UNDCF)

A multi-stakeholder forum hosted by the UN, including donors, recipient governments and civil society. So far mainly a talk-shop, but with aspirations to do more.

(c) In country cooperation

Many of the issues of coordination are addressed in developing countries through donor cooperation forums, with the recipient government sometimes playing a leading role. So far these have tended to focus on information sharing and some harmonization of donor efforts.

(d) High Level Forums (Rome Paris, Accra and Seoul)

These meetings every two to three years have brought together developing countries and donors, together with largely token representation by civil society, in an effort to set and enforce new rules of the game.

(e) Multilateral organisations

Multilateralism can be viewed as an effort to overcome some of the challenges above: by giving aid through international organisations, aid can be put more at arm's length from the political pressures of the donor, and aid from many donors can be coordinated into a single operation. Multilateral organizations have also played an important role in improving lesson learning and information sharing.

How well governed is the aid system today?

The aid industry stands accused of being ineffective and wasteful. The problems are serious and real: unnecessary proliferation of aid agencies without adequate division of labour, rising transactions and administration costs, short-termism and unpredictability, risk aversion, undermining of local systems of service delivery and accountability, inability to stop failing projects or organisations, ineffective provision of technical assistance, lack of mechanisms to take success to scale, underinvestment in public goods, lack of evidence of impact and results, inadequate learning, distortion of aid for national interests, and poor aid allocation.

Arguably all these challenges are the direct consequence of failures of collective governance.

This failure of governance is encapsulated nicely by the process of agreeing the MDGs. The declaration by world leaders was a historic event, setting a clear agenda for development for the following fifteen years. But there was no organisation to translate strategic objectives into specific milestones and to monitor progress. There was no allocation of responsibilities; and no accountability of donors or developing countries for their contribution to the agreed goals. In short, the Millennium Summit willed the ends but not the means.

This does not imply that the aid system necessarily needs a single governance mechanism, such as an overarching council or committee. But, as we have set out here, there are real issues of collective action that have to be addressed if the aid system is to be effective, which are currently not being addressed in a sufficiently effective way.

Table 1 below sets out our subjective judgments of existing governance mechanisms in international development against the five dimensions of our governance model: effective,

efficient, legitimate, accountable and adaptive. We find that none scores the highest marks available on the score-card. Multilateral options score relatively well, however.

Table 1: Assessment of existing governance mechanisms against criteria of good government

	Effective	**Efficient**	**Legitimate & fair**	**Transparent and accountable**	**Adaptive**
OECD DAC	Effective at information sharing among donors; some lesson learning. Not good at preventing spillovers, investing in public goods, improving division of labour, aligning incentives, or promoting long-term development interests.	Very high transactions costs for donors and recipient countries	The DAC is a committee of 23 rich countries.	The DAC collects and publishes statistics about aid outflows from its members; and it publishes peer reviews. But decision-making by consensus limits its ability to criticize members and accountability is weak.	The DAC has almost completely failed to respond to a changing context. DAC donors lack transparency.
UN DCF	So far the UN DCF has been a talking shop and has little to show for its meetings.	Expensive for few results.	Under the auspices of the UN, the DCF is representative.	The DCF is a fairly transparent and participative process.	Early days, but the process seems unlikely to be responsive to changing circumstances.
In country cooperation	Some country-led processes have made progress towards harmonisation. But many of the challenges cannot be solved at country level – eg. investment in global	Coordination processes can be labour intensive, with few results	Developing countries can, in principle, exercise leadership over development activities in their country.	In country cooperation happens behind closed doors, with very little involvement of either local or international civil society. Taxpayers from donor nations have no access	Decsion-making close to the ground is most likely to be informed by the effects of those choices. The process lacks local transparency.

	public goods, division of labour. In practice it is difficult for recipient countries to change donor incentives to purse their national interests. In-country processes have not engaged new actors such as foundations.			to these forums.	
High Level Forums	Declarations have been modest in ambition, reflecting lowest-common denominator agreements, and poorly implemented or enforced. Many issues have not been addressed at all.	Very expensive processes leading up to summits; very expensive implementation and monitoring.	Led by the DAC and World Bank, with rather token representation of hand-picked developing countries and little place for civil society.	The HLF declaration is negotiated in a smoke-filled room from which civil society is excluded. The microphones were removed from the desks of civil society delegates in the plenary sessions at Accra.	These processes feel as if they were designed in the 1970s, with little recognition of the changing landscape.
Multilaterals	Providing money through multilaterals is easier and more effective than harmonising. Multilaterals have been less susceptible to political second guessing. But they	Some multilaterals – especially UN agencies – have high overheads. Proliferation adds to costs.	Many stakeholders are underrepresented in decision making – for example on the World Bank board. But UN bodies are legitimate.	Multilaterals are generally more transparent than bilateral aid. The World Bank, in particular, has advanced hugely in this regard.	Multilaterals seem to adapt more quickly to changing needs, partly because of the need to raise money from donors.

	continue to under-invest in public goods, and multilateral proliferation is becoming a problem.				

Reform proposals and timetables

There are currently a number of proposals for reform of the aid system and individual institutions within it. In aggregate, these should improve performance across the indicators on the score-card.

(a) Following the recommendation of the OECD Council's In-Depth Evaluation in 2007, the DAC has recently undertaken a Strategic Reflection Exercise, to review its role, structure, functioning and composition. The outcomes of the Exercise are to form the basis for reform of the DAC mandate, expected to be renewed by the Council in 2011 for five years. The report concluded that the DAC needed to adapt its core activities - sharpening its principal tools and working methods and taking an active role in the process of reforming the global governance framework. Amongst other recommendations, the report outlined the need for the DAC to: re-articulate its role in a changing development landscape in its mandate; to extend and deepen inclusion of key development stakeholders in all areas of its work; to help the wider process of reforming and strengthening the multilateral development system; and, to adapt its internal structures and processes[18]. Presently, the DAC is working on the detail of implementing the recommendations and is expected to submit a draft revised mandate to the Council in mid-2010.

(b) In light of both the Paris Declaration and the Accra Agenda for Action, the DAC's Working Party on Aid Effectiveness recently underwent structural changes (principally by expanding its membership) and formulated a revised workplan, to establish itself as the international partnership on aid effectiveness.

(c) The biennial Development Cooperation Forum, hosted by the UN's ECOSOC, was launched in 2007, with the first Forum meeting taking place in 2008. The second Forum meeting is currently being prepared for 29-30 June 2010. Structured around three themes - mutual accountability and aid transparency; South-South and triangular cooperation; aid policy coherence, in order to move to more long-term sources of development financing - the objective of the 2010 DCF will be to produce agreement on priority issues for action that are based on practical outcomes.

(d) The reform of the governance of the World Bank and the IMF has been the subject of debate for many years. Whilst both donors and recipients are member states and shareholders in the two institutions, voting power on the Governing Boards is determined primarily by financial contribution. Most recently, however, at meetings in April 2010, the Development Committee approved a proposed voting reform for the Bank. In summary, these changes would instigate:
   - an increase in the voting power of Developing and Transition countries (DTCs) at IBRD, bringing them to 47.19 percent;
   - an increase in the voting power of Developing and Transition Countries at IFC to 39.48 percent; and

[18] DAC Reflection Exercise (2009), Investing in Development: A Common Cause in a Changing World, p. 4

- an agreement to review IBRD and IFC shareholdings every five years with a commitment to equitable voting power between developed countries and DTCs over time.

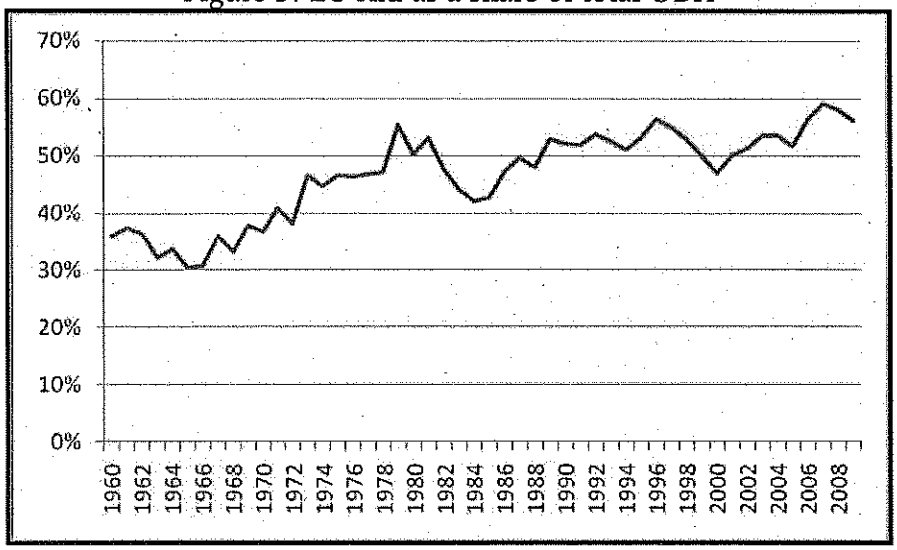
Proposals to increase aid effectiveness, such as the declarations made in Paris (2005) and Accra (2008), have worked to mitigate the problems of the aid system in ways which add layers of complexity. Harmonisation and alignment have, in practice, been translated on the ground into donor coordination committees, with lead donors and sectoral plans. At their best, these have helped to reduce transaction costs and harmonise donor approaches; at their worst, they have led to very little real change in behaviour. At its most positive, the agreement of clear standards – particularly in the Paris Declaration (2005) – has emboldened some recipient countries to be clear about their expectations of donors. But addressing the symptoms without addressing the underlying causes results in new problems: to the extent that the expectations of recipient countries conflict with the underlying political and strategic interests of the donors, the long-term consequence is sometimes a reluctance of donors to give aid to those countries. Aid effectiveness declarations describe a better way of giving development assistance, but they do not address the underlying reasons why donors have given aid in less effective ways for the last forty years. If barriers to good aid are political, not technical, then technocratic agreements cannot overcome them.

4. The EU in the global aid context

The EU is the world's leading exporter of goods, largest trader of services and biggest donor of both development and humanitarian aid, the second largest foreign investor and the second destination for foreign migrants (behind the USA). As a model of multilateral cooperation itself, the EU is a frontrunner in the pursuit of value-based multilateralism and its commitment to effective multilateralism in all fields is a defining principle of its external policy. As noted in the European Commission Communication on 'The European Union and the United Nations: The Choice of Multilateralism',
"Taking international co-operation as a precondition for meeting numerous global challenges, the EU has a clear interest in supporting the continuous evolution and improvement of the tools of global governance."[19]

Although the EU is a major player in official aid and in private flows, critics have argued that it is (a) falling behind on its aid pledges, (b) lagging behind on its commitments to improving aid effectiveness and cost efficiency, (c) lacking in strategic focus of its aid, and (d) undecided about what role EC managed aid should play in the future. In 2010, the big challenge for the EU will be to demonstrate that it is able to live up to its commitments in the run-up to the UN MDG Review Summit in September. Other important decisions on the horizon include the EU Budget Review in 2010 and the launch of the negotiations for the next EU Financial Perspectives in 2011.

Figure 5: EU Aid as a share of total ODA



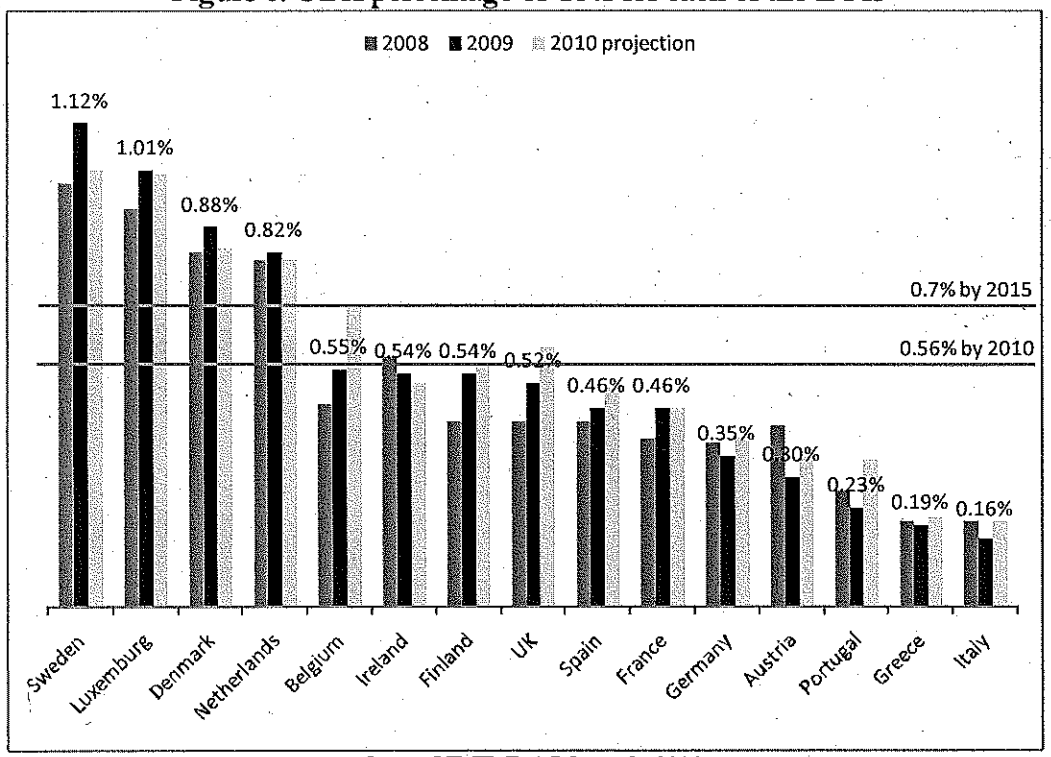
Source: OECD-DAC data

[19] European Commission (2003), 'Communication from the Commission to the Council and the European Parliament', *The European Union and the United Nations: The Choice of Multilateralism*, COM(2003) 526 final, Brussels, 10 September 2003, p. 3

As the world's largest donor to developing countries, collectively the EU provides 56% of global development aid flows (around €50 billion of the €90 billion total given in aid)[20] and in 2009, the EU provided 0.44% of its GNI. According to the OECD's analysis, eight EU Member States are going to surpass their individual targets of 0.51% of GNI for aid: Belgium, Denmark, Finland, Ireland, Luxembourg, the Netherlands, Sweden and the United Kingdom. Spain will meet its target of 0.51%. In 2009, France increased disbursements by 16.9%, as did the UK, by 14.6%. Yet, there were substantial aid cuts in: Austria -31.2%, Italy -31.1% and Ireland -18.9%. Six EU Member States have underperformed: Austria, France, Germany, Greece, Italy and Portugal. The greatest absolute decrease in ODA has been Germany's - almost €1.5 billion less in 2009 than in the previous year. While in Italy and Ireland, decreases were caused by actual cuts to aid budget, in Germany and Austria ODA shrank because no major debt relief was given. Figure 6 shows the ODA percentage of GNI for the EU 15 in 2008 and 2009, the forecast for 2010 and the 0.7% target by 2015.

As a consequence, total EU ODA is projected to amount to 0.48% of GNI in 2010 rather than the pledged 0.56%. At the same time, as the economic downturn continues to have a negative effect on growth in many developed countries, GNI is likely to fall. Therefore, even if the EU continued to meet the percentage targets for aid expenditure, the actual *amount* derived from that percentage is less than would have been predicted when the 0.7% target was set. The EC has time and again encouraged all Member States to set out rolling multi-annual indicative timetables showing how they will reach agreed ODA/GNI targets. However, most Member States have yet to produce a timetable, citing legal restrictions related to their national budget cycle.

Figure 6: ODA percentage of GNI for each of the EU15



Source: OECD DAC figures for 2009

[20] OECD-DAC data for 2009

Almost all of the EU-12 - the newer Member States, which have a common interim target of 0.17% by 2010 - will decrease or stagnate around existing aid levels.

At present, the share of EU aid channelled through the EC is currently around 20%.[21] In 2009, the EC's ODA increased by 4.4% in real terms, down from the 17.5% increase in 2008.[22]

How does the governance of the EU compare?

Effective

A decade ago, the UK Secretary of State for International Development at the time, Clare Short, characterised the Commission as the "worst development agency in the world"[23]. At the time, the EC suffered from a variety of ailments: the distinctive added-value of EC aid was unclear; it largely failed to adopt a coherent approach to managing its external assistance; its policies were guided by individual instruments rather than by clearly defined development objectives per country, region or sector; its aid system was fragmented in terms of small, ad-hoc instruments, too many procedures and opaque institutional mechanisms; and its organisational set-up was outdated and incoherent. As a result, long delays built up in different parts of the system and bureaucratisation and centralisation were rampant.

A decade ago began the reforms of the EC which addressed strategy and management. Since 2000, there have been substantial improvements to the effectiveness of EU external assistance, designed to restore the credibility, effectiveness and legitimacy of EC aid, and also to articulate common values and principles.

Adopted in 2005 by the EC, the Council and the European Parliament, and building on the initial 'EC Development Policy Statement' the European Consensus on Development[24] sets out the common vision of values, objectives, principles and means to development shared by all Member States and the EC. It emphasises poverty reduction as the central goal and asserts the priority of assistance to Low Income Countries (LICs). Administratively, it professes a shift from project aid to general budget support and to performance-based assessment. Conditionality is expressed in a 'contract' with the partner country, recognising that aid effectiveness can only be achieved through 'national ownership' of aid programmes by the developing country. It defines the comparative advantage and priorities of the collective development effort implemented by the EC.

The European Consensus was hard-won. However, it has not been adopted as the visionary policy statement beyond its founders, the Development Commissioner and DG Development, let alone by the EU Member States. In spite of the fact that the European Consensus calls for concentration of aid in LICs, EC aid retains ambition of almost universal coverage. It is present in 120 developing countries. In 2007, 44% of EC aid was allocated to LICs. The DAC average for all donors was 63% and the average for the EU was 65%. In 2008, EC aid to LDCs fell to 42%. The 2007 OECD DAC Peer Review of EC Aid[25] attributes this to the

[21] OECD-DAC data for 2009
[22] *Ibid.*
[23] See: http://www.publications.parliament.uk/pa/cm199900/cmselect/cmintdev/669/66904.htm
[24] See: http://ec.europa.eu/development/policies/consensus_en.cfm
[25] See: http://www.oecd.org/document/0/0,3343,en_2649_34603_38897408_1_1_1_1,00.html

EC's limited ability to influence the EDF (determined by Member States) and the Community budget (determined by the Council of Ministers and the European Parliament). The DAC points out that the EU attaches particular importance to its neighbouring states, particularly in the context of their prospective membership of the EU. Turkey's status as the main recipient of EC aid for the past years is a case in point. Furthermore, while the European Consensus emphasises the need for the EC to concentrate upon its areas of comparative advantage, these are broadly defined, with the number of priority areas for EC action increasing from six in the original Development Policy Statement to nine in the European Consensus – water and energy provision, and social cohesion and development have been added to trade and regional integration, the environment, infrastructure and transport, rural development, governance, conflict prevention and fragile states, and human development.

The Consensus also proposes to enhance EU coordination through greater emphasis upon a division of labour, exploiting individual partners' comparative advantage. In particular, it emphasises the potential for co-financing, either with Member States providing additional funding for EC-led programmes or the EC supplementing Member State-led programmes.

In May 2007, the Council approved the EU Code of Conduct on Complementarity and Division of Labour in Development Policy[26] and joint financing approaches that include common EU funds, co-financing agreements, mutual recognition and delegation. The Code of Conduct addresses the division of labour amongst the Member States and the EC, across developing countries and across sectors within each developing country. In particular, all donors should restrict themselves to a maximum of three sectors per country and either redeploy out of other sectors or work as a silent partner, allowing another EU donor to take the lead. A further constraint is that there should be only three to five donors per sector. But, it remains voluntary and it wills ends rather than means.

In April 2008, the EC issued a Communication on 'The EU – A global partner for development: Speeding up progress towards the Millennium Development Goals'[27] in which it proposed actions to encourage Member States to increase the volume and the effectiveness of aid, as well as areas where EU policies could be better coordinated to meet the MDGs. And in April 2009, the EC produced a Communication on 'Supporting developing countries in coping with the crisis'[28] in which it analysed progress on aid effectiveness, on the EU's own Code of Conduct on Complementarity and Division of Labour and on aid volumes, and offered 28 concrete proposals covering the volume of aid and other finance; aid effectiveness; social protection; sustaining economic activity; revitalising agriculture; investing in green growth; stimulating trade and private investment; economic governance; trade; and global institutions.

Following the adoption of the Accra Agenda for Action (AAA) in 2008, there are now, in addition to the 12 indicators agreed to in the Paris Declaration, 48 new or strengthened commitments for the development community as a whole, 34 of which are for donors to implement. The EU has four additional targets from 2005, confirmed in the European Consensus on Development and now partly reflected in the AAA:

[26] See: http://europa.eu/legislation_summaries/development/general_development_framework/r13003_en.htm
[27] EC Communication (2008), 'The EU – a global partner for development: Speeding up progress towards the Millennium Development Goals', COM(2008) 177 final, 9 April 2008
[28] EC Communication (2009), 'Supporting developing countries in coping with the crisis', COM (2009) 160/4, 8 April 2009

(1) Providing all capacity-building assistance through coordinated programmes, increasingly through multi-donor arrangements;
(2) Channelling 50% of government-to-government assistance through country systems, including by increasing the aid we provide through budget support or sector-wide approaches;
(3) Avoiding setting up any new project implementation units; and
(4) Reducing by 50% the number of uncoordinated missions.

To date, coordination between Member States has proved to be an uphill task. Dilemmas about the current and future roles of the EC in driving division of labour continue to persist:

- European codes versus global decision-making, with the EU Code of Conduct focused on EU donor sectoral specialisation and the Accra Agenda for Action focused on global aid effectiveness, involving partner countries in the discussions on division of labour;

- European versus country-led comparative advantages, with the EU Code of Conduct defining the EC's comparative advantage based on 'amount of money', 'experience', 'staff/expertise', 'history of engagement', and so on, whereas most of the country-led criteria relate to alignment and harmonisation, as well as dialogue skills, risk-taking, innovation and credibility; and

- Brussels leadership versus stagnation on the ground, with the EU Code of Conduct lacking leadership both at Headquarters and country levels and the need for clarity as to the mandate of the EC in promoting division of labour.

Efficient

According to the EC study 'Aid Effectiveness Agenda: Benefits of a European Approach'[29], the financial costs of donors failing to ensure aid effectiveness could be between €25 and €30 billion from now until 2015, or €5 to €7 billion per year. This amounts to around 10% of total aid spending. It is worth noting that throughout the study, the authors seemed to struggle to obtain the accurate data needed to calculate the real cost savings of implementing the current aid effectiveness agenda. Even the most basic data on office costs or staff time was either unavailable or undisclosed by Member States. For the EC, while input and output of EC aid are documented quite well, efforts to analyse outcomes and impact are rare.

Table 2 gives the EU's performance on some of the key targets in the Paris Declaration and the Accra Agenda for Action (AAA). Progress on aid effectiveness has been slow, in particular on:

- Division of labour, due to, among other things, Member States' wish to remain engaged in politically attractive sectors, the lack of visibility when cooperation is delegated, the perception that coordination is time-consuming and not cost-effective for some interventions, the lack of overview on what different donors are doing in a

[29] Carisson, B. T., Schubert C. B., Robinson S. (2009), 'The Aid Effectiveness Agenda: Benefits of a European Approach'. Available at: http://ec.europa.eu/development/icenter/repository/AE_Full_Final_Report_20091023.pdf

given country or region, and in some cases hesitations by recipient countries that fear losing aid for particular sectors. The EC itself is the biggest culprit because of its presence in 120 countries. Only 33% of EU donors' and the EC's missions are coordinated[30]. The EU target is 66%.

- Use of country systems, because of lack of trust in the use of recipient country systems and legal impediments in the Member States. Another major impediment is the mode in which aid is delivered. Only five EU Member States now say budget support is their preferred way to scale up aid to Africa and to promote ownership, compared with ten in 2008. Budget support, granted for a three-year period, is the EC's "preferred aid modality where conditions allow".[31] Proponents of budget support argue that it boosts ownership and raises the effectiveness, efficiency and significance of development contributions. Others point to the risks arguing its potential to permit misuse and misappropriation of development funds; to concentrate power in finance ministries at the expense of key line ministries, thereby marginalising them from policy debates; and to intensify conditionality by giving donors a seat at the table in fundamental discussions on issues such as civil service reform and budget formulation. Under EDF 10, the EC aims to increase budget support, both general and sectoral, to 44% of programmable funds, 25% of all funding.

- Conditionality, with most Member States claiming the irrelevance of it. Irrelevant possibly as a result of conditionality imposed by intermediaries such as the World Bank and the IMF, or because recipients accept them just to receive aid. Only five Member States told the Commission that they are actively reducing the number of conditionalities, while thirteen are not, and no result is recorded for the remaining nine. Fourteen Member States still do not make their conditions public, although this was one of the commitments in the AAA that was supposed to take instant effect.

- Predictability of aid, due to legal constraints in Member States and annual budget cycles. The consequences of short-term aid include conservative budgeting practises by recipient governments, poor resource allocation, investments in capital expenditure to the detriment of recurrent costs and even macro economic instability. In 2008, the EC launched the 'MDG Contract', an innovative spin-off of budget support. It provides General Budget Support (GBS) for six years instead of three, including one mid-term review rather than annual assessments and a minimum guaranteed aid level (70% of total commitment). MDG Contracts, which are subject to the provisions of the Cotonou Partnership Agreement, have been rolled out in eight African countries (Burkina Faso, Ghana, Mali, Mozambique, Rwanda, Tanzania, Uganda and Zambia). Collectively, these account for €1.8 billion, or 50% of all GBS commitments in EDF 10 national programmes, and some 14% of all EDF 10 national programmes. There has, however, been little forthcoming support from

[30] EC Staff Working Paper (2009), 'Aid Effectiveness after Accra: Where does the EU stand and what more do we need to do', COM (2009) 160 final

[31] Official Journal of the European Union: Joint Statement by the Council, the European Parliament and the EC on European Union Development Policy: 'The European Consensus' (2006/C 46/01), par. 113

Member States to co-finance these contracts; only Belgium has, contributing €12 million to the MDG Contract with Mozambique.

- Tied aid, because of inadequate procurement regulations and capacities in developing countries or risk aversion at donor headquarters level. At present around 10% of EU aid is still tied. While most DAC members have made commitments to untie aid in the future, this is the one Paris Declaration commitment to which a quantitative target has not been attached.

Table 2: Monitoring the Paris Declaration: EU state on some key targets

Paris Indicators	EU (Member States and EC)	EC	2010 Target
Aid flows are recorded in countries' budgets	44%	57%	85%
Technical assistance is aligned and coordinated	53%	43%	EU target: 100% (Paris target is 50%)
Donors use country systems for public financial management	47%	35%	50-80% (EU and now Accra global target is 50%. Targets for each individual partner country depends on performance)
Donors use country procurement systems	54%	34%	50-80% (EU and now Accra global target is 50%. Targets for each individual partner country depends on performance)
Aid is more predictable	43%	53%	71%
Aid is untied	94%	NA	Indicative: 100%
Donors use coordinated mechanisms for aid delivery (through programme-based approaches)	46%	44%	66%
Donors coordinate their missions	33%	33%	EU target: 66% (Paris target is 40%)
Donors coordinate their (country) studies and analytical work	62%	72%	66%

Source: EC Staff Working Paper: 'Aid Effectiveness after Accra: Where does the EU stand and what more do we need to do', COM (2009) 160 final

Legitimate and fair

The EU does not consistently 'speak with one voice' as a global actor, but its representation varies from the EC, to the rotating EU presidency, to the national positions of the Member States. For instance, the EC represents the EU on trade issues in the World Trade Organisation (WTO); the rotating EU presidency negotiates on behalf of the EU (for example, in the climate change negotiations); and the Member States are dispersed over several voting groups that also include third countries in the complicated structures of the Bretton Woods institutions. Since the early 1990s there have been increasing calls for a strengthening of the EU's external representation in international fora and for the Union "to speak more with a single voice".[32] This continuing fragmentation impairs the coherence and effectiveness of the EU's policies and undermines its commitment to multilateralism and global governance. As

[32] European Commission (2001), *European Governance: A White Paper*, COM(2001) 428 final, Brussels, 25 July 2001, p.27

Coeuré and Pisani-Ferry argue, "the current arrangements involve significant deficiencies that weaken the European position in international negotiations and thus involve welfare costs".[33]

Box 2: The EU and the UN

The EC channels a considerable and increasing portion of its aid through UN funds, programmes and agencies. However, it does so on the basis of non-membership, and consequently, voluntary contributions. The idea that EC contributions to the UN system should, in some way, be translated into visibility and, ultimately, impact runs like a thread through most relevant official EU documents. And there is consensus about the fact that neither the visibility nor the impact of the EU is sufficient. The representational issue points to a fundamental problem - the ill-defined role of the EC in EU-UN relations, and, more specifically, in EU Development Policy. There are two options:

(a) The EC, as an actor in its own right, the 28th donor of the EU, clearly visible in donor charts, annual reports and, through the European logo, on EC-funded vehicles, equipment and major supplies, becomes a full member, and it is helped by being a discernible actor whose financial contributions are translated into greater visibility amongst the broader public;

(b) In the absence of being a sovereign state, the EC focuses on less formal ways of exerting influence that fit the EU's specific nature. It adopts a 'front-runner' approach to the negotiation and implementation of UN initiatives and takes a more proactive approach to the development of international instruments and specific EU implementing actions. Visibility is primarily defined by the EU's capacity to ensure coherence and co-ordination and complementarity.

Source: European Parliament, Directorate-General for External Policies of the Union, Visibility and impact of EU activity in the UN and its various programmes, funds and agencies, February 2006

A combination of legal competences, institutional factors and the EU Member States' constellation of interests and collective identity (or lack of it) prevent the EU from having its voice heard. From a legal perspective, development cooperation is a shared competence between the EU and the Member States. Its governance model is a mix of supervised delegation to the EC and coordination. Externally, EU development cooperation is represented both by the EC and the Member States. In the World Bank, for example, European representatives (plus the EC as an observer) meet at least once a week to exchange information and to reach coordinated or joint statements that are prepared by the EU Presidency. At the biannual meetings of the Joint IMF/World Bank Development Committee, where the EC holds observer status, the Commissioner for Development submits a speech on behalf of the Community. However, the EC and the Member States may have different donor interests. In addition, several ministries may be responsible for World Bank matters at national level, and coordination may be difficult both between and within ministries. The creation of an EU-level committee for World Bank issues has therefore lacked consensus so far. Finally, the lack of a collective EU identity may also prevent a joint external representation. A shared belief would have to be constructed about the appropriateness of a single EU seat or EU membership.

The Lisbon Treaty provides the EU with a full-time president of the European Council and a *de facto* Foreign Minister (High Representative for Foreign Affairs and Security Policy),

[33] Coeuré, B. and Pisani-Ferry, J. (2003), 'One Market, One Voice? European Arrangements in International Economic Relations', Paper prepared for the conference on 'New Institutions for a New Europe', Vienna, 10-11 October 2003, p. 19.

assisted by a European External Action Service (EEAS). However, it has not put an end to this patchwork of international representation. The EU now has four important players dealing with external policy and representation – the President of the European Council, the rotating Presidency, the President of the European Commission and the High Representative. The question, however, remains as to how the High Representative's role will be balanced with the other Presidencies. A declaration to the Final Act of the Lisbon Treaty calls for the choice of the three positions (High Representative and the respective Presidents of the European Council and the Commission) to "respect the geographical and demographic diversity of the Union and its Member States"[34], which could give rise to the familiar jockeying between the Member States. This may, in turn, influence relations between the three positions.

Transparent and Accountable

The EC is not accountable in the way that bilateral donors are. On the one hand, this peculiar status insulates it from the direct political pressures experienced by bilateral programmes, reflected in practices such as tied aid. On the other, this potentially reduces scrutiny and responsiveness. Although not explicitly mentioned in the European Consensus on Development, the EC is accountable to a variety of stakeholders:

a. To the Council of Ministers and the European Parliament;
b. To the European tax payers;
c. To the legislative and executive powers in recipient countries; and
d. To citizens of the recipient countries.

Accountability at home

Institutional rigidity has been commonly used to describe the EC. Part of the problem, however, lies in its accountability framework determined by the treaties, the basic and financial regulations, which includes College collective responsibility, Member States comitology and European Parliament scrutiny. For example, the EC's multi-annual/strategic programming phase, including approval and barring the occurrence of any unforeseen events, takes 42 weeks. Although the time span is comparable with other donors, the EC has the longest approval period (20 weeks) in order to accommodate the comitology[35] and parliamentary scrutiny procedures. Furthermore, approval of programmes happens at the political level in the EC as opposed to the administrative or field levels. And finally, EU Delegations do not have the authority to modify financing agreements.

The general sense amongst the development community is that the EC needs to go beyond providing financial data by demonstrating results and value for money. The problem is that its prescriptive and complex management system tends to emphasise adherence to procedures rather than outputs. Furthermore, the excessive focus on fiduciary risk demanded by the European Parliament and the Member States could be seen to be at the expense of impact evaluation.

[34] Official Journal of the European Union (2007), 'Treaty of Lisbon amending the Treaty on European Union and the Treaty establishing the European Community', (2007/C 306/01), A. Declarations concerning provisions of the Treaties, para. 6.
[35] The committee system which oversees the delegated acts implemented by the EC.

Accountability abroad

The European Consensus on Development recognises the role of the EU in a "share(d) responsibility and accountability for their joint efforts in partnerships"[36] with developing countries whose ownership over development policies is to be respected and fostered. The EU's Cotonou Agreement is the most advanced form of partnership based on a contractual framework of political, trade and development cooperation with the 79 countries gathered under the umbrella of the African, Caribbean and Pacific (ACP) region. It includes mutual accountability provisions as well as joint institutions and arbitration procedures.

In 2006, the EC issued a Communication on Governance[37] reaffirming its commitment to basic principles set out in the European Consensus on Development. It asserted that governance should be a home-grown process as it cannot be imposed from the outside; that the EC and the Member States should work together to provide complementary and harmonised support to developing countries' governance efforts; and that responsibility lies both with donors and recipients to improve governance, emphasising the notion of mutual accountability. The EC also introduced an incentive-based approach to programming within EDF 10. When preparing new strategies with the ACP, the EC grants additional financial support – an incentive tranche – to encourage ambitious, credible measures and reforms in governance. Access to these incentives is based on the outcome of an enhanced dialogue between the EC and the recipient country, facilitated by governance profiles. Action plans are then put forward by the government of the recipient country. No mention has been made of any methodology for monitoring the implementation of the action plans or the precise way performance in implementation will affect the country allocations.

The main criticism of the governance incentive tranche is that it leaves little room for ownership. The profiles and the priorities are defined by the EC and the action plans are expected to fit the priority issues identified in the governance profiles. If the recipient government accepts the EC's priorities and promises the corresponding reforms, it receives access to a higher tranche. The fact that there is only a five to ten percent differentiation between the tranches, means that countries are not really motivated to expend time and effort. Furthermore, by submitting a governance action plan, the country automatically qualifies for a 10% tranche, whether the action plan is ambitious or not.

Adaptive

The financial crisis provides an interesting lens to look at the adaptiveness of the EU in response to changing global situations. Following the meeting of the G20 in April 2009, the EU came out with a support package for helping developing countries to cope with the crisis. In its Communication on 'Supporting developing countries in coping with the crisis', the EC

[36] See http://europa.eu/legislation_summaries/development/general_development_framework/r12544_en.htm

[37] European Commission (2006), "Governance in the European consensus on development: towards a harmonised approach within the European Union" *Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of Regions COM(2006)421*, Brussels, European Commission

proposed actions that would frontload €8.8 billion.[38] How this has affected the medium/long term predictability of funding remains to be seen. It set up two new finance mechanisms:

- The Vulnerability FLEX (V-FLEX): an ad hoc and rapid, counter-cyclical financing instrument to mitigate the social consequences of the economic downturn in the worst hit countries. It is limited to the ACP. The fund will dispense a maximum of €500 million in 2009 and 2010, and the money will be set aside from the reserves of the national and regional indicative programmes under the EDF 10. Given that the Member States decided against increasing the contribution ceilings, frontloading will be managed by shifting payment priorities for programmes in less vulnerable countries to the most vulnerable countries. Some have criticised the V-FLEX on the basis that donors need to allocate new resources to mitigate the effects of the financial crisis, rather than just bring forward available funds. The problem is that most of the funding (almost 99%) comes from pre-existing commitments. Furthermore, its responsiveness has also been questioned. The proposal was launched in April, the country application deadline was the end of July and the EC approved the package in December for a total of €215 million. However, when the Democratic Republic of Congo's reserves fell to two days worth of imports, the V-FLEX was not fast enough and the IMF came to the rescue.

- The Food Facility: an instrument providing grants of €1 billion in unused European farm subsidies to farmers in the 23 developing countries most impacted by the crisis over seeds, fertiliser and other agricultural projects. Following difficult negotiations between finance ministers of Member States, Members of the European Parliament and the EC, an agreement was finally reached on where the money would come from. Although the initial proposal recommended the use of €1 billion of surplus funds, only €760 million was agreed as additional funding. Furthermore, although the Food Facility was intended to be programmed over three years (2008-2010) by the end of 2009, over €800 million will have been disbursed. Criticism of the Food Facility has rested on the fact that the EC transferred the funds to other multilateral institutions to disburse instead of primarily using existing European bilateral modalities.

The 10th EDF regulation provides for Additional Voluntary Contributions (AVCs). However, these AVCs are very restrictive in terms of their use and focus. In the past, AVCs have been used to co-finance the Africa Peace Facility (around €40 million from Member States together with the €400 million from the 9th EDF). Generally, most Member States are reluctant to provide AVCs.

The new EU arrangements post-Lisbon

Vague mandates of the new top jobs, willingness of the Member States to allow the posts and people to represent Europe and turf wars have all come to the fore as the dust tries to settle on the new arrangements following the approval of the Lisbon Treaty. In all of this, it remains to

[38] EC Communication (2009), 'Supporting developing countries in coping with the crisis', COM(2009) 160/4, 8 April 2009, pp. 6 -12.

be seen how prominent development will be in the new set-up, and whether the EU's external relations structures will be simplified and development will have more leverage over other areas than before, so as to ensure real development effectiveness rather than just aid effectiveness.

How the new EEAS is designed and operates will carry direct implications for how effectively EU Member States and the EU as a whole are able to influence the world beyond their borders. Over the coming months, as EU policy-makers finalise the arrangements for the functioning of the EEAS, their choices will have an indirect but no less important effect on the EU's ability to live up to its potential as a constructive proactive and effective actor on the international stage. Even the largest EU Member States are no longer in a position on their own to shape international events or the world we all live in. Acting together in the EU they have shaped the international trade agenda. They have been much less successful in foreign policy for a combination of reasons, largely lack of will and poor arrangements.

The Lisbon Treaty is thin on detail about the EEAS: little more than that it is to assist the High Representative and be composed of officials from the EC, Council and the Member States. It is to be established by the Council on a proposal from the new High Representative in agreement with the EC and after consulting the European Parliament. Setting up the EEAS with so little guidance from the Treaty has been contentious. The EU institutions, the Member States and the European Parliament have been embroiled in a quarrel about control, accountability and budgetary responsibility.

From a development perspective, three points stand out:

(1) The High Representative will have a role to play in delivering coherent and joined-up policy to achieve the MDGs. The Development Commissioner will need to be given the space and authority to work with the EEAS to develop new ideas, team up in international diplomacy, and stop initiatives which do not conform to development principles. The College of Commissioners will be the guarantor of this arrangement. Although the High Representative is 'double-hatted', reporting directly to Member States, as well as being a member of the EC, it is the collegiality of the college that will be tested.

(2) As the EEAS will have significant responsibilities both in conducting political dialogue with developing countries and in allocation and programming of development funds, the EEAS will need expertise on development. Given that the EEAS will be bound by political and bureaucratic imperatives, it is unlikely to allow for staff recruitment based on technical expertise in development only, not least because of rotation requirements. Seconded national experts could fill this capacity gap to a certain extent, as has been the case in the EC and in the Council in the past.

(3) The development work of the EEAS will need to be accountable to the European Parliament's Development Committee. It might seem obvious that this should be the case, but the double-hatted nature of the High Representative's role leaves scope for some ambiguity.

It is likely that the creation of the EEAS will raise some significant problems with EU representation in multilateral institutions. For example, in the UN, the EU is represented by

the EC as an observer, with no right to vote and limited rights to speak. But preponderantly it is the Presidency, exercising its right as a nation-state that speaks for the EU. The Presidency is also responsible for internal coordination among the EU Member States, the preparation and negotiation with others of draft resolutions etc., and the delivery on behalf of the EU of statements, explanations of vote and so on. With the new arrangements, there will be a real problem over how the EU makes its voice heard formally in meetings. There are a series of options:

(1) Negotiation of a special status for the EU, giving it the rights of a state. But it would be very difficult or maybe impossible to achieve in view of the likely resistance of many other UN members, including many with their own collective observer observations, for instance, the African Union or the Arab Leagues.

(2) Seek to establish conventions rather than rules, for instance by exploiting openings such as the rules which have allowed the Development Commissioner to make a speech on behalf of the EU or the former High Representative Javier Solana to address the Security Council.

(3) The EU Member States invite the General Assembly to adopt a resolution that effectively gives the EU participation and speaking (but not voting) rights.

The future of the EU in global governance

The future role of the EU in global governance will depend on two sets of conditions, internal and external. Political developments in the EU will determine whether it has more or less assertive international presence. Internal factors include:

(a) The design of the EEAS, its role in development cooperation and the coherence and efficiency of the EU's institutional setting in Brussels and between Brussels and EU delegations in country;

(b) The relationships of governments and leaders in the EU capitals, and whether they can reach a common vision of EU development cooperation;

(c) Arrangements towards a more or less permanent 'division of labour' in development cooperation between Member States and the EU;

(d) The capabilities given to the EU institutions to carry out their tasks;

(e) A significant increase in the budget for EU external action and investments in strategic partnerships; and
(f) The size of the EU.

Along with internal factors, the EU's global role will also be defined by external factors:

(a) The degree to which it is able to cope with and mitigate the negative effects of the global financial crisis and other crises, man-made and natural catastrophes;

(b) The level of success it has in demonstrating that it is able to live up to its aid commitments in the run-up to and at the MDG Summit in September 2010;

(c) The level of unity and ambition it portrays in the continuing climate change negotiations, in particular in June 2010 in Bonn and in November 2010 in Mexico;

(d) Political developments and the foreign policy of the US and emerging powers, in particular China and India; and

(e) The situation in the EU's neighbourhood.

The future success of the EU will depend on its ability to meet the challenges of globalisation and of a world in which the weight of individual European countries has been declining steadily and will decline further as countries such as China, India and Brazil gain in economic and political weight. The only hope for European countries to maintain global influence is to act together in the EU.

Table 3: Assessment of EU good governance

	Effective	**Efficient**	**Legitimate & fair**	**Transparent and accountable**	**Adaptive**
EU	Strong policy statements based on values and principles, but not adopted by Member States at national level; Provides a forum for information sharing among Member States; Good coordination of studies and analytical work with some lesson learning; Slow progress in division of labour, aligning incentives, or promoting long-term development interests.	High transaction costs spread over 120 countries; Only 33% of missions coordinated; Budget support not widely used.	Legitimate, although not able to 'speak with one voice' in interna-tional fora.	Transparent and accountable to the Member States, the European Parliament and partner countries through 'mutual accountability' clauses in partnership agreement.	Attempts to adapt more quickly to changing needs but constrained by accountability and decision-making procedures.

5. Conclusion

Two paradoxes begin to emerge from the analysis.

First, good governance of the aid system obviously matters: it cuts transactions costs, reduces market failure and assures accountability. Multilateral channels offer a fast-track to good governance, especially when the channels in question are characterised by high levels of accountability to recipients, as is the case for the UN, to a significant degree for the EU (at least for ACP countries) and increasingly for the Bretton Woods Institutions. At least, the multilaterals out-perform the other governance mechanisms. Yet – and here is the first paradox – donors (and sometimes recipients) seem reluctant to follow the logic. In the case of the EU, only 20% or so of all oda is channelled through the EC. This is a classic case of prisoners' dilemma: every country is better off if the multilateral channels are strengthened, but they each have strong incentives to use bilateral channels themselves.

Indeed, donors have multiple objectives in distributing aid, related to foreign policy, commercial interests and domestic politics, as well as the purely humanitarian. Some also believe strongly in the value of a multiplicity of channels, to encourage innovation and provide a degree of contestability. In this case, they need the non-multilateral aspects of governance to perform more effectively than they do.

In this endeavour, the Development Assistance Committee of the OECD is the obvious market-leader, with a long history, an institutional depth, and a range of services which make it an indispensable tool for keeping score. It does, however, have restricted membership, as a rich-country club, it has been ineffective in driving substantial change, and it has a deficit in terms of accountability to recipient countries. This remains true, however many new donors, developing country governments and civil society representatives are invited to Paris. The UN-led process of the Development Cooperation Forum does not suffer from these handicaps. However, it is new and under-resourced, and should not replicate the technical functions of the DAC. No doubt, also, decision-making in the DAC is likely to be more efficient than that in the DCF, at least if general UN cultures prevail. This, then, is the second paradox, and one familiar in other aspects of development cooperation: the least ineffective organisation (in this case the DAC) can never be the most legitimate and accountable.

It is not surprising that all stakeholders are struggling with these paradoxes. The reform agenda is full whichever way one turns. Perhaps this is also a sign of good governance of the system as a whole. In an ideal world, a kind of race might be underway: whoever improves governance fastest wins the prize.

If the DCF manages to improve effectiveness quickly, well, it could take over the statistical and reporting functions of the DAC. Conversely, if the DAC's Working Party on Aid Effectiveness can rapidly demonstrate that it provides a mechanism by which developing countries can hold donors to account, then the DCF might lose its appeal.

In terms of funding, if the BWI governance reform can be completed, then the World Bank might win funds that would otherwise have gone to the EC. Or if the UN can improve its effectiveness, then it might see its funding increased.

Of course, it is fanciful to think that the players of the aid game will be quite so instrumental in their decision-making. Nevertheless, Ministers do make choices in multilateral space, and good governance is one of the criteria they will use. Institutions and agencies would be well-advised not to be left behind.

For the European Union, this last conclusion has particular resonance. There will be major changes to the governance of EU development cooperation in 2010, resulting from the ratification of the Lisbon Treaty and the consequent reorganisation of Commission and Council structures, including the creation of the EEAS. In 2010 also, negotiations will also begin for the new Financial Perspectives, to run from 2014 to 2020. Decisions will also be made about how to allocate fast start climate funding and eventually much larger financial flows for climate change mitigation and adaptation. If the EC is to retain and increase its share of global and European aid, then continued improvements specifically to governance will be required. Four priorities might be suggested.

First, the Cotonou Convention contains strong provisions for mutual accountability between developed and developing countries, especially as regards the administration of the European Development Fund. These will be at risk is the EDF is 'budgetised', that is taken into the framework of the Financial Perspectives. In any case, it applies only to aid supplied to countries of the ACP and not to other regions or to climate funding. It should be a condition of financial re-engineering that the partnership principles of Cotonou be preserved and generalised.

Second, the Code of Conduct on Division of Labour needs to be taken more seriously, both within countries and between countries. Greater transparency, especially of unit costs, would drive donors towards greater specialisation. New targets should be set for greater coherence in EU aid, for which the EU Council should agree to be accountable.

Third, the EC will want to continue finding was to respond quickly to emerging crises, as with Vulnerability Flex and the Food Facility.

Fourth, the EU as a whole can do better in working together in international fora, including the BWI, but also the UN, the G8, the G20 and the UNFCCC. A single seat is too ambitious for now, but further investment in better coordination ma eventually lead in that direction.

The EU should lead the way in greater transparency and accountability of aid, and for looking for ways to increase accountability to stakeholders in developing countries. Greater responsiveness to these stakeholders is the most important way, in the long run, of improving performance.

This list does not exhaust the EU aid reform agenda. For example, a greater focus on low income countries in EC aid would be desirable. However, improved governance would be a strong further asset as the EC shapes its future role.