Financing and Aid Management Arrangements in Post-Conflict Settings

This note, summarizing the analysis and recommendations of an upcoming CPR Working Paper of the same title, looks at issues related to financing modalities and aid management arrangements in post-conflict situations. It makes a number of recommendations based on a review of several recent case studies, of which four are assessed in detail: West Bank and Gaza, Bosnia and Herzegovina, East Timor, and Afghanistan. It focuses on the lessons of experience on multi-donor trust funds and on the recipient government’s aid management architecture in post-conflict settings.

The general setting

Severe conflict, especially its most virulent ethnic form, destroys much more than buildings and power plants. It short-circuits the rules that keep human interaction constructive and predictable, targets primarily the organizations and individuals who administer those rules, and wipes out most positive forms of social capital. Post-conflict reconstruction is first and foremost an institutional challenge. Hence, the first lesson of experience for aid in post-conflict situations is the imperative of assuring robust linkages between the aid and the rebuilding of local institutions, and the core challenge is the balancing of immediate reconstruction priorities with long-term institutional development.

This paper is concerned with the specific issues of financing modalities and aid management arrangements in post-conflict situations, and advances a number of recommendations on the basis of a review of several recent cases, among which four are assessed in detail: West Bank and Gaza, Bosnia and Herzegovina, East Timor (Timor-Leste) and Afghanistan. While generally applicable recommendations do emerge from the review, the most important recommendation is to tailor the design and sequencing of financing and aid coordination to the circumstances of the specific case. Each case has its own unique core features. Thus, for example:

- In West Bank and Gaza, the key features to which the funding and programming of post conflict reconstruction had to adapt were the constraints posed by Israel, the excessive centralization of decision-making in the Palestinian Authority, and the patchwork nature of the territories under Palestinian control.
- In Bosnia and Herzegovina, the extreme interethnic hostility and political and administrative fragmentation conditioned everything, the main challenge of aid arrangements was to recognize the reality of dysfunctional fragmentation without thereby strengthening it, and the strategic principle for future recovery can be formulated as "infant social capital" protection.
- In East Timor, external assistance was affected from the start by the virtual absence of any administrative capacity in the territory, the extremely weak human resource base and its poverty.
- In Kosovo, by contrast, some local capacity existed, but mainly in parallel informal networks (often linked to criminal organizations), competing for influence and resources with the UN and the formal provisional institutions of self-government.
- In Sierra Leone, the core issue was disarmament and reintegration of former rebel combatants—including the difficult problem of child soldiers.
- In Afghanistan, the key objective is to reconstitute a functionally limited but effective state, and to reduce economic distance by re-establishing security and restoring transportation and communication links.

While oversimplification is to be avoided, an identification of the core features of each post-conflict situation is mandatory for an effective reconstruction strategy, and for the design of the financing and aid management architecture that is to embody that strategy.

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Trust funds and aid management organization

By all evidence, the World Bank has been generally effective and very timely in assisting post-conflict reconstruction; the trust funds and other financing arrangements have not only been grounded on the experience of earlier cases, but have also been innovative where needed; and much successful effort has gone into facilitating the involvement of the recipient government and local partners. In particular, the quality, efficiency and speed of Bank work in the early post-conflict days has been nothing short of remarkable. The Bank has also endeavored to consult with and elicit the cooperation of other major donor agencies, albeit with mixed results—mainly because of higher-level political disputes. However, the Bank (and the donor community as a whole) has occasionally been weak and/or insufficiently clear on the need for the recipient government and other donors to abide by certain basic policy standards. Also, the dynamics of the development business and the short-term urgencies typical of post-conflict situations have often been allowed to prevail over long-term institutional development objectives. In the future, the Bank might consider being more firm on the essentials and more flexible on everything else. Overall, there is a strong consensus that only the World Bank can provide the experience, drive, and diversity of knowledge required for effective leadership of international assistance to post-conflict civilian reconstruction. With that consensus comes a responsibility for the Bank to listen, consult, and facilitate—qualities not traditionally associated with this institution. The main lessons of experience on multi-donor trust funds (MDTFs) and on the recipient government’s aid management in post-conflict situations are summarized below.

Among structural and design issues, the main conclusions are:

- An MDTF must fulfill both a fiduciary and an executive function. The legal, accounting, disbursement and reporting provisions required for the fiduciary function are now well defined. The effective exercise of the executive function of an MDTF requires, in addition, an agreed program of reconstruction activities; ownership by government and major potential donors; a workable interface with the local aid management agency; fullest possible transparency; and openings for citizens’ voice.

- A realistic, comprehensive and public government budget, consistent with the reconstruction program, is essential.

- There must be incentives for individual donors to join an MDTF, including an MDTF design that gives them comfort that their aid goes for priority purposes while precluding earmarking of the aid. While all contributions are commingled into a common pool, donor preferences can be explicitly acknowledged, and expenditures in the broad categories should be regularly reported.

- MDTF governance arrangements must provide for systematic consultation with and reporting to the contributing donors. In this regard, clarity of arrangements and cohesion among the main donors are more important than organizational simplicity per se.

- The coverage of an umbrella MDTF can potentially encompass all civilian expenditure except very large flagship investment projects, strictly humanitarian aid, or security-related programs such as demining—separate dedicated trust funds can be useful mechanisms for those activities. The main advantage of an umbrella fund is the possibility of a closer linkage with the recipient country’s budget, and hence more robust dialogue on fiscal and development policy. What is to be avoided is fragmentation of funding vehicles, especially between financing of recurrent costs and investments.

- On balance, it is preferable for a Bank-administered MDTF not to finance police or prisons.

Among the organizational and procedural issues, the main ones are:

- Time is of the essence for aid interventions in post-conflict situations. A pragmatic compromise is needed between the extremes of waiting until all contributions are deposited, and of starting MDTF operations as soon as the first pledges are made.

- No compromise can be made, however, with the need to put in place measures to minimize corruption and leakages before the MDTF enters into any commitment.

- Non-project technical assistance (TA for institutional development and capacity building) can be financed either as a component of an umbrella MDTF or by a separate trust fund. In either case, the key requirements are an agreed framework of priorities, the closest possible involvement of the local counterparts, and tight monitoring and quality control. Non-project TA activities should be linked with a host-government capacity-building program, and every single TA contract should include a training element. At a minimum, TA should take special care not to aggravate local capacity problems by introducing overly complex systems or methods unsuited to local conditions.

- While an agreed reconstruction program and national budget are fundamental, an unallocated financial cushion should be maintained in the MDTF for urgent expenditure needs as they arise.

- Recurrent costs are well-suited for financing through an MDTF, but the monitoring of the broad expenditure categories (on the basis of clear budgetary understandings) is essential. Also, the payments mechanism must function well—even if it must be initially subcontracted. On balance, in post-
conflict situations it is advisable to hire a consulting firm to act as agent for the MDTF to verify the eligibility and correctness of withdrawal applications, and carry out spot checks of the validity of transactions.

- The Bank should be prepared to halt disbursements in the event of serious and uncorrected deviation from the agreed policies and expenditure composition, and/or substantial corruption.

The aid management agency (AMA) of the recipient government is the bridge from donors to government and the main source of initial client ownership. As noted, the fundamental strategic challenge of post-conflict reconstruction is the reconciliation between immediate urgencies and longer-term sustainability. In most cases, the government is extremely weak during the immediate post-conflict period. Thus, the agency must not only interface with donors and regulate aid traffic, as in steady-state situations, but also help formulate the reconstruction program, serve as protogovernment, and implement directly a number of activities. There is accordingly a “sunset dilemma” in post-conflict reconstruction: an aid management agency is created because the formal government structures do not yet exist or do not have the capacity to implement reconstruction, and also because donors require transparent and reasonably corruption-free financial management. Over time, as the regular governmental institutions grow, competition emerges between the governmental structures and the parallel aid management agency. Instead of a smooth handover, the parallel tracks tend to persist, partly because the AMA has built up greater implementation capacity and partly because accountability and financial transparency remain a must for donors. And so, the AMA stays active longer than envisaged, competing with regular government ministries for resources and authority.

The key lesson of experience is thus that government and donors should agree from the outset on an exit strategy for the aid management agency; link that strategy to appropriate conditionality vis-à-vis emerging government structures; and at the same time assist in building institutional capacity in the regular organs of government. Proliferation of weak or corrupt government ministries is not a sound alternative to a technocratic monopoly of decision-making by the AMA. Other lessons of experience with the structure and operations of aid management agencies in post-conflict cases are discussed in the text.

The reader is also referred to the text for a discussion of the allocation of MDTF responsibilities among the Bank, the aid management agency, and the monitoring agent for the trust fund, as well as a suggested sequence of stages of Bank involvement in reconstruction needs assessment, aid coordination and MDTF establishment—respectively during the in-conflict, pre-post-conflict, and immediate post-conflict periods.

General issues and recommendations

A general prerequisite for post-conflict reconstruction and effective financing is to establish and maintain public order and security. The best needs assessment, reconstruction program, ownership, staffing, financing arrangements, resource availability, policy framework, and implementation capacity are worth little if program implementation and economic activity are constrained by lack of physical security.

Among the other contextual and coordination requirements emerging clearly from experience (in addition to the need for a comprehensive and realistic government budget, noted earlier) the most important are:

- The need for a definite political resolution of the conflict and clear mandate for the Bank.
- Genuine partnership among the key international institutions—the Bank should insist on the “script”, not on the “cast”, i.e., actively provide for meaningful roles for other donors and liberally share the credit for accomplishments, but without compromising on the basic criteria for effective assistance. For their part, once a consensus is reached all donors should cooperate with the norms and programs—whether or not they choose to contribute to the MDTF. The frequently-used “comparative advantage” terminology is especially misleading in a relationship that should be characterized by cooperation and not by trading.
- Although the priority in post-conflict reconstruction is on urgent short-term needs, neglect of basic economic policy issues will preclude the achievement of sustainable results.
- Aid must encourage government capacity building and facilitate local initiative as much as possible.
- A large diaspora can be a human and financial asset, but a balance between “outsider nationals” and “insider nationals” is important for sustainability. External agencies should be mindful of their natural bias in favor of the “outsiders” and try to correct it.
- Proactive communication is important to deflate early unrealistic expectations and the ensuing erosion of public support.
- A tight timetable of political and economic progress, with appropriate benchmarks, is needed for momentum and focus.
- The divergence between the political timetable and the reconstruction timetable is normal, but needs to be recognized in order to be bridged. In cases when the UN exercises civilian authority and serves as de facto government, it is especially necessary for the Bank and the UN to reach early and clear understandings of each other’s roles and responsibilities.
- The international experience yields no conclusion as to the relative advantage of tackling hard political
issues early in order to facilitate the reconstruction efforts, or after a period of consolidation in order to permit some rebuilding of trust. However, it must neither be assumed that hard issues must necessarily be left until later, nor to forget that at some stage they do need to be addressed.

- Setting public management standards and sound policies is key for sustainable fiscal and institutional development, but in high-profile cases efforts to do so can be frustrated by external pressures to keep the money flowing. Reasoned firmness by the Bank, through judicious use of the MDTF resources, has a chance to prevent excessive expansion of governmental structures and erosion of standards of transparency, integrity, accountability and the rule of law—but only if there is a general consensus on policy direction and the donor community coalesces around those standards.

- Because post-conflict reconstruction is inherently a top down affair, caution must be exercised lest existing NGO activities and local structures are inadvertently suffocated by the reconstruction assistance. Beyond protecting what exists, the Bank should aggressively encourage the recipient government (and the donors) to incorporate into the reconstruction program the contribution of local communities, and of the local and international NGOs that have been laboring in conflict areas for years.

The last point leads back to the initial remark. The potential contribution of NGOs and local structures goes much beyond assisting in implementation, or even acting directly as implementing agencies. Some of the most effective components of reconstruction programs in the past have relied on empowerment of local communities and partnerships with NGOs. Moreover, capacity-building at the local level is a necessary condition for the evolution of the rule of law, accountability, and transparency, and the local structures can be essential as well to underpin the gradual rebuilding of the social capital destroyed by the conflict.