

# WHAT IF DEVELOPMENT AID REALLY REWARDED RESULTS? REVISITING THE CASH-ON-DELIVERY (COD) AID MODEL

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**Introduction.** “Results-based” funding discipline is in high political demand today, but the devil is in the details. Tight earmarking of aid runs counter to local ownership of spending choices and channels. Measurement, attribution and perverse incentive problems arise with many target-driven schemes. The Cash on Delivery aid model, though not yet implemented in its pure form, potentially offers a way to handle these tensions in a simple yet effective design.

After rehearsing the basic features of COD, as it relates both to “traditional” development practice and to some similarly-inspired “results based” aid instruments, I consider what features might make COD contracts an attractive alternative, given the choice, from both recipient country and donor perspectives. This is mostly to do with the shifting risk burden and how that is appreciated by different parties.

For the sake of emphasis, I relax COD proponents’ assumption that COD should be implemented only at a pilot scale initially, and be funded entirely over and above existing traditional aid. That is, I explicitly consider it, starting now, as a potential substitute for such aid. This perspective forces us to confront some systemic aid effectiveness issues sooner.

**What is Cash on Delivery (COD) ?** The radical and refreshing COD proposal by Barder and Birdsall (2006)<sup>i</sup>, fleshed out in Birdsall, Savedoff and others (2010)<sup>ii</sup>, advocates a “hands-off” approach to aid, triggered *purely and proportionately* by recipients demonstrating additional verifiable development outcomes, compared to earlier years.

Their usual illustration is of a guaranteed payment of, say, \$200 in respect of every extra “assessed completer” of primary school, i.e an additional child enrolled in their last primary year who sits a standardised achievement test. Test results are not themselves a condition of aid disbursement, but must be made public, increasing political pressure on raising learning standards. Independent auditors validate how many children sat the test on a given day, to forestall excessive COD claims.

This approach can apply equally to other measurable outcomes, or at least well-defined outputs closely associated with outcomes, like immunisation rates or access to basic sanitation. And it can operate at different levels, for example as a contract between donors (including private ones) and one or more national governments, or between the latter and their state and local communities.

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<sup>1</sup> The facts and analyses in this document have been verified by the OECD Development Co-operation Directorate. However, the opinions and arguments expressed do not necessarily reflect the official views of the Organisation or of the governments of its member countries.

## What's New Here? "Pure" COD contracts sidestep at least three major features of traditional aid design:

- (1) There is *no external requirement to track* on what, or how well, the recipient spends money disbursed under a COD award.
- (2) There is *no obligatory tie-in to inputs or expertise* offered by the donor for, say, education. COD recipients are free to choose between alternative offers of such aid, to contract out implementation, or to rely entirely on their own human and financial resources for delivery. The result, not the method, matters in contractual terms.
- (3) There is also *no free lunch*: if sufficient results are not verified, COD funds for that year are not disbursed, and *vice versa*. Contrast this discipline with the usual muddling-through process after performance targets are missed in other aid contexts, when suspension of aid is very much a last resort. Conversely, political "accidents" unrelated to specific outcomes can and do stall traditional aid unexpectedly.

### How does this relate to other results-based financing?: some close cousins of COD.

The nearest precursor of COD is the (original) **immunisation system strengthening (ISS)** payment offered by GAVI (the Global Alliance for Vaccination and Immunisation), involving fixed payments of \$20 per extra child immunised over a baseline year. The bonus so generated is made available as a lump sum, usually into an account controlled by the relevant Ministry of Health, without end-use restrictions from GAVI. (This scheme has reportedly evolved toward greater hands-on engagement by GAVI more recently NB.)

A variety of other **results-based disbursement schemes** have been tested, especially for health and notably by the World Bank (most recently through its Health Results Innovation Trust Fund). Two completed programmes, aimed at polio eradication in Nigeria and Pakistan, included so called "buy-backs" or conversion into grants of concessional loans, triggered directly by evidence of immunisation results. They also demonstrate such designs' potential for leveraging non-ODA finance (in the polio example, the Gates and Rotary Foundations), which could apply more broadly to COD-type constructs.

The European Commission's **MDG Contract (MDG-C)** is also quite similar in intent to COD, offering as it does a "variable tranche" of budget support contingent on the country reaching agreed threshold levels of health or education outcomes, on top of a "fixed tranche" which is not. However, there remain external audit requirements on the use of funds, and there are tapering-in arrangements to phase in the effect of any missed target on subsequent year disbursements (diverging, i.e., from COD key features 1 and 3 above).

Also, while the expected MDG-C payoff closely approximates the idea of a "tariff" for extra units of achievement, it also varies according to overall country performance, as assessed by the Commission. Access to the MDG-C is conditional on a fiduciary environment judged adequate for general budget support, which is not strictly speaking the case for COD.

Proponents of COD argue that it has major **advantages over traditional aid** from an aid effectiveness perspective, chiefly these seven (Box 1):

### BOX 1: Advantages of COD?

1. It reinforces recipient accountability to domestic constituencies.
2. It focuses on end results and makes these transparent to a wide audience.
3. It allows for learning by doing : interventions can be adjusted to raise impact.
4. It provides opportunities to attract private funders by “syndicating” awards.
5. It drives harmonisation among participating funders.
6. It gets donors out of micromanagement, saving bureaucracy and costs.
7. It provides a strong narrative for continued taxpayer and philanthropic support.

At the same time, **observers have raised concerns** (Box 2). Some of these can only be gauged when there is a rigorously evaluated COD track record: others hinge on design features which are not yet finalised. A large subset (especially points 1, 3, 6 and 7) holds true at least as much for other forms of aid as for COD, if not more so, so does not tilt the comparison against COD. The inter-play of traditional and COD aid, where they might coexist in large amounts, is discussed further below.

### BOX 2: Possible question marks?

1. COD aligns to national priorities only if the results menu maps closely to them.
2. For poorer countries, pre-financing outside of COD is needed to prime the pump.
3. No new project-level control on waste and corruption of aid proceeds.
4. No provision for *force majeure* safeguards excusing low performance.
5. Real possibility of payment against fluke results, not deliberate effort.
6. Some COD metrics are inevitably closer to outputs than outcomes.
7. All targets can be “gamed” to some extent, with unintended consequences.

### Size and the substitution effect.

As now proposed, COD is envisaged as a modest top-up, over and above current levels of aid to typical country recipients. It should be large enough to have an incentive effect, but it is NOT intended to cover the full costs of, say, enrolling and retaining in school as many as possible of the children who miss graduating today. Most of these ambitions are already built into current government expenditure plans and related donor programmes. COD could however accelerate these plans and thereby achievement of the relevant MDG.

A recommended design feature is that the “tariff” or prize of, say, \$200 per extra child be established as a global flat rate, not subject to variation at the country level. Therefore countries with lower marginal costs- mainly those starting from lower achievement levels-should be able to achieve big increments initially for much less than \$200 on average, generating a substantial surplus . Conversely, countries closer to the MDG threshold are likely to find the last part of the gap much more expensive to close *per capita*, and may get only a partial subsidy for that effort from COD.

Simulations for a mid-sized African country estimate COD awards peaking at \$30 million in year 12 and declining to zero ten years later. The peak is roughly equal to total external aid for basic education in that country today, or half of aid to education, or around ten percent of overall aid, from a single major COD contract. These are not marginal amounts therefore, albeit building up only gradually.

### Box 3. DFID's Pilot Programme on Results-Based Aid and Cash on Delivery Contracts

DFID supports various approaches linking payments to results, including most of the multilateral instruments mentioned here. It categorises them broadly as Results-Based Aid (RBA), an aid relationship between donors and partner governments, or Results-Based Funding (RBF), an approach to contracting service providers beyond central government, or incentivising beneficiaries to use services.

DFID is committed under its Structural Reform Plan to "Pilot Results-Based Aid and Cash on Delivery contracts in 3 developing countries by November 2011". The most advanced cases at different stages of design are:

1. **Ethiopia.** Using the COD model to increase the school completion rate for girls: for every extra girl completing grade 10, the Government will receive a certain amount (RBA). Payments are passed on to local schools, which control their end-use. The approach is expected to increase completion rates by 10-12% over four years.
2. **Uganda.** Private nonprofit health providers will be paid (RBF) for subsidised or free maternal and child health care in certain regions, at a given rate per child under 5, and per pregnant woman. A voucher scheme for transport of pregnant women to health facilities is also envisaged to address demand-side issues.
3. **India.** Private sector providers are to be paid (RBF) on provision of renewable energy technology to poor households. Pricing to be set by auction to ensure value for money.

Other pilots are also under consideration.

### What happens if COD really takes off?

A few donors, notably the UK, are actively testing COD-like approaches (Box 3). There is a strong political driver for greater accountability to taxpayers for value-for-money, and better metrics to document this, and this works with the grain of COD. It is hard nonetheless to predict how far and fast COD's popularity will spread, in different budget contexts for different donors. Its proponents, moreover, explicitly state that in the absence of rigorous evidence about how well it works, this endeavour should remain on a modest scale initially, funded entirely from increments in overall aid.

But as a thought experiment, let's instead assume COD "goes orbital". Let's interpret that to mean that in at least a subset of relevant countries and major donors, it quickly rises to say 10% of the expected aid envelope, and considerably higher, say 30%, in some major sectors like education (as, incidentally, happened in less than 5 years, when the Global Fund to fight TB, AIDS and malaria was injected into the donor universe for health with a unique funding mandate).

This are only crude benchmarks, to illustrate one among several plausible scenarios. Even given sustained political interest, it will be objectively hard for some years to frame most development efforts in strict COD terms, given measurement limitations, and wrong to focus funding solely on what is easy to measure. (Note, however, that "pure" COD funding is unrestricted in terms of end-use, notwithstanding that disbursements are triggered by specific outcomes). Over time, moreover, COD-type incentives could bring impact evaluation discipline into outcome areas hitherto relatively unscathed by "hard" performance metrics, like civil service reform. This push could lead to a general shift of aid toward interventions and sectors where results metrics are more persuasive.

## Systemic risk shift. With COD implemented to scale, the risk burden shifts between and within donors and recipients.

From the **recipient** perspective, in COD, they are asked to bear more of the performance and delivery risk, for which they are usually better suited, in exchange for a freer hand on how outcomes are to be achieved, and the promise of more predictable donor disbursement behaviour, a risk now largely outside their control. For any expected payoff, recipient reactions will vary according to domestic actors' risk profiles and experience. Thus there is evidence suggesting that flows of traditional aid for education, for example, are much more volatile than hypothetical COD payoffs based on historical completion rates, which are relatively stable. Greater predictability of donor behaviour and fewer transaction costs will weigh in on the side of COD, in the minds of national decisionmakers and especially of finance authorities.

Conversely, the audited aggregate of thousands of school and family stories may fail to match expected levels for reasons well beyond government control, such as parents pulling children out of school in the wake of a failed harvest or other calamities. These are not risks to which traditional aid overtly exposes recipients, financially at least, though socially and politically they have always borne them. Recipient governments could also presumably mitigate the narrow financial loss risk at a relatively affordable cost (say, by giving vulnerable families small cash benefits conditional on continued school attendance). COD is intended as a relatively *long-term* (5 years plus) contract, so unexpected shocks are more likely to be balanced by subsequent rebounds than in shorter-term experiments. But different types of risk are nonetheless to be weighed.

If COD donors are expected to phase out their traditional sectoral aid in parallel, there will be classic fungibility effects, rather like when traditional project aid is replaced by general budget support. The COD payoff does not necessarily have to be ploughed back into, say, the education budget, as against being directed elsewhere by the country's Treasury<sup>2</sup>. That feature is obviously efficient from the national perspective. The education authorities might nonetheless fear losing powerful external allies, assuming their present earmarks align with the ministry's ambitions. Conversely, they could expect to gain domestic political allies for improving educational outcomes, and more policy space to implement their plans. So the preference for COD depends to some extent on whom, on the recipient side, is making the call between COD and traditional aid, and what their other opportunities are, if and when a choice between the two is offered, explicitly or implicitly.

For **donors**, taking COD to scale means that they reduce the risk of paying for low-impact inputs, or conversely, increase their chances of buying success. Underspends can be politically defended as being beyond their sphere of control, increasingly, and spending surges as being good news, not lax management. COD could however pose them significant problems of managing *liquidity*. This is because most donors' resources are country-earmarked, but COD payout is sectorally variable, both in bad and unexpectedly good years. The latter have to be honoured in full, obviously, if COD credibility is not to collapse. There will therefore probably have to be at least regional if not global sectoral pools (within which individual country risks are uncorrelated) to smooth these fluctuations. Donors could consider various other devices to manage their financial exposure: maximum cash limits per country, limited numbers of countries allowed to enter similar parallel contracts, and/or cross-country pools or challenge funds with an aggregate limit. All will have consequences on the broader appeal as well as the ultimate impact of the scheme through the set of incentives generated.

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<sup>2</sup> However, in the DFID Ethiopia pilot, COD funds are directed to the school level through the regional authorities. This encourages innovation and flexibility at the point of service, but precludes or restricts other potential uses, both outside the education sector and on demand-side interventions, such as cash transfers or other incentives, connected to it.

## Questions for further discussion:

At the level of **overall aid effectiveness**, several questions remain to be answered in respect of COD design. Most obviously:

1) *Who sets the COD reward tariff and on what basis?* Are they the product of bilateral or multilateral negotiations? If there is competition across countries, how might those who have already achieved more progress not be unfairly penalised, and how do those with the greatest present need get recognised?

2) *How is the broader menu of COD contracts decided on, and how is country ownership respected in doing so?* COD offers may materialise in combinations deemed (by donors) relevant globally or regionally, whereas country priorities are set nationally. Over time, the “menu” of COD rewards could become broad enough to cater for most situations: but that is unlikely to be the case initially in any country, and for many years in some.

3) *What is the commitment from the outset, if any, of COD donors to maintain additionality* (a) at overall country level and (b) at sector level? Against what baselines is this pledge calculated? (NB India was reportedly interested in joining the original polio buyback schemes, but as polio eradication was and is a global as against purely national priority, only if such funding were clearly over and above its country IDA allocation at the time).

4) Will donors agree to exempt COD from *political suspension safeguards* applying to traditional aid (as failing that, COD could compound the risks of both types of aid)? For example, could COD payments justified by verified outcomes be guaranteed for a minimum of one year beyond suspension of other types of aid?

5) Conversely, are donors prepared to consider “*insurance*” aid outside of COD, to cover situations where purely exogenous factors, not lack of government effort, explain unfavourable COD outcomes? Or to structure the COD payoff baseline so as to recover some of the lost funding faster, if and when outcomes improve?

6) Could *existing instruments* such as the European Commission’s MDG-Contract be adapted and expanded to serve some or most of the intended purposes of COD? For example, could MDG-C be available in some form for fragile states with a relatively heavy MDG deficit, despite their overall macro and prudential situation not qualifying them for other forms of budget support?

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<sup>i</sup> Barder, Owen and Nancy Birdsall. 2006. “Payments for Progress: A Hands-Off Approach to Foreign Aid”. Working Paper 102. Center For Global Development, Washington, D.C.

<sup>ii</sup> Birdsall, Nancy and William D. Savedoff, with Ayah Margoub and Katherine Viborny. 2010. “Cash on Delivery: A New Approach to Foreign Aid”. (With an Application to Primary Schooling). Center for Global Development, Washington, D.C.