Stockholm School of Economics

Department of Economics

Master's Thesis

CONTROLLING AID

- Information, Incentives and Monitoring Structures within Swedish Aid -

Abstract

The issue of control and regulation of development aid is continuously subject to debate and criticism, in Sweden as well as globally. Recent discoveries of irregularities and poor administration of projects funded by the Swedish International Development Cooperation Agency (Sida) and executed by local NGOs have added to the skepticism. This thesis examines Sida's relations with its sub-organizations through principal-agent theory in order to find a theoretical explanation for the problems. We examine information, incentives, and monitoring flows within Sida's organizational framework. Further, as an increasing part of Swedish aid is channeled through the European Union (EU), we use the example of the EU's aid organ EuropeAid and the relationship with its contracted NGOs, in order to draw some more general conclusions. We conclude that Sida's information and monitoring structure are not fully efficient, the incentive structure needs to be reinforced and perverse incentives need to be eliminated. We believe that a significant reason for some of the current issues is that Sida regards its relationships as partnerships rather than of principal-agent nature.

Key words: Principal-agent, information, incentives, monitoring, control, aid, Sida, civil society, NGOs

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1 INTRODUCTION

The general concept of aid is relatively deeply rooted in Swedish society, and public opinion is supportive of humanitarian aid and development support[1]. Recent opinion polls show that 95 percent of the Swedish population considers it important that Sweden contributes to the development of poor countries and 83 percent believe that Swedish aid directly contributes to a positive development in the world (Sida 2008c). The Swedish civil society and Non Governmental Organization (NGO) sector is unique. "Political parties, solidarity groups, church organizations, trade unions, etc., form an integral part of the shared social and political fabric…Swedes see these NGOs as ways to volunteer and to participate directly in helping those in poorer societies" (Ostrom et al 2002, p. 112).

The issues of control and regulation of aid are, however, continuously questioned, debated and criticized in Sweden as well as globally. Several cases of poor administration and corruption have been discovered and added to the public skepticism. The issue of how to increase efficiency in the use of funds is becoming crucial for the aid to maintain purpose, as well as legitimacy.

As Sweden annually contributes around one percent of its gross national income to foreign aid, how this extensive amount is being distributed is of considerable public interest. The Swedish International Development Cooperation Agency (Sida) distributes around 53 percent, SEK 15.4 billion in year 2006, of the total aid budget (Sida 2008b).

The report published by The National Audit Office (NAO) in 2007 (RiR 2007:20) brought attention to the problem of Sida's lack of control of foreign aid organizations. In the report NAO claims that in the case of aid to projects and NGOs, several of Sida's sub-organizations have provided inadequate reporting and lacked satisfactory auditing routines. The total grant channeled by Sida's department of NGO cooperation, SEKA, to these organizations exceeded SEK 1.3 billion in year 2008 (Sida 2008a).

1 Please note the difference between these two concepts. Humanitarian aid is defined as emergency aid to regions struck by crises such as natural disasters, wars etc. Development support consists of contributing opportunities and structures for improving living conditions in the long run. This study is concerned with development support.

When it comes to development aid the European Union is increasing in significance. Currently, Sweden contributes approximately SEK 1.5 billion to the development work of the European Commission (EC) each year (Regeringen 2008), but the long-term vision is that all the member state aid funds will be channeled through the EU (Carlsson and Malmström 2008).

The issue of aid control and administration has been the subject of several studies, amounting to a joint critique of these aspects of the projects. To our knowledge, however, no study has yet addressed the link between information flow, incentives, and monitoring on the basis of principal-agent theory. We believe this link to be essential not only to assess the extent to which the problems can be explained by theory, but more importantly to provide an explanation as to why these problems arise.

1.1 AIM

The aim of the thesis is to study Sida and the organizations it collaborates with an attempt to identify and understand the mechanisms that can cause anomalies. In order to determine whether our findings are exclusive to the Swedish aid process, or if one can draw more general conclusions, we look at similar aid projects conducted by EuropeAid for a point of reference.

2 METHOD

In this section we explain what motivated our choice of subject, the necessary delimitations, the chosen empirics, and the applied theories.

2.1 CHOICE OF SUBJECT

What initially awakened our interest for the subject of the control of distributed aid was the publication of the NAO's report: RiR 2007:20, "Irregularities within aid – is Sida's control of grant contribution through NGO's sufficient?" The investigation was in itself interesting, but for us it raised new questions concerning why control might not be sufficient and which underlying circumstantial factors were influencing the situation. We approach the subject through principal-agent theory to fully grasp the different aspects of the link between Sida and its sub-organizations. To our knowledge there are no previous studies that analyze the subject through principal-agent theory, and we wanted to give structure, shape, and logic to a seemingly amorphous problem.

2.2 DELIMITATIONS

The topic is studied from a qualitative viewpoint. We look at Sida's cooperation with civil society through Non-Governmental Organizations (NGOs), and not at any other forms of collaboration, such as state channeled or budget aid etc.

The focus on Sida's NGO cooperation makes for a natural delimitation, as this is one of the most controversial and considered one of the riskiest components of Sida's activities. The control measures taken in this area should therefore be representative for, or higher than, the entire organization. In the case of EC aid, we limit the example to EuropeAid's relations with NGOs.

One should bear in mind that this study does not in any way question the dedication, idealism, or competence of aid workers, but rather focuses on structures and systems in aid management.

2.3 CHOICE OF THEORETICAL FRAMEWORK

We aimed to find a theoretical framework that would suit our purpose to in a methodical and organized manner study Sida and the organizations it collaborates with in an attempt to identify and understand the mechanisms that potentially cause anomalies. Through the NAO's report, RiR 2007:20, we recognized that control issues had been highlighted and could potentially be studied through organizational theory. Having consulted various studies, for example Jarskog (2007), Petersson et al. (2003), and Henningsson (2007), in the field of aid, this has shown to be the most common theoretical approach. There also exists considerable work on institutional analysis of the topic by Ostrom et al. (2002). However, to get a broader understanding of the issues, we also aspired to address what might have caused the problems to arise, e.g. lack of contractual understanding or adequate incentives through the organisational levels. Through discussions with professionals within aid and financial theory, we decided to approach our study through principal-agent theory which satisfies our intent to investigate the sufficiency[2] of information, incentives and monitoring throughout Sida's organizational framework.

Although the organizational structure of Sida and its liaised sub-organizations is multilayered, we view it as several layers of simplified principal-agent relationships. As Sida bears the final responsibility for the performance of all its sub-organizations, Sida acts as the main principal and the underlying organizations act as agents. To understand the underlying mechanics of the relationship between Sida and its sub-organizations we use the principal-agent theory as formulated by Perloff (2002) and Laffont and Martimort (2002) as the basis of our analysis. We divide it into sections of information, incentives and monitoring. We have chosen this approach as these issues are interdependent and constitute the central flow between the parties. For the agent to be able to fulfill its duties it needs to have access to clearly stated and allocated information regarding goals and responsibilities. Incentives are central in principal-agent theory and in a larger perspective; "economics is to a large extent a matter of incentives" (Laffont and Martimort 2002, p. 1). Finally, due to the problem of asymmetric information, monitoring needs to exist as a complement to incentives.

[2] Adequate level to avoid irregularities

As incentives within aid organizations may differ from other organizations due to the relative irrelevance of financial incentives for the agents and the potential importance of non-monetary incentives, we include Ellingsen's and Johannesson's article "Paying respect" (2008) in our theory base, as it addresses potential non-monetary drivers such as social and moral incentives.

2.4 CHOICE OF EMPIRICS

As Sida bears the final responsibility for the legitimate and efficient distribution of funding, we have chosen to approach the issues in this thesis from Sida's point of view. We have therefore based our empirical selection on documents, reports and interviews concerning Sida.

Initially, we looked at previous studies relating to the efficient use of aid and corruption within aid, as well as at relationships in the structures of aid organizations. Furthermore, we received guidance from Sadev research fellow (and SSE PhD student) Anna Krohwinkel Karlsson and SADEV evaluator Fredrik Rakar, in order to ascertain a suitable approach. Reports from the NAO, external reports issued by Sida, and Sida's internal documents on rules, directions and guidelines have been central in the thesis. To access more up to date information we have continuously monitored the relevant content of Sida's webpage and other related sites.

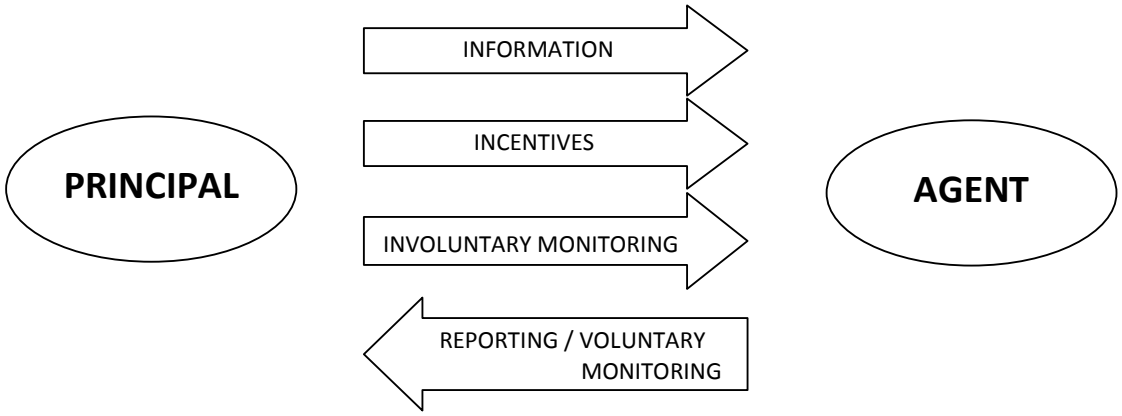
In order to get a clear understanding of how these issues are perceived by the concerned parties we interviewed five people with relevant positions and experiences. It was necessary to get complementary information from the NAO so we interviewed one of the authors who were involved in the production of the report, Johan von Eijsenberger. In addition, we interviewed two people at SEKA, the head of unit, Lena Ingelstam, and the handling officer for frame organizations, Carl-Johan Smedeby. To get a more profound understanding of Sida and its evaluation activities we had continuous contact with a former head of aid evaluation at Sida, Elisabeth Lewin. We also conducted an interview with the handling officer of democracy and civil society at the Ministry of Foreign Affairs, Tomas Brundin. When possible and appropriate, we recorded the interviews and transcribed them in Swedish, which were then translated into English. In other cases, we kept detailed notes from the interviews which were also translated into English.

The aid distributed by the EU member states is becoming increasingly coordinated and harmonized and the long-term vision is that all the member state aid funds be channeled through the EU (Carlsson and Malmström 2008). In order to see whether our findings are exclusive to the Swedish aid process, or if one can draw some general conclusions in a broader context, we briefly look at similar aid projects conducted by EuropeAid.

3 THEORETICAL FRAMEWORK

This section introduces the principal-agent problem and then develops the theory in accordance with the individual sections: information, incentives and monitoring. The section is primarily based on Perloff (2002) and Laffont and Martimort (2002). In sub-sections 3.1, 3.2, and 3.3 we further develop the theories on information structure, incentive structure, and monitoring structure.

Figure 1 **- The Principal-agent Relationship**



Note: Figure 1 shows the general flow between the principal and the agent. The principal provides information, incentives and involuntary monitoring, for instance by random samples. The agent in turn provides the principal with information through voluntary reporting.

The principal-agent problem stems from the existence of imperfect information. A principal contracts an agent to perform a certain task on behalf of, and with resources provided by, the principal. The fulfillment of the principal's goal (reducing poverty, disease etc.) is dependent on the asset that the principal is providing (aid funding), the agent's actions (projects) and factors beyond the control of the principal or the agent (e.g. unfortunate circumstances). If the principal and the agent have divergent interests, the principal cannot observe the agents actions but only their result, and if the agent does not bear the full consequence if its actions, the agent may behave opportunistically. This moral hazard will reduce the joint profit or alternatively complicate the fulfillment of goals. In order for the agents to act according to the principal's objectives, they need proper

motivation. There are several ways to achieve motivation among agents; one is the use of contracts that make the agent responsible for the project.

Efficient contracts between principal and agent lead to efficient task fulfillment, eliminating moral hazard and maximizing joint profit, but they require complete information, something that is only theoretically possible. Nevertheless, this reasoning does have practical implications as it identifies a need for an efficient information flow between principal and agent.

In strict agency theory, the agent will perform optimally if he or she retains the marginal profit. This is generally not the case due to the existence of asymmetric information and thus the principal needs to monitor the agent to avoid shirking or corruption. Monitoring can be performed either continuously or through random samples during the contract period. As monitoring is a quite expensive activity, random samples can with advantage be used as it minimizes the cost of monitoring whilst maintaining the threat of monitoring at any given time. The principal can also choose to control actions and results after the task is performed, which may be efficient if punishment can be inflicted at the conclusion of the project (e.g. withholding or lowering funds etc). The agent may also choose to signal efficiency through creating verification backed financial and action reports.

3.1 INFORMATION STRUCTURE

For the agent to be able to fulfill its duties, the goals and responsibilities regarding these duties have to be clearly stated and allocated. Further, the relevant information needs to be given to, and properly absorbed by, the agent. Information absorption entails that the agent has read and understood the information. To ensure information absorption in a complicated organizational structure with many hierarchical levels, it is particularly important that clear rules for information flows are established. There should also be a control system to ensure that the information is absorbed. In itself, this system creates the possibility to understand, integrate, and adhere to the information given.

3.2 INCENTIVE STRUCTURE

Ostrom et al (2002) define an incentive as a motivation for a course of action. There are many different ways as to motivate action, and these can be classified into three categories: financial, moral, and coercive incentives. Either the motivation lies within remuneration (achieving a goal), moral convictions *(*praise or shame), or in negative incentives (e.g. threat of physical force). In the non-profit, civil society sector motivation tends to stem from moral convictions, as financial incentives are not completely explanatory and coercive incentives are not applicable. Incentives are either positive or negative. Positive incentives are incentives stemming from some kind of reward or compensation; negative incentives arise in order to avoid reprimands.

Ideally, in a well-structured and competitive market with private goods, positive financial incentives lead parties to take actions that benefit both themselves and others. Without these as the driving forces, a market or organization has to emphasize the promotion of other positive and negative incentives.

According to Ellingsen and Johansson (2007), incentives are not only achieved by monetary rewards. In fact studies show that employees value respect and esteem to a large extent. "Many of these observations can be captured in a standard principal-agent model, once the principals and the agents are assumed to care about respect or esteem as well as money" (Ellingsen and Johannesson, 2007, p. 136). Respect and esteem go hand in hand with trust, and trust has also been shown to have a positive effect on performance. Results achieved by Stogdill and Coons (1957) suggest that "supervisor trust, friendship and respect were associated with better performance" (Ellingsen and Johannesson, 2007, p.140). According to Nagin, Rebitzer, Sanders, and Taylor (2002), one cannot on the basis of agency theory assume that the trust built up between the principal and agent necessarily induces trustworthiness, as trust is not always rewarded. "Some researchers report that a reduction in monitoring induces some workers to shirk more, and that it increases average shirking" (Ellingsen and Johannesson, 2007, p. 140). Thus, trust should be expected to entail abuse to some extent. To be able to rely on trust as a successful strategy, one needs to make sure that the benefits are not outweighed by the costs (Ellingsen and Johannessen, 2007, p. 140).

The incentives for aid workers differ from the incentives for non-aid workers. This is partially due to the substantial difference in monetary rewards but mainly a consequence of conviction. Aid workers tend to be idealists "and part of the value […] is the satisfaction of an idealistic image, both in their own minds and in the eyes of others. Presumably, one of the reasons for nonprofit incorporation is to send a clear signal that principals are willing to forgo economic surpluses" (Ellingsen and Johannessen 2007, p. 142).

The effects of introduced incentives are generally subject to imperfect information and may cause problems. Incentive problems mainly include the existence of perverse incentives, i.e. incentives with unintended and negative consequences that may lead parties to act in ways that are unhelpful or even damaging to themselves and others.

3.3 MONITORING STRUCTURE

Due to the problem of asymmetric information, monitoring needs to exist as a complement to incentives. The purpose of monitoring is not only to secure goal fulfillment but also to ensure that the means have been used in an appropriate and value maximizing manner.

Monitoring should be performed either by the principal or by an independent third party contracted by the principal. There must not exist any dependency relationships between the monitor and the agent. If the monitor is dependent on the agent for future work etc., this tends to generate perverse incentives for the monitor.

There are several methods of monitoring. Voluntary monitoring entails continuous or final performance reports provided by the agent to the principal. Involuntary monitoring can, for example, include the use of time reports or unannounced controls. Involuntary monitoring can be applied during the course of the project, acting as a negative incentive for the agent. Another form of involuntary monitoring is the control of results after the completion of the project. This is, however, dependent upon the possibility of retrospective punishment, for example withholding remuneration or demanding reimbursement of funds.

As monitoring is generally a quite expensive activity, the principal should try to optimize incentives to keep monitoring costs at a minimum. The importance of keeping monitoring at a reasonable level is further enhanced by the fact that excessive monitoring can eliminate

the positive effects of trust on the agent's incentives to perform well, as it signals that the principal does not in effect trust the agent.

4 EMPIRICS

In this section, we present our findings originating from literature, articles, relevant websites and interviews in order to address the questions at issue. In sub-section 4.1 we use a figure to clarify the organizational structure of Sida and its collaboration partners. In 4.2, 4.3, and 4.4 we account for our empirical findings in terms of information structure, incentive structure, and monitoring structure. We initiate each section with a question, based on the theory. Section 4.5 presents our empirical findings in the case of EuropeAid.

4.1 ORGANISATIONAL STRUCTURE

To facilitate the understanding of the empirics section, we commence by outlining the organizational structure to show how information, incentives and monitoring flows from Sida to the local projects and back.

Figure 2 **– Information, Incentive and Monitoring flows**



Note: At present, the flows within Sida's organizational structure are somewhat complex due to the quantity of organizational levels that needs to be passed through.

4.2 INFORMATION STRUCTURE

The information structure can be broken down into four components; the standardized directions on information and responsibility allocation, information distribution, information absorption, and finally control of information absorption.

4.2.1 Sida's Information and Responsibility Allocation Guidelines

Are responsibilities regarding information forwarding and control clearly stated and allocated in the contracts?

Sida has formulated standardized directions on information and responsibility allocation, "Guidelines for Grants from the Appropriation for NGOs" (2007), with the aim of facilitating transparency and ensuring that set rules are known throughout the organizational structure in order for them to be followed.

The role of Sida is to ensure the quality of the frame organizations' capacities and activities, as well as facilitating common learning. Sida essentially has three roles in their interaction with the frame organizations. Primarily, Sida should act as an analyst in order to assess and understand the mechanics that promotes the development of civil society and how it can best be supported. Secondly, Sida should act as a dialogue partner for the frame organizations and their partners, to share experiences with civil society, and to bring together organizations with similar goals and work procedures for different forms of collaboration. Thirdly, Sida should act as a financier through assessing the capacity and system of the frame organizations, in addition to preparing and following up on the aid contributed to the frame organizations' activities. Furthermore, it is Sida's responsibility to verify that the grant channeled through SEKA is used as efficiently as possible to promote the development of civil society. This should be verified through grant contracts and the design of policy, direction and other guidelines. Sida should also ensure that SEKA supplies sufficient reporting of results to the government and the public as well as the frame organizations and their partners.

Sida's collaboration with the frame organizations is based on lasting relationships. A contract with a frame organization generally covers a period of eight to ten years, and Sida-contributed financing contracts are generally entered for a period of three years.

The frame organizations are responsible for ensuring that funds are used according to Sida's directions and conditions. Frame organizations are formally required to plan, evaluate, report and analyze the organization's results in a way that enables Sida to assess its quality and use it in cross organizational learning. The frame organizations also take part in a broader dialogue about the development work, in Sweden as well as in the collaboration countries.

Frame organizations that mediate grants have further roles and responsibilities. They must first secure quality through ensuring that applying organizations and their action proposals comply with Sida's regulations and guidelines. This is then to be presented to Sida. Second, they should also take on a consultancy role, ensuring that the applying organizations are supplied with sufficient information about important policies, principles, and rules within the NGO-grant. Third, they should support applying organizations in their capacity and competence development. Finally, they should function as a communication link between Sida and applying organizations. They are responsible for the applying organization having access to essential information from Sida, as well as Sida having access to the applying organization's development and activity.

The NGOs have a responsibility towards the frame organizations to ensure that the grant given by Sida is used in accordance with Sida's rules and regulations. Similar for all subordinate organizations; NGOs, international organizations and local organizations, they should plan, execute, follow up, report, and analyze the results of their activities in a way that enables the organizations one level superior to them to control the activities, as well as forward this information to Sida.

Smedeby (2008) considers a well functioning delegation of responsibility as an important part of the efficiency of the aid organizational chain. In case of irregularities or other problems, Sida is held responsible for follow up, to minimize damage and for prevention.

"After all, the responsibility to ensure that the sub-organizations have adequate control systems is Sida's. For example, the NAOs report highlighted that there is some disorder, implying that the systems are inadequate" (Smedeby 2008).

Previous studies have highlighted some problematic issues within the responsibility allocation, especially regarding the communication of desired goals and results. Information sent to Sida from sub-organizations often includes unnecessary information, adding administrational costs to the sub-organization as well as the reviewer, and resulting in an inefficient communication process. The recommendations from these studies include clarification of: Sida and its sub-organization roles; required information; and finally non-required information (Winai 2004).

4.2.2 Information Distribution

Are Sida's demands and relevant information forwarded through all organizations down to the local projects?

Ingelstam (2008) states that regarding aid to NGOs, the chain of organizations is especially long due to the additional level of grant distributing frame organizations. She affirms that it is clear that the signaling strength of rules and policies is weaker in such a chain because of the special aid form, which has been shown in the projects studied by the National Audit Office, (2007), Eriksson and Ehrenberg (2008) and further confirmed by Eijsenberger (2008). Sida is currently attempting to locate the weak link in the chain, since "the process is evidently dysfunctional" (Ingelstam 2008). Having located the weak link, Sida can focus on the specific area and attempt to strengthen communication. She adds that one also has to remember that there is a lack of capacity that needs to be seen to. Sida needs to identify what is needed in order to supply more development capacity and communication. She finds this very important and encourages SEKA personnel to actively look for signs to solve the problem during control trips. One of the aims of the field trips is to see whether directions, conditions, and rules are communicated, understood, accepted, and finally if they are used. However, control might stop earlier in the organizational chain if information is not passed on efficiently. According to Smedeby (2008), information is generally forwarded through paper copies and sometimes through directions to web pages.

Ingelstam's (2008) personal experience is that the lack of information in the local organizations is not due to ignorance, but because the information has not been provided to them.

4.2.3 Information Absorption

Is the information being absorbed by concerned employees in all organizations down to the local projects?

At SEKA there is an awareness of the risk that documents are put away and rarely consulted, and that there is nothing guaranteeing that the employees have actually understood and used the rules and regulations. Smedeby (2008) expresses that it is important for Sida to be certain that the frame organizations, but also the underlying organizations, follow the regulations and contracts. Furthermore, organizations need to implement systems to ensure that the underlying organizations follow the regulations as well.

4.2.4 Control of Information Absorption

Does Sida in any way control whether the information has been absorbed by the concerned employees?

According to Ingelstam (2008), information absorption is verified partly through field studies but also through contract audit, and evaluations. One of these is the Compliance Audit (2008), which is used to ensure that organizations throughout the chain of distribution act in accordance with the contracts and general conditions at all organizational levels. This is an essential tool to locate the weakness in the chain. There are no competency-tests to ensure that the information has been absorbed.

During Sida's visits to local projects, the absorption of information is not thoroughly tested, but questions are asked regarding the countries' laws and regulations and how the project faces suspicion of irregularities. Moreover, frame organizations seldom thoroughly test the absorption of Sida regulations. This is due to the fact that many organizations have their own regulations, which they see as equally appropriate. Some rules from Sida are very distinct, e.g. that money should be kept in one bank account (Smedeby 2008) but others may vary to a higher degree, subject to varying interpretations.

4.3 INCENTIVE STRUCTURE

In this section we look at the incentive structures throughout Sida and its collaboration partners. We identify the positive, negative, and perverse incentives.

4.3.1 Positive Incentives

Are there sufficient positive incentives through all organizational levels down to the local projects to support goal fulfillment?

According to Smedeby (2008) Sida's control trips rarely lead to a discovery of corruption, but they are imperative tools to show interest in the projects and encourage the work. The purpose of the trips is mainly to show interest for what is being accomplished with the aid funds provided by Sida. Generally, the aid workers are very interested in their work and they tend to be eager to show what they are doing whilst also showing a sense of pride for the project. "The main incentives that apply to the aid workers are identification with the work, pride, long term view, solidarity and social capital" (Brundin 2008), something that is emphasized by Ingelstam (2008), who states that the role of self-contribution encourages engagement.

The visits are viewed as more of a mutual exchange and an opportunity to get to know the organizations better and Smedeby (2008) suggests that they get an estimation of the people working with the project and can assess if they are trustworthy as "the aid business is to a large extent based on confidence in people".

Sida attempts to educate the organizations about why they are interested in them, and their visits tend to be appreciated. The trips act as a positive incentive for the organizations to behave well and help strike a balance between encouragement and control which is important for the cooperation to function.

4.3.2 Negative Incentives

Are there sufficient negative incentives through all organizational levels down to the local projects to prevent wrong doings?

The strongest negative incentives are the threats of cessation of funding and/or repayment of funds. According to Brundin (2008), a deviation from Sida's policies may well force a reimbursement of the grant. If reports are not handed in, this threat can be realized. Sida has repeatedly overlooked such situations in the past, but at SEKA they believe that it is nowadays clear in most organizations that no report implies no further funding. In the event of more serious issues, Sida aborts the collaborations. When encountering illegalities such as corruption or financial irregularities, the police are contacted. In the case of minor issues, the responsible are reprimanded and reported.

The investigations also serve as an incentive, as the workers are subjected to the constant threat of being investigated at some point. Smedeby believes that it is better to have random sample controls and not exaggerate costly controls which would "lead to there being less money left over to the project - in which case you would have nothing to control" (Smedeby 2008).

4.3.3 Perverse Incentives

Are there any perverse incentives through the organizational levels that affect goal fulfillment?

"The incentives are stronger for distributing the funds than for controlling the use of them" (Eijsenberger 2008). Eijsenberger (2008) finds that the control issue is impeded by the one percent goal and that project funding should be more based on results than they are now and Sida should suggest a number of projects for which it gets funding. Today the process is the reverse. Lump-sum contributions to all projects lower the incentives to accurately manage the projects individually.

The reference frequently made to the importance of having established relationships with the frame organizations in order to create trust and a durable cooperation, is disputed by the NAO. In the end it becomes an issue of "quality vs. trust" (Eijsenberger 2008). Eijsenberger (2008) stresses that aid distribution should be unaffected by previous relationships to avoid perverse incentives, but agrees with the statement that this adds an element of catch 22. He emphasizes the importance of testing random samples in order to increase control and transparency, and adds that it is being developed within Sida.

The key is to analyze risks, not ignore and conceal them. “There needs to be substantial risk evaluation. Should we give aid to organizations in Somalia? It is reasonable to assume certain shortcomings in aid administration in Somalia. If the project lacks administrative resources to accurately carry out the project, we need to calculate what percentage reaches the recipients and simply decide whether or not this is an acceptable amount” (Eijsenberger 2008).

4.4 MONITORING STRUCTURE

When examining the monitoring structure we focus on three aspects; monitoring sufficiency, competency of monitors, and resource sufficiency.

4.4.1 Monitoring Sufficiency

Is monitoring sufficient through all organizational levels down to the local projects?

”Sida does not monitor the framework organizations – it has neither the capacity nor the mandate to do so” (Ostrom et al. 2002, p. 114).

In 2007 the NAO carried out a revision of fifteen projects in four countries, finding auditing errors in ten of them, irregularities in seven (RiR 2007:20). The report states that Sida is aware that corruption and other irregularities are present and that Sida has tried to organize a protection through contracts and other control measures. These measures have, however, proven to be inadequate. Within the Swedish organizations there is a lack of awareness of the risks of irregularities, which has made the measures of protection inadequate (RiR 2007:20, p.7). Eijsenberger (2008) states that the organizations chosen for examination by the NAO were admittedly riskier than the average projects funded by Sida. He adds, however, that this should only have resulted in more thorough controls by Sida that did, in fact, approve them.

The NAO states that the attempted control system has not uncovered the irregularities and Sida has remained unaware of the shortcomings and problems that exist. Further, Sida has trusted the insufficient audit certificates that have been issued by local auditors. The audit certificate from the Swedish auditor should constitute a last filter of quality control before

the Swedish organizations get their project reports approved. The Swedish auditor has, however, in none of the investigated cases required additional verifications, or even been in contact with the local auditor. The report shows that all the audit certificates have been without remarks, indicating that the financials and the reports of results have been without any essential errors (RiR 2007:20, p. 8).

According to Sida's agreement, the auditors should not only comply with existing audit regulations, but also with Sida's own audit instructions. According to the NAO the latter are written in a manner that can be interpreted as limiting the auditor's work to merely reviewing documents. This has created an inadequate routine for auditing and Sida is thereby considered to contribute to the non-fulfillment of its purpose. The review indicates that several of the errors are critical. The discovered shortcomings relevant to this study are mainly that: essential parts of the financial verifications are missing. In some cases there is no proof that actual project activity has been carried out. Further, false documents such as presence lists and receipts, have occurred in a third of the reviewed projects. Eijsenberger (2008) says that the projects are to a large extent relying on cash payments. For example, as an incentive the local population is often remunerated financially for attending meetings held by the project. The main issue here is the poor record keeping of who has been remunerated. This leads to questioning their very existence. One reason for poor control of projects in Africa for example, could be derived from the lack of proper institutions. Proper financial control is not feasible without the establishment of proper institutions for accounting standards and regulations. Taking the extensive lack of proper institutions into consideration, a suggested solution is for the participants to leave phone number or e-mail address, both increasingly present in developing countries of today. This would increase the extent to which control is possible and decrease the risk of fraud. There are in addition several occurrences of unjustified costs, such as high salaries, large overhead costs and unmotivated consulting costs (RiR 2007:20, p.8).

The report has been met with skepticism as well as criticism by concerned parties. Brundin (2008) questions the representativeness and degree of seriousness of the report given as it was, in his opinion, conducted in a generalizing manner and gained disproportional media

exposure in relation to what was revealed ("negative news give bigger headlines than positive news" (Brundin 2008)).

In the Compliance Audit carried out by request of Sida and published in November 2007 (Jarskog et al. 2007) five frame organizations were examined on their observance and adherence to contracts. According to the report, Forum Syd is the only one of the reviewed organizations that is considered to adequately supply the Swedish NGOs with Sida's general terms. It is also the organization with the best-established control systems, something that is especially necessary given the scope and diversity of Forum Syd's NGO partners. The organization most often performs controls of the financial statements and economic reports of the Swedish NGO's, but shows certain shortcomings in its routines. It does not at all, however, control the accuracy of the local NGO's reports. The auditing instructions demands that the organizations revise the audits of the local NGO's, but according to the compliance audit this is not done. Forum Syd's auditor does not, however, find these flaws crucial enough to cause remarks in the audit certificate. Since the reports do not contain information on the local NGO's, the compliance audit concludes that they do not comply with Sida's auditing instructions. The main flaw in the organization is the lack of control of whether contract terms are followed on the subsequent levels (Jarskog et al. 2007).

Conversely, according to Smedeby (2008), Sida regularly evaluates the frame organizations. It is done partly through a frame evaluation and a capacity evaluation. Given that these evaluations have historically not been common, it was easy to achieve frame organization status. Since the frame system is quite rigid, many organizations have maintained the title. This changed, however, after the evaluations. Now Sida looks more at how the frame organizations secure quality in underlying organizations.

Sida's project administrators look at the funds that have been channeled to a local organization, which in turn has to demonstrate how the funds have been used. An evaluation is then performed to ascertain that the activities are reasonable in relation to the grant. The auditors and accountants will continue if more controls are needed. Smedeby (2008) does not think that a large part of irregularities or corruption is discovered through random sample controls. Usually it is not during Sida's trips, or through auditing, that

corruption is discovered, but through tips from people close to the project, i.e. whistle-blowers. In the vast majority of cases, it is the whistle-blower who reacts to something that is questionable or in another way not in the interest of the project, and report the liable. Smedeby (2008) disagrees that is always pride that motivates the whistle-blowers; it can also be jealousy or personal gain. Thus, Sida has to be careful with these accusations and investigate matters further before reprimands are issued. He adds that it can be difficult to encourage whistle-blowers, as this tends to be harmful to their status.

Brundin (2008) agrees with Smedeby in that whistle-blowers are of greater importance than the audit. He is of the opinion that Sida has good financial control systems, especially in comparison with the United Nations in terms of quantity of discovered corruption cases. He believes the auditors should clarify the organizations' financial situations to Sida, but that there needs to be a balance between cost efficiency and control. Prioritized geographical areas need to be viewed in a more long-term perspective according to Brundin (2008). Previous studies, such as Winai (2004), have highlighted the need for more detailed information regarding control and learning procedures. Development is dependent on experience and contacts from independent organizations, as "the focus is on results - not on financial clarity" (Lewin 2008).

4.4.2 Competency of Monitors

Do monitors have adequate competency to control the work of the agents?

According to Eijsenberger (2008) the weak links in the control process are the absolute reliance on the local auditing and the absence of substance reviews, two issues that are contradictory to good auditing practices. Irregularities have on several occasions been discovered without reactions or reprimands on behalf of Sida. Sida's focus needs to be shifted towards the proper and efficient distribution of funds.

The local auditor is required to produce a narrative financial report and an audit report, but according to the NAO (RiR 2007:20) the bookkeepers in the projects have shown a lack of knowledge about financial accounts and relevant rules applying in the countries. Ingelstam (2008) claims that in development countries it is normally quite expensive to procure an

auditor from one of the top branded audit firms, and many of the local projects therefore choose to hire a cheaper or more easily available, perhaps less qualified, alternative.

It is the local auditor who has the final responsibility of the financial control of the projects and it is up to the Swedish organizations to control the suitability of the local auditor through checking contracts and performing other appropriate due diligence measures. Sida has no proactive routines to ensure auditor competency and the Sida personnel employed with the embassy in the respective countries are not involved in the projects. Sida only controls the auditor's aptitude in special circumstances, when there already is suspicion of corruption. Smedeby (2008) agrees on these report findings and believes that this may be due to the fact that it is difficult to find auditors with adequate competence in some areas (e.g. where education is expensive). Finding a good auditor may be expensive and some projects may try to avoid these costs through settling for someone with easier access but who is ultimately perhaps less appropriate or qualified. Fortunately, as expressed by Smedeby, projects with budgets below the limit of SEK 200.000 do not need an auditor. Controlling all minor projects would be too expensive.

When asked about his view of the Swedish auditors and their alleged lack of contact with the local auditors, Smedeby (2008) says that he does not consider that to be part of their responsibility. The Swedish auditors should control the Swedish organization and make sure that their bookkeeping is correct and not assess the work of the local auditor. It is the responsibility of the Swedish organization to make sure that the local auditor is competent. Adding that he is not an expert within the auditing principles of Sida and that responsibility lies principally on the auditors, he finds it strange that the responsibility of controlling all sublevels of organizations should fall on the Swedish auditor alone.

4.4.3 Resource Sufficiency

Are there sufficient resources to ensure that means are used in an appropriate and value maximizing manner and to secure voluntary monitoring (reporting)?

Frame organizations are entitled to an eight percent administrative grant of the project budget to use for general administration, which is in part directly transferred to the Swedish organizations (Smedeby 2008). The amount that the Swedish organizations then decide to

transfer to the local organizations may vary greatly. Some Swedish organizations keep the funding for administration in Sweden. The line between administration and organizational activities becomes blurrier the further down the organizational chain you get. The regulations are quite clear, but there are some directions that allow for interpretation. Smedeby (2008) believes there is a possibility that some organizations may misuse this administration contribution given that there are many organizations and projects where financial documents are not in order.

Ingelstam (2008) adds that it is difficult to follow the grant through the organizational chain. She further claims that most organizations have enough working capacity and are doing well. The smaller organizations are not necessarily worse, but they usually have fewer administrative resources. This refers not only to the local organizations, but also to some Swedish organizations that have fewer resources and therefore have a harder time living up to existing general rules and administrative demands. She states that it is also difficult to get a good overview because of the size and complexity of the organizational structure.

The Swedish organizations hire the Swedish auditors. Sida does not make random sample testing of projects, but if there is a suspicion of irregularities, auditing firms are consulted. Eijsenberger (2008) believes that the element of a constant likelihood of testing would reduce the risk of perverse incentives.

Eijsenberger (2008) states that the handling officers tend to be very ambitious and active in the beginning of the project, but at the end the incentives for appropriate report writing have decreased significantly. This is confirmed by Lewin (2008) who is of the opinion that more evaluation documents are necessary, but that the incentives for producing them after finalizing a project are weak. She stresses the importance of reputation and creating confidence in the frame organizations, and finds financial control less relevant. If the project performs poorly or fails to comply with the demands, Sida has the options of cutting the funds or suggest improvements. The administration of the frame organizations is evaluated on a regular basis but it is normally not the case for the local organizations as there are difficulties with equipment and administrative personnel.

4.5 THE CASE OF EUROPEAID

When it comes to development aid, the European Union is increasing in significance and scope. The total amount of funding channeled by the European Commission (EC) equals approximately SEK 70 billion annually to different development projects around the world. SEK 6.5 billion is channeled through NGOs (CONCORD Sverige 2007). Sweden contributes with approximately SEK 1.5 billion (Regeringen 2008). These numbers are expected to increase as the aid from the EU member states is becoming increasingly coordinated.

The aid is mainly administered by EuropeAid, the "Directorate-General of the European Commission that is responsible for implementing external aid programs and projects across the world" (EC 2008a). EuropeAid is also responsible for the entire aid process, for a proper and transparent conduct of management as well as tendering and contracting. In short, EuropeAid is the international development agency of the European Union.

The EC collaboration with NGOs is primarily based on the B7-6000 budget line, i.e. the main EU instrument for NGO co-financing, and the "Evaluation of co-financing operations with European non-governmental development organizations (NGOs), Budget line B7-6000" (EC 2000a). According to the evaluation "most projects were relevant in the sense of clearly identifiable needs […] delivered acceptable outputs in relation to stated objectives, and in most cases there was a satisfactory relation between costs and outputs" (EC 2000a, p. 1).

In the latest evaluation, (conducted in year 2000) the main criticism of the budget line was the lack of clearly stated goals and strategies: "The evaluators recommend a fundamental re-think of the nature and objectives of the budget line. It should be considered as a strategic fund and not merely an open and unfocused source of funds" (EC 2000b, p. 2).

Further, the budget line was criticized for its lacking monitoring and evaluation functions. There was a contradiction between its objectives and its reporting systems, as the latter exclusively focused on quantitative measures such as immediate results and sound financials. "This was confirmed by EC staff who clearly articulated their frustration at not being able to conduct on-site verification, to follow up more closely developments in the field and focus on the broader purposes of B7-6000" (EC 2000a, p. 55). The focus was on so-called ex-ante

screening, not only leading to lengthy approval times for projects but also causing any problems or failures to go unnoticed by the EC.

Furthermore, the recommendations in the evaluation covered the issue of decentralization and recommended that the Commission staff work directly with the local organizations, partially because this was concluded as more efficient with the specific projects, but also as a means to strengthen local civil society in general.

Following the recommendations of the evaluation, EuropeAid has since 2004 narrowed down the number of targeted countries and worked more closely with the local organizations. Instead of spread out, the resources were concentrated to a smaller number of projects that received greater consideration. "…since then its management has been 'de-concentrated' to the respective EC Delegations, with very encouraging results" (EC 2008b). According to the current policy of the EC there are considerable advantages in de-centralizing the activities and working closer with partners and recipients, when it comes to adapting the programs to the circumstances and needs of different countries as well as EC control. Finally, the auditors can now be contracted directly by the EC, allowing for a greater level of control.

5 ANALYSIS

In this section we apply the principal-agency framework on the empirical data. We look at information, incentives, monitoring, and the case of EuropeAid separately and use the same structure as in section 4, basing the analysis on our questions.

5.1 INFORMATION STRUCTURE

In Sida's document "Directions for aid from the grant position of Non Government Organizations" (2007), it is stated which organization has responsibility for planning, follow up, reporting and analysis of results and to whom this should be forwarded. However, the responsibilities are very generically described and can easily be misinterpreted. A more detailed explanation of what is demanded by Sida from the sub organizations is not stated in the document. One can therefore conclude that even though an attempt to state the allocation of responsibilities have been done, these guidelines are too vague for the agent to understand his/her task in full.

As a result of the responsibility allocation not being sufficiently clearly stated, the sub organizations may not be aware of what information needs to be forwarded, when and to whom. Ingelstam (2008) and Eijsenberger (2008), as well as results from the reports from the NAO (2007) and Eriksson and Ehrenberg (2008), jointly conclude that the signaling strength of rules and policies gets weaker the further down in the organizational chain you get. Ingelstam (2008) is aware that the process is dysfunctional and that where lack of information absorption has been discovered it has largely been due to errors in the distribution process rather than inability of the employees. The fact that information is generally distributed in paper form obliges every sub organization to print and distribute information packs to each of the local projects, which does not seem to be the general case.

We may conclude from the empirics that there is a potential risk that information is not absorbed by concerned employees in all organizations down to the local projects. The focus of the aid workers seem to be on distributing aid rather than necessarily doing it exactly "by the book".

Ingelstam (2008) concludes that, in theory, Sida has a system to control that information has been absorbed by the aid workers through the so called Compliance Audit (2008), which aims to ensure general contract compliance throughout the organizational structure. The field trips are highlighted by Ingelstam (2008) and Smedeby (2008) as opportunities to test competency within the projects, but there is no official agenda to do so. Ingelstam (2008) concedes that there are no official competency tests and that only a general competency level is checked, something that does not seem to be streamlined throughout the organization. Smedeby (2008), who has previous experience within one of the frame organizations (Forum Syd), claims that information absorption is not generally tested, either by Sida or the frame organizations.

We believe that it is crucial for agents to have knowledge about responsibility restrictions and access to adequate information in order to be able to execute the tasks at hand.

5.2 INCENTIVE STRUCTURE

In the non-profit, civil society sector motivation tends to stem from moral convictions, so it is especially important to promote positive incentives other than monetary. Both theory and empirical information support the statement that workers are motivated by pride, respect and esteem. They tend to be idealists who consider self-contribution essential. This may very well result in high efforts and performance with respect to their work. It does not necessarily result in efforts aligned with Sida's recommendations and demands. While corruption is less frequent, the empirics show that irregularities occur despite idealistic motivation. It can thus be concluded that the positive incentives for accurate reporting are too weak and that aid distribution should be unaffected by previous relationships in order to avoid perverse incentives.

The most powerful negatives incentives are fund cessation, funds repayment, and/or termination of collaboration. Previous reports state that these measures are rarely taken. Sida has undermined the negative incentives on several occasions by failing to follow through with reprisals in the face of irregularities. At SEKA they are of the opinion that "nowadays", referring to after the NAO report, it is clear with most organizations that no report implies no further funding. This will be left for future studies to investigate. Whilst control visits serve as incentives, they rarely lead to discoveries of corruption or irregularities.

In addition, challenges arise with respect to smaller projects in that investigation costs are higher than their actual grants.

The one percent goal entails complications. As focus is on distributing a set amount of funding, it is shifted away from looking at previous results. A potential solution is for Sida to suggest a number of projects for which it then gets funding, as today the process is the reverse and the main incentive is to distribute the funds, not necessarily to spend it all well, and even less to control their use. Lump sum contributions to all projects significantly distort the incentives to accurately manage and control each project.

The fact that it is commonly acknowledged that Sida bears final public responsibility for the total performance of all organizations it contributes grants to (Smedeby 2008), may act as a perverse incentive for the organizations to shirk and intentionally misinterpret the directions.

5.3 MONITORING STRUCTURE

Sida does not monitor the framework organizations, but it does require that the frame organizations themselves perform evaluations and control. The Swedish organizations have, however, proven to lack the necessary awareness of the risks of internal irregularities. The fact that all of the projects criticized by the NAO, had previously been approved by Sida, suggests insufficient monitoring. The applied control system was limited to merely reviewing documents. It failed to detect the insufficient audit certificates issued by local auditors, and Sida remained unaware of the shortcomings and problems. In accordance with the auditing instructions the organizations are required to revise the audits of the local NGOs. According to the compliance audit, however, this was not done. As Sida's own controls missed the lack of financial verifications, poor records, and unmotivated costs, we draw the conclusion that monitoring has not been sufficient through all organizational levels. Since the reports do not contain information on the local NGOs, the Compliance Audit (2008) concludes that they do not comply with Sida's auditing instructions. Following the NAO report, however, we are told that Sida regularly evaluates the frame organizations. Particular focus is now on how the frame organizations ensure compliance in underlying organizations and the amount of funding in relation to the activities performed.

The primary means of uncovering corruption and irregularities is not the random controls, but the whistle-blowers. The monitoring should not be too reliant upon these, however, as they are both difficult to encourage and not necessarily trustworthy.

It is the responsibility of the Swedish organization to make sure that the local auditor is competent. Irregularities have on several occasions been discovered without consequence on behalf of Sida. These have resulted from absolute reliance on the local auditing and absence of substance reviews. It tends to be expensive to consult the most qualified auditing firms, so the projects tend to go with a more inexpensive alternative, possibly entailing a lower competency. There exist no proactive routines to ensure auditor competency, and the Swedish auditors do not have contact with the local auditors. Further, the Sida personnel at the embassies in the respective countries are generally not involved in the projects. We find this to be one of the main weak links in the control chain.

We have not found explicit information suggesting any inappropriate dependency relationships between third party monitors and agents. Yet, intuitively the structure and circumstances do not exclude this risk. The auditor is hired directly by the local NGO and reports only to the local NGO. As the documents are not properly reviewed by the Swedish organization or by the frame organization, the auditor's main incentive may well be to keep the client satisfied. This argument represents an extreme case as the local auditor may well be driven by own moral incentives, but this can not be ensured with the routines applied today.

The Swedish organization receives a individual grant to cover administrative costs it incurs itself, but also the costs of its sub-organizations. This grant is not always distributed according to need. Given that there have been discoveries of disorderly administration, there is inevitably a possibility that this grant is sometimes misused. It is concluded that it is difficult to follow the grant through the organizational chain and that the size and complexity of the organizational structure makes it difficult to get a proper overview.

We find from several sources that there is great ambition and activity in the beginning of a project, but that the incentives for appropriate report writing decrease significantly after project finalization.

5.4 THE CASE OF EUROPEAID

In the example of EuropeAid, the relation between cost and output is considered satisfactory, but the process of reporting and the lack of clearly stated goals and strategies are criticized. The type of reporting applied has focused on quantitative measures such as immediate results and sound financials instead of the fulfillment of long-term goals. It has not been possible to conduct on-site verification and maintain focus on the broader purposes of the activities. Further, directing efforts completely on ex-ante screening rather than ex-post screening results in long approval times for projects and causes problems to go unnoticed by the EC. It can thus be concluded that monitoring has not been sufficient through the organizational levels from the EC down to the local projects.

Similar to Swedish aid, the EU aid has been focused on the distribution of a set and unfocused amount of funding, rather than a strategic fund with clearly stated objectives. A lump sum contribution distorts the incentives for accurate management and control of the different projects.

The recent decentralization of the EuropeAid organization in combination with a reduced number of targeted projects has, however, led to a higher concentration of resources and EC personnel per project. This has in turn resulted in a higher degree of control on behalf of the EC, as its personnel have direct access to the local projects, working more closely with the local organizations. The presence of EC employees has led to a reduction in the risk of irregularities and improper reporting between the local organizations and the Commission. As previously stated, the Sida staff at the embassies does not have any contact with the local organizations or projects. Further, the possibility for the EC to directly contract auditors allows for a greater level of control.

6 CONCLUSIONS

The purpose of this study is to study Sida and the organizations it collaborates with in an attempt to identify and understand the mechanisms that can cause anomalies. Through analyzing Sida's organizational structure as well as aiming to add international perspective through the EuropeAid case, we have found a number of factors which affect the principal-agent relationship and thereby the efficiency of aid management.

In order for sub-organizations to fully grasp their role within the aid framework a clearer allocation of responsibility is required. At present, responsibilities are too vaguely and generally formulated.

The length of Sida's organizational chain is shown to diminish signaling power, causing the information flow to become weaker as it passes through each sub-organization. Sida defends this structure by referring to the vast number of projects that need to be controlled. We find, however, that the solution to the problem might be to mimic EuropeAid's strategy to focus on fewer projects in order to work closer with local NGOs and enhance quality.

Furthermore, as information absorption is not tested in an official manner, there is no way to confirm that personnel within the sub organizations have in fact, assimilated the information. According to principal-agent theory, the information structure within Sida's organizational framework is not efficient.

The fact that aid workers are driven by pride and self fulfillment is in many cases sufficient to meet principal's and agent's common goals. Where possible, however, Sida should strengthen positive incentives in order to align the outcome with Sida's specific demands.

An important issue for Sida in order to maintain negative incentives, such as the threat of fund cessation, is consistency. Organizations that do not fulfill Sida's demands should be reprimanded accordingly.

Publishing information and reports would increase both positive and negative incentives, positive through public approval, and negative through a general expectation that Sida will

comply. Responsibility shifts from Sida to the individual organizations, ultimately resulting in fewer perverse incentives for the organizations.

Furthermore, the one percent goal creates perverse incentives in itself as focus becomes to spend a lump-sum of funds. In our opinion, the applications for funds should be based on a budget portfolio of risk assessed projects. This would hopefully encourage a more thorough analysis of projects and prevent the risk of funds potentially being distributed for the sake of distribution goals.

We draw the conclusion, based on the findings in the consulted empirics, that Sida's monitoring structure is not perfectly efficient. We believe that this is partially due to the length of the organizational chain, which complicates the overview needed for efficient monitoring. Furthermore, the main monitoring responsibility falls on the local auditor, whose capability is not generally verified and whose work is seldom comprehensively tested by Swedish auditors. This creates a vulnerable link in the control chain. Once again, we recommend an application of EuropeAid's strategy. Altering the auditing to become more centralized, and allocating the audit service to projects of relevant financial size, would eliminate one level of the control chain and bring Sida closer to the projects, enabling superior quality. Moreover, this would eliminate the risk of dependency relationships arising between auditor and project personnel.

Conclusively, we believe that one of the main problems with Sida’s relationship with its sub organizations is that it is recognized as a partnership rather than of principal-agent nature. For issues to be solved, Sida needs to understand the underlying mechanics of the problems at hand. We hope to have shed some light upon this issue and modestly wish to have contributed to a discussion that might facilitate aid management in the future.

7 FUTURE RESEARCH

As this thesis is a case study of a minor part of Sida's organizational structure, there are great possibilities for future research within the area. With more time and resources, a larger study of the sector would be of interest in order to draw broader conclusions.

We would consider it of interest to go into additional detail in the structure of incentives within aid organizations in general, using an interdisciplinary approach combining economic theory with e.g. organizational and behavioral theories.

Organizations functioning without financial incentives must have other strong drivers such as pride and self fulfillment in order to function efficiently, and studying the mechanics surrounding this complex issue could ascertain the best possible techniques to maximize the positive effects of positive and negative incentives and thus shed more light on the issue of managing aid efficiently.

8 PRACTICAL IMPLICATIONS

Although it is not required in the academic scope of this thesis, we have during our work reflected upon what possible solutions may assist to solve these problems in information, incentive and control systems that unfortunately seem to exist within the organizational chain of Sida and its sub organizations. Analyzing the empiric statements through a theoretical view, and discussing the issue with professionals within aid, financial control and principal-agent theory, we have developed a potential solution that may be beneficial. We believe that an internet based database containing information about the organizations in Sida's umbrella organization, as well as details concerning the projects at hand would address many of the theoretical shortcomings that may have contributed to the noted organizational weaknesses. The database would be accessible to all of the levels within Sida's organizational structure as well as to the government and the public. The main purpose of the database would be to increase transparency and shorten the communication distance between Sida and the actual user of the grants; the local organizations. Users would have different levels of utilizing constraints concerning viewing and altering information. We will introduce the content of the database through a structure referring to the different theoretical components.

We are aware that SEKA has developed an internet based database that can be accessed through Sida's homepage. However, the database has not previously been used by all levels of the organizational structure and does also have several shortcomings, which could be further developed to increase effectiveness in many different areas.

To practically implement the database, Sida should require all local projects to have access to a computer, a scanner, internet and possibly a generator, which should be procured with a mandatory allocated part of the grant. These devices would be essential for the database to function efficiently and Sida should have no problem imposing them as a prerequisite for grants as the projects would otherwise not be approved. We are aware that there might be technical administrative issues, e.g. people resisting change and lacking technological skills, but as in all implementations of new systems, this is something that needs to be discussed and solved during the implementation period to achieve full efficiency.

8.1 INFORMATION STRUCTURE

8.1.1 Responsibility allocation

As contracts between parties in Sida's organizational structure are official documents, all such records should be supplied in the database for increased transparency and enlightenment of responsibility allocation. Discussions should take place to enhance the comprehensibility of the detailed instructions for the areas of responsibility. Employees throughout the organizations should at any time be able to control their area of responsibility, and contracts should be detailed enough to ensure that no responsibility gets lost between organization due to double responsibilities or unclear wording.

8.1.2 Rules and policies

Documentation containing rules and policies should be accessible through the database, much as it is already through Sida's homepage. Naturally, all documents should be available in English to enhance comprehensibility and direct information flow to the local projects. An important change to the present system would be the addition of providing tests to employees at all levels within the organizational chain, ensuring knowledge absorption and fulfillment of the contract clause of information distribution. For the most important rule and policy documents, testing and a certain percentage degree of correct answers should be mandatory. This may raise the importance of information distribution throughout the organizations and hopefully create a stronger respect for rule and policy enlightenment.

8.1.3 Education

Non-mandatory tests may also be supplied through the database. Employees desiring to learn more about particular areas (e.g. book-keeping) would be able to attend internet based courses and access course documents through the database.

8.2 INCENTIVE STRUCTURE

8.2.1 General publicity

The database itself, being available to all organizational levels as well as to the general public, will increase transparency thereby creating positive incentives to behave in accordance with the requirements. As has been evident after the publication of the National Audit Office's report, media has played an important role in the enhancement of incentives for Sida and its

sub organizations. Having the public eye as an additional source of monitoring have certainly increased discussion of possible action plans to increase performance efficiency.

8.2.2 Public financial reporting

Even though public financial reporting is certainly not necessary for all levels of the organizational structure (depending on the size of the grants), a simple indication on whether the project has passed the required financial reporting is sufficient to create a positive incentive to do so. This function also appeals to the usual pride the projects show for their activity, it should be natural to want to show that the project is not only enhancing life conditions for people in the collaboration countries, but that the project is doing so in accordance to Sida's, and international regulations.

8.2.3 Comparability

The database will enhance comparability between projects. Being able to sort the projects by country, size of grant, activity, member size or other criteria, will give a clearer picture of average performance and what general level of performance which should be acceptable in comparison to other projects with similar requirements. Being compared to other projects creates a feeling of probability to complete a task as others have been proven to succeed at. It is also perceived as increasingly shameful not to have completed a task if the public can see that others have.

8.3 MONITORING STRUCTURE

8.3.1 Written report system

As all local projects are obliged to report once or twice a year, these reports could be integrated into the database. In order to avoid double reporting systems (where Sida's reporting requirements might differ from requirements at other levels in the organizational structure) discussions should be held to unify the reporting system and present it in the database for increased access concerning all parties. This function would imply no additional workload to the employees in the local projects, nor other parties, but would rather aim to present the reports of the existing system in a different forum, streamlining the information flow. It would probably be of interest to give the general public consistent updates of the projects activities and results.

8.3.2 Financial reporting

The following detailed financial information should mainly be accessible to Sida, bookkeepers and auditors, not to the general public. The database would facilitate financial reporting substantially through the possibility of scanning financial verifications. Within the book-keeping and audit sectors, there have lately been discussions about the scanning of documents to decrease the large quantity of documents, but in this case the focus would rather be on the accessibility of documents to financial controllers such as the Swedish auditors. As the report from the National Audit Office shows, in the reviewed cases, the Swedish auditors have been reluctant to demand underlying documents or to have an open dialogue with the local auditor in order to support audit certificates. This in turn has caused many shortcomings to pass by unnoticed. Increasing document accessibility through the database would hopefully strengthen incentives for the Swedish auditor to review them, according to proper auditing standards.

Budgets and outcome should also be available through the database. As budgeting sufficient means for administrational tasks has historically been problematic , the publication of budgets would hopefully encourage projects to put additional focus on this area to efficiently manage the database.

Over time, the database would create an easy accessible, extensive storage of financial records that would help facilitate economic follow up and development overview.

As mentioned earlier, whether or not a project has completed the required financial reporting would be shown to the public, creating further incentives to act obligingly to Sida's requirements and the international laws of financial reporting.

We acknowledge that this would add supplementary administrative workload to the employees of the local project, but considering the potential outcome of these additional steps in the bookkeeping, which is backed by international law and has a substantial influence on the organizations trustworthiness, we believe it is well-invested time.

8.3.3 Reporting of finalized projects

A task with previously scarce incentives is the paperwork that needs to be produced after a project has been finalized. As the activities are completed and the actual results been reached, the administrational burden of describing the results to higher levels in the organization may be under prioritized. Publishing these reports through the database may introduce additional incentives for timely and accurate reporting. Furthermore, Sida may have direct access to the documents, as opposed to several levels of organizations that the reporting needs to pass through.

8.4 DESIRED OUTCOME POST IMPLEMENTATION

Assuming the database is properly used by all parties, the desired outcome following an effective implementation, will hopefully be simplified information and reporting flows between principal and agent, monitoring facilitation and additional incentive creation through the increased public accessibility. In figure 3, we have described the resulting simplification of flows between principal and agents, compared with Figure 2 (p. 14).

Figure 3 – Desirable Information, Incentive and Monitoring flows post efficient database implementation



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