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# **Monitoring Elite Capture in Community-Driven Development**

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## 1. Introduction

Recently, a lot of attention has been paid to improving techniques and data to better assess the effectiveness of development interventions. This is a welcome move in so far as the impact of such interventions in the past has usually been poorly assessed. It is particularly welcome with regard to community-based, or participatory aid projects since considerable resources are being currently earmarked for them by almost all types of donor agencies, including large international organizations. For example, the amount lent by the World Bank for CDD (Community-Driven Development) projects has massively increased from \$325 million in 1996 to a conservatively estimated figure of \$2 billion in 2003 (Mansuri and Rao, 2003). Furthermore, CDD has been, for many decades, the key approach advocated by many Non-Governmental Organizations (NGOs) working in developing areas. Yet, it is a sobering fact that, in spite of such a long experience with this approach, scant material is available from NGOs to allow us to gain useful insights into the validity and the conditions for success of the participatory approach.

The scepticism of many NGOs about the need and purpose of evaluation and their emphasis of action over analysis are largely responsible for this situation (Ebrahim 2003: 817). The evidence produced in favor of CDD thus tends to be anecdotal, based on unqualified generalizations or unsubstantiated claims. In point of fact, when evaluations take place, they are often biased in a direction favorable to CDD projects. Indeed, a “praise culture” is pervasive among all the actors involved who have a tendency to “resist the presence of evaluators and make efforts to influence their work and present results that will provide a more favorable impression” (Mansuri and Rao 2003 : 30-31; Riddell 1999: 223-34). Finally, to the extent that serious evaluations of NGO projects exist, they are almost never released for public scrutiny. As pointed out by Alnoor Ebrahim (2003: 825), “For a sector that views itself as largely mission-driven, there is an urgent need to take performance assessment seriously in order to justify activities with substantiated evidence rather than with anecdote or rhetoric”.

Unfortunately, the criticism can be extended to almost all organizations that have adopted the CDD approach. Thus, for example, interventions funded by the World Bank have also been inadequately assessed, a fact deemed “inexcusable” by Mansuri and Rao (2003). The consequence of this dearth of reliable evaluations is ineffective learning-by-doing where it is badly needed. Clearly, so far as we can judge from recent surveys (Conning and Kevane 2002 ; Bardhan 2002 ; Mansuri and Rao 2003), available evidence does not justify the speed and the enthusiasm with which many agencies, especially large bureaucracies, have started to implement CDD (Platteau and Abraham 2001, 2002, 2003). As a matter of fact, the evidence at hand does not unambiguously confirm the view that CDD projects are more effective than more conventional

approaches in terms of efficiency, equity (reaching the poor), and sustainability. NGOs themselves, contrary to a widespread belief, have not produced impressive results, even with respect to alleviation of poverty and promotion of participation (Carroll 1992; White and Eicher 1999: 33). The same agnostic conclusion emerges from a recent review of empirical studies of decentralized delivery of public services. For the author, indeed, although the studies available suggest generally positive effects of decentralization, “it is hard to draw conclusive lessons” and, therefore, “the idea of decentralization may need some protection against its own enthusiasts” (Bardhan 2002: 200, 187; and Asthana 2003, for an example). Caution is required because most studies are essentially descriptive and point to correlations rather than carefully tested causal relationships.

This being said, both the limitations and the cost of new impact appraisal techniques, especially for comparatively small organizations that sometimes have a long experience, and perhaps a comparative advantage in, the CDD approach, may constitute a serious barrier to adopting them. In addition, not all projects and programs are amenable to evaluation by these modern techniques, and the extent to which some objectives, such as sustainability, have been attained are not easily captured by them either. Finally, a point that is rarely made by economists concerns the reliability of the data collected. My own experience with NGO projects over the last thirty years has convinced me that quality of the data is probably the most tricky problem. Consider the following judgment pronounced by an anthropologist with a long field experience in Mossi villages of Burkina Faso:

“Confronted with the hegemonic ‘project’ of the donor, the local population, for fear of losing the aid offer, prefer to remain silent about their practices and aspirations. This is because these practices and aspirations are perceived to be so far away from those of the donor that they are better not disclosed. Such is the vicious circle of development cooperation: the fear of avowing the discrepancy between the two views because it could lead to the discontinuation of the aid relationship, has the effect of strengthening the donor’s confidence in the validity of its approach” (Laurent 1998: 212 –my translation).

Reliability of information is still more questionable when we consider queries about the distribution of projects benefits that are not directly and easily observable. Answers may be elusive or squarely wrong because asymmetrical social relations prevent people from speaking out the truth.

The purpose of this paper is to argue that, when the so-called ‘elite capture’ problem is serious, mechanisms of fraud detection are necessary, yet they are not enough. Coordination mechanisms, at the level of aid agencies and/or at the level of the ultimate purveyors of funds for CDD, must exist to tame or mitigate the opportunism of local leaders. One important conclusion of our analysis is that no effective control of the elite capture problem is possible if failures encountered

by aid agencies are punished while successes are rewarded. Taking this conclusion into account would involve a radical change of perspective in development aid circles. As for impact assessment studies, they would clearly make an important contribution if they could be used towards the purpose of detecting fraud, which implies that the aforementioned problem of fact disclosure in distributional matters is somehow surmounted.

In Section 2, the importance of the elite capture problem is illustrated from a case study material and further documented. Based on a framework of strategic relationships between the various actors involved in CDD projects, Section 3 then proceeds by examining the feasibility of a leader-disciplining mechanism using sequential and conditional disbursement of aid funds in the context of decentralized bilateral relationships. In the light of the inherent limitations of such a solution, more sophisticated, multilateral control mechanisms are discussed in Section 4. The role of impact assessment studies and the dissemination of their main results will come out clearly at that stage. Section 5 concludes.

## **2. Evidence of Elite Capture at Local Level**

### *A Case Study from West Africa*

In the late years of the 20<sup>th</sup> century, a Western European development NGO (whose identity is not disclosed for the sake of discretion) established a relationship with a village association in a Sahelian country (see Platteau and Gaspart 2003). This association, which is a federation of several peasant unions, had been initiated by a young and dynamic school teacher, the son of a local chief. The NGO decided to follow a gradual participatory approach consisting of strengthening the association institutionally before channeling financial resources to it. This decision was the outcome of a carefully worked out diagnosis that brought to light important weaknesses of the partner association. Clearly, those weaknesses had to be corrected before genuine collaboration could take place: proclivity to view aid agencies as purveyors of money which can be tapped simultaneously, lack of analysis of local problems and of strategic vision for future action, loose and undemocratic character of the association (ill-defined objectives, ill-defined roles and responsibilities of the office bearers, absence of internal rules and reporting procedures, etc.).

After two years during which institutional support was provided in the form of guidance to improve the internal functioning of the partner association and to help define development priorities and the best means to achieve them, funds were made available for different types of investment. Within the limits of the budget set for each prioritized line of investment, the association could choose the project deemed most useful. A special committee was established to

prepare rules regarding the use of the budget and enforce the abidance of such rules by different projects. In this way, the group could hopefully appropriate the process of decision-making, preparation of project proposals and programming of the activities involved (all aspects traditionally undertaken by the foreign donor agencies). Continued support at different levels (technical, administrative, organizational, and methodological) was found necessary to help in the effective implementation of the projects.

In spite of all these efforts to strengthen the partner association institutionally, things turned out badly. Thanks to the collaboration of two active members of the General Assembly (actually two animators) and the local accountant, the foreign NGO discovered serious financial and other malpractices that were committed by the main leader of the African association: falsifying of accounts and invoice over-reporting, under-performance by contractors using low-quality materials, etc. It reacted by calling on the local committee to sanction these manifest violations of the rules, yet at its great surprise no punishment was meted out and the general assembly even re-elected their leader in open defiance of its request. The two dissident animators were blamed for being driven by jealousy and envy, while the accountant was fired. Here is a clear illustration of the support that poor people are inclined to give to an elite member on the ground that they have benefited from his leadership efforts. That he appropriated to himself a disproportionate share of the benefits of the aid program is considered legitimate by most of them. They indeed think that without his efforts their own situation would not have improved at all. In particular, he created the village association which had to be formed in order to be eligible for external assistance.

In a context where the ability to deal with external sources of funding is concentrated in a small elite group, the bargaining strength of common people is inevitably limited, hence their ready acceptance of highly asymmetric patterns of distribution of programs' benefits. If the intervention of the elite results in an improvement of the predicament of the poor, however small is the improvement, the latter tend to be thankful to their leader(s): the new outcome represents a Pareto improvement over the previous situation and this is what matters after all. In the above example, it is thus revealing that the ordinary members of the association defended their leader on the ground that "everybody around him benefited from the project and, if he benefited [much] more than the others, it is understandable because he is the leader". They think it is highly unfair on the part of the foreign NGO to have withdrawn their support to the existing team and to have "humiliated their leader" by depriving him of all the logistical means (jeep, scooters, etc) previously put at his disposal.

As for the leader himself, he openly admitted (during a conciliatory meeting organized by the high commissioner of the province) to have used a significant portion of the money entrusted to him for his own personal benefit. Yet, he did not express any regret since it was his perceived right to appropriate

a large share of the funds. Did he not devote considerable energies to the setting up of the local organization and the mobilization of the local resources as required by the foreign NGO? By attempting to curb his power to allocate funds in the way he deemed fit, the latter exercised an intolerable measure of neo-colonialist pressure. This criticism was voiced in spite of the fact that the NGO paid him a comfortable salary to reward his organizing efforts.

Stories like this one could be easily multiplied and the authors personally went through several similar experiences while working with local groups, NGOs and associations through Europe-based aid agencies. What must be stressed is that the attitudes involved partake of the logic of clientelistic politics characteristic of the African continent. In the words of Chabal and Daloz, indeed, “For those at the very bottom of the social order, the material prosperity of their betters is not itself reprehensible so long as they too can benefit materially from their association with a patron linking them to the elites” (Chabal and Daloz, 1999: 42). As a result, abuses of power are tolerated so long as the patron is able to meet the demands made by his clients who are concerned above all with ensuring their daily livelihood.

It is ultimately because they overlook the genuine nature of the links between elites and commoners, rulers and ruled in Africa that international donor agencies overestimate the capacity of the participatory approach to deliver development gains more effectively and equitably.

### *Elite Capture and Development Brokers*

The problem of ‘elite capture’ is especially serious as donor agencies are enthusiastically rushing to adopt the participatory approach because they are eager to relieve poverty in the most disadvantaged countries and/or because they need rapid and visible results to persuade their constituencies or sponsors that the new strategy works well. Clearly, such urgency runs against the requirements of an effective CDD since the latter cannot succeed unless it is based on a genuine empowerment of the rural poor (see, e.g., Rahman 1993; Edwards and Hulme 1996). If the required time is not spent to ensure that the poor acquire real bargaining strength and organizational skills, ‘ownership’ of the projects by the beneficiary groups is most likely to remain an elusive objective, such as has been observed in the case of the World Bank’s Social Investment Funds (Narayan and Ebbe 1997; Tandler 2000: 16-17).

The perverse mechanism that risks undermining CDD is triggered by the temptation of donor agencies to skip the empowerment phase by asking intended beneficiaries to form groups or partner associations and to ‘elect’ leaders to direct them. As pointed out by Esman and Uphoff (1984: 249):

“The most prominent members are invariably selected and then given training and control over resources for the community, without any detailed and extended communication with the other members about objectives, rights, or duties. Creating

the groups through these leaders, in effect, establishes a power relationship that is open to abuse. The agency has little or no communication with the community except through these leaders. The more training and resources they are given, the more distance is created between leaders and members. The shortcut of trying to mobilize rural people from outside through leaders, rather than taking the time to gain direct understanding and support from members, is likely to be unproductive or even counterproductive, entrenching a privileged minority and discrediting the idea of group action for self-improvement” (Esman and Uphoff 1984 : 249).<sup>1</sup>

Confirming the prediction of Esman and Uphoff, several studies have concluded that the formation and training of village groups in community-based projects have the effect of encouraging the entry of wealthier and more educated people into leadership positions because of the attractiveness of outside funding (Gugerty and Kremer 1999, 2000; Rao and Ibanez 2001). In point of fact, a major problem confronted by the community development movement of the 1950s (which had been attempted by the Ford Foundation and US foreign assistance programs) lay in its inability to effectively counter the vested interests of local elites (Holdcroft 1984: 51). Being adept at representing their own interests as community concerns expressed in the light of project deliverables, local leaders often succeed in deluding the donors into thinking that their motivations are guided by the collective good (Mosse 2001; Harrison 2002; Ribot 1996, 2002). Their demands are replete with the sort of pleas and vocabulary that strongly appeal to the donors and, in order to create the appearance of participation, they may go as far as spending resources to build community centers, hold rallies, and initiate showcase labor-intensive activities (Conning and Kevane 2002: 383).

Traditional elites are not the only category of persons to benefit from the newly channeled resources since they are frequently involved in tactical alliances with educated persons and politicians operating outside the village domain. Urban elites may actually be responsible for initiating the process that deflects CDD from its intended purpose. Witness to it is the proliferation of national NGOs that are created at the initiative of educated unemployed individuals, politicians, or state employees who may have been laid off, or deprived of access to key logistical resources, as a result of structural adjustment measures. Acting as ‘development brokers’, political entrepreneurs have been quick to understand that the creation of an NGO has become one of the best means of procuring funds from the international community (Bierschenk, de Sardan, and Chauveau 2000). In the words of Chabal and Daloz (1999):

“...a large number of key political actors have now shifted their operations to the local level, which currently enjoys wide international favour and receives substantial

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<sup>1</sup> In the light of this diagnosis, Cernea’s contention that “NGOs insert themselves not as a third and different/independent actor, but as an emanation and representation of the community” (Cernea 1988: 10), appears almost surrealist.



assistance...[] a massive proliferation of NGOs ... is less the outcome of the increasing political weight of civil society than the consequence of the very pragmatic realization that resources are now largely channelled through NGOs... Indeed, NGOs are often nothing other than the new 'structures' with which Africans can seek to establish an instrumentally profitable position within the existing system of neo-patrimonialism... Above and beyond the new discourse of NGO ideology..., the political economy of foreign aid has not changed significantly. The use of NGO resources can today serve the strategic interests of the classical entrepreneurial Big Man just as well as access to state coffers did in the past... Furthermore, NGO-linked networks are inevitably intertwined with those emanating from the state" (Chabal and Daloz 1999 : 22-24, 105).

Thus, in the case of Benin, a West African country especially spoiled by the donors, we learn that local NGOs and associations, which are often "empty shells established with the sole purpose of capturing aid", have multiplied within a short period of time to number several thousands. Many others wait to receive the approval of the ministry of interior (Le Monde, 26 February 2001). In non-African countries also, NGOs often constitute "an opportunistic response of downsized bureaucrats, with no real participation or local empowerment" and, inevitably, program officers themselves become involved in the creation of community institutions (Conning and Kevane 2002: 383-84; see also Meyer 1995; Bebbington 1997; Gray 1999). In India, for example, we are told that "NGOs promoted by the politicians and contractors do not hesitate to bribe the officials and have a tendency to keep information to themselves. Therefore, they were far more successful in mobilizing the resources as compared to those NGOs with social commitment and values" (Rajasekhar and Biradar 2002: 18). Such risk of aid capture by development brokers is obviously high when self-conscious, organized local communities do not actually exist prior to the opening up of new development opportunities by state agencies or international donors (see Li 2001, for a well-documented illustration of this possibility), while the latter presume their existence on *a priori* grounds (McDermott 2001).

Of course, not all local leaders are opportunists ready to divert foreign aid from the intended beneficiaries. Several studies actually point to substantial variations in targeting effectiveness across villages (Ravallion 2000; Jalan and Ravallion forthcoming). Interestingly, intra-village inequality is often found to be inversely related to this effectiveness (Galasso and Ravallion forthcoming), confirming the prediction derived from Bardhan and Mookherjee's political economy model (see supra) and suggesting that the local elite tend to appropriate a larger share of the transfers in communities that are highly unequal to begin with.

Future evidence will settle the issue of the extent to which cases of embezzling behavior outweigh cases of leaders who are either unable (owing to sufficient empowerment of the grassroots) or unwilling (because they somehow share the ethical code of aid agencies) to embezzle aid funds. Results are likely

to vary from one region to another, depending on the strength of social movements, levels of rural literacy, etc. Yet, we believe that anecdotal evidence about the misdeeds of local elite is plentiful enough, at least in poor countries such as those of SubSaharan Africa, to justify a cautious attitude about the possible impact of the CDD approach. While thinking about mechanisms aimed at keeping fraudulent behavior in check, we will therefore assume that leaders do not share the values of foreign aid agencies and that the grassroots are not empowered to dispute their decisions.

### **3. Sequential and Conditional Disbursement Procedures in the Context of Decentralized Bilateral Relationships**

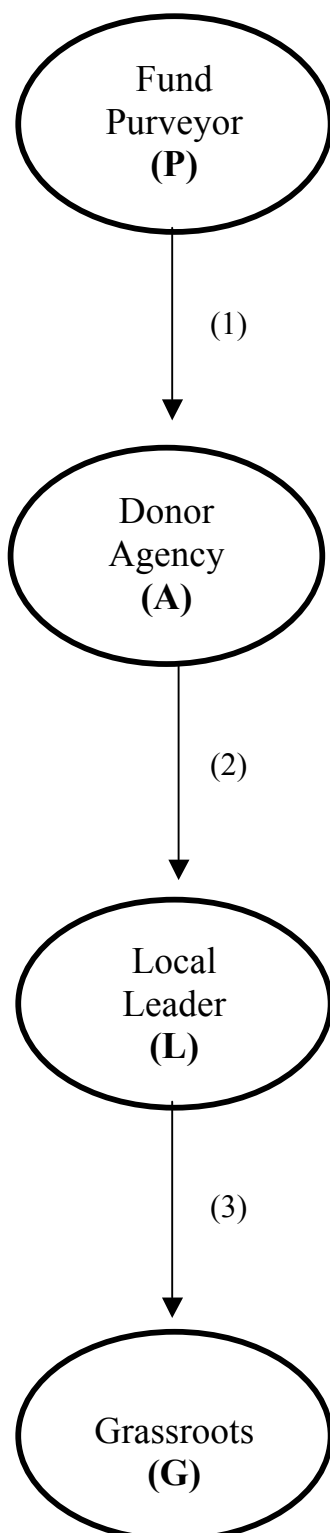
In order to analyze with the necessary rigour possible mechanisms for controlling elite capture as well as the influence of different factors on the extent of this phenomenon, I adopt a framework of inter-agency relationships that is directly inspired by the case study material presented in the first half of Section 2. Such a framework is, of course, a simplification of reality as it is based on stylized facts generalized from one particular sort of experiences. It comprises assumptions regarding both the setting of inter-agency interactions as well as the behaviour of the various agencies involved. Yet, I believe that the kind of story on which the following conceptualization is based is sufficiently credible to justify building the analysis upon it. In addition, the plausibility of the main results obtained will actually confirm the validity of the underlying theoretical model as a useful guide to understand some key determinants of the effectiveness of CDD for reaching poor people.

We have four sets of actors, namely the ultimate purveyors of funds (denoted by  $P$ ), such as the taxpayers or the general public in fund-raising campaigns, aid agencies (designated by  $A$ ), local leaders or intermediaries (designated by  $L$ ), and the grassroots (designated by  $G$ ) who are the intended beneficiaries of the aid transfers. To begin with, let us focus our attention on the last two steps in the sequence of aid disbursement, such as are represented by links (2) and (3) in Figure 1. In other words, we abstract away from the upper link between an aid agency and its ultimate fund purveyor. Following the logic of the CDD approach,  $A$  contemplates providing funds to a particular community or group of grassroots people,  $G$ , who do not have any alternative funding possibility.  $A$  therefore aims at reaching the grassroots as effectively as possible because it is its social purpose to do so. There is no direct contact between  $A$  and  $G$ , however, since  $A$  deals with a local leader or intermediary acting on behalf of the intended beneficiaries. Typically,  $L$  has organized  $G$  into a development association and has been 'elected' president.

What  $A$  can do, however, is to check whether  $L$  is genuinely supported by  $G$ , say because  $G$  can be asked to confirm that  $L$  is their authentic leader, whether

through a formal voting procedure or otherwise. As a matter of principle, *A* will not disburse funds through *L* unless it has received such confirmation. How the money is being shared within the group or community of grassroots is not observed by *A*, but *A* acts strategically taking the behavior of *L* into account while making its decision to support or not to support a given community. It is assumed that *L* wants to appropriate as much aid as possible subject to *G*'s approval and respect of local norms (see *infra*).

*Figure 1 : The Sequence of Aid Disbursement*



The strategic interactions between *L* and *G* can be essentially depicted as an ultimatum game. That is, *L* has the first move and makes an offer to *G* regarding the apportionment of the aid fund. Then, *G* has to say whether they accept the offer or not, knowing that its rejection would mean the collapse of the group consensus required to receive aid from *A*. In such a game, as is well-known, it is in the interest of the second mover (*G*) to accept the proposal made by the first mover (*L*), and the latter's (*L*'s) interest is therefore to set the share accruing to the former (*G*) at as low level as possible. This is so because *G* do not wield sufficient leverage to dispute the self-asserted right of *L* to appropriate a large share of the aid proceeds. In fact, as illustrated in the above story, *G* may not resent *L*'s disproportionate share in so far as their own situation has simultaneously improved.

Here is obviously a depressing result in view of the CDD's objectives. One would therefore like to conceive of some mechanism that could discipline local leaders in the absence of democratic governance within target groups or communities. The mechanism that comes immediately to the mind of economists is a stepwise process of aid transfer. Instead of releasing money in a single shot, aid funds would be disbursed in successive tranches, the disbursement of each of them being conditioned on *L*'s proper behavior regarding the use of previous tranches. Inherent in such a strategy is the recourse to a fraud detection technology without which local leaders would not be incited to behave. Detection is necessarily costly, yet it is in the interest of an aid agency to incur the related expenses since it can thereby hope to better achieve its own objective of poverty relief (fraud detection is incentive-compatible).

As we know from repeated game theory, however, as long as the duration of the game is finite, and no matter how high is the number of periods in the game, the equilibrium outcome will be the same as that obtaining in the one-period game (Kreps and Wilson 1982 ; Kreps 1990: 536-43). The effort, including the monitoring resources, spent by the aid agency over the successive stages of the project will be of no avail. Assuming that the local leaders are selfishly rational, they will embezzle funds from the very beginning and, knowing that, aid agencies should refrain from disbursing even the first tranche of money. True, if the aid agency interacts with communities over an infinite (or indeterminate) period of time, this awkward result can be avoided. But this is hardly a consoling thought inasmuch as CDD aid, in particular, is precisely aimed at making communities self-supporting after a certain period of time and the limited duration of the external intervention is better made clear from the beginning.

That being said, the assumption of strategic rationality underlying the above reasoning is questionable. This is not only because actors may not perfectly anticipate the future consequences of their actions and the reactions of others, or because they may entertain doubts about the rationality of the persons with whom they interact (in which case we know that even in a finitely repeated

game, cooperation may be established as an equilibrium), but also because some social norms may exist that have the effect of constraining rational calculations.

The existence of a norm of intertemporal fairness among  $G$  may thus make gradual, conditional disbursing of aid money effective even in the context of a finitely repeated interactions between  $A$  and  $L$ . The reason becomes evident if such a norm dictates that a division rule adopted during one period may not be changed at will by  $L$  during a later period, especially if the change is made at the expense of  $G$ . In other words,  $L$  is not allowed to reduce the share of aid transfers accruing to  $G$  over the successive stages of a project. In a two-period ‘CDD game’, he or she will thus be unable to strategically lower the share allotted to  $G$  between the first and the second rounds. As a result, since the granting of the second tranche is conditional upon  $L$ ’s proper behavior in the previous round and since the probability of fraud detection can be assumed to increase with the extent of the embezzlement, the portion granted by  $L$  to  $G$  will be the minimum share compatible with an acceptably low risk of detection at the end of the first round, and this share will be applied again during the second round. Clearly, the norm of intertemporal fairness serves the purpose of conferring a genuine bargaining power upon  $G$  during the second round.

This is not sufficient, however. For the mechanism to be effective,  $G$  must also be able to perfectly enforce  $L$ ’s promise to pay them the agreed share of the aid transfer once  $A$  has released the money. The story told in the previous section seems to attest that enforcement is not the real problem: even though their leader embezzled substantial amounts of aid money, villagers did not feel cheated and actually voted for the predatory leader again even after his malpractices had been fully revealed and confessed. It therefore appears that  $G$  must be empowered enough to enforce  $L$ ’s promise but not enough to actively debate the sharing rule with him (her). If  $G$  were not empowered enough even in the first sense, they would be doomed to be seriously exploited by  $L$  and there is not much that could be done to relieve their poverty until, through time-consuming conscientization and learning processes, they become better able to defend their rights and effectively participate in decision-making. On the other hand, if they were empowered enough in both senses, the sharing rule would be determined as the outcome of a bargaining process between  $L$  and  $G$ , and not by  $L$  only<sup>2</sup>.

In the two-period game-theoretical model proposed by Platteau and Gaspart (2003b),  $A$ , which is altruistic, decides the way to allocate the available aid budget between two successive periods, as well as the amount of monitoring expenses on which the effectiveness of fraud detection partly depends. Given the amounts of the first and second aid tranches as well as the size of the monitoring

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<sup>2</sup> Provided that the bargaining strength of  $G$  is strong enough, disciplining  $L$  with the help of a stage-process of aid disbursing will not have the effect of raising the share of aid money accruing to the intended beneficiaries. To achieve its objective, the aid agency could therefore rely on the bargaining strength of the latter. To be sure, some embezzlement would still occur, but the agency would not be able to do better by using such a stage-mechanism .

effort made by  $A$ ,  $L$  chooses the share of the aid transfers that he or she will hand over to  $G$ , among whom a norm of intertemporal fairness is known to prevail. While making its decisions,  $A$  faces the following trade-off. On the one hand,  $A$  would like to disburse as much money as possible during the first period because it is impatient to see the poverty of  $G$  alleviated. On the other hand,  $A$  wants to defer its disbursement of aid till the second period, since late payments serve to discipline  $L$ . Indeed, the higher the amount of the second tranche relative to that of the first, the more  $L$  is encouraged to use the aid transfers according to  $A$ 's prescriptions (that is, for the benefit of  $G$ ).<sup>3</sup>

One important result derived from the comparative-static of the model is the following: the more impatient the aid agency –that is, the more  $A$  discounts the benefits enjoyed by the target population during the second period–, the smaller the amount of the second aid tranche relative to that of the first tranche, and the lower the share accruing to  $G$ . (At the limit, if  $A$  is very impatient, the share accruing to  $G$  will tend to a value as low as that obtained under a one-shot disbursement procedure.) In other words, because the subjective cost of waiting is higher,  $A$  is less ready to use the leader-disciplining mechanism and to postpone disbursement of aid funds. As a consequence,  $L$  is less effectively induced to behave during the initial period, holding monitoring expenditures constant. At the new equilibrium, however, the amount of these expenditures is being increased. The net effect of these two opposite forces is nevertheless shown to be detrimental to  $G$ : the share appropriated by  $L$  increases and the absolute amount of aid money that will accrue to  $G$  if there is no detection of fraud by  $A$  is smaller. Bear in mind that monitoring expenses, which have been increased to substitute for the smaller use of the conditional mechanism of aid disbursement, are to be subtracted from the gross aid budget before transfers to  $G$  are made.

A second interesting comparative-static result is that the higher the cost of recycling aid funds –or the smaller the proportion of aid money earmarked for the second tranche that can be costlessly redirected to another group or association in the event of detected fraud in the initial project–, the lower the relative amount of the second aid tranche, the smaller the share accruing to  $G$ , and the lower the amount of aid money accruing to them in the absence of fraud detection. In other words, if it is more difficult to reallocate funds intended for a particular project, say, because of larger set-up costs, a donor agency will find deferment of their disbursement to be less attractive in equilibrium. As a result,  $L$  will be in a better position to appropriate the aid money. Aid agencies may therefore be tempted to avoid working in low density and remote areas where high set-up costs arising from long distances to be travelled, low education levels, etc, tend to reduce the effectiveness of their efforts to reach the poor.

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<sup>3</sup> Note that the amount granted under the first tranche must be positive so as to ensure that  $L$ 's behaviour can be effectively tested before making a decision about whether or not to disburse the second tranche.

To sum up, (1°) if  $A$  adopts a sequential, conditional disbursement procedure, and (2°) if  $G$  wield enough power to compel  $L$  both to stick to his (her) promises and to maintain over time the sharing rule followed in the initial round, then  $A$  is able to discipline  $L$  so as to make him (her) share aid money more or less equitably with the intended beneficiaries. This said, it must be emphasized that the above model implicitly assumes that  $A$  enjoys local monopoly power in the supply of aid funds. In point of fact, the problem gets complicated once aid agencies compete among themselves for access to target groups or communities. If perfect competition prevails in a context characterized by an abundant supply of aid funds,  $G$  will only get crumbs. This is the worst scenario: in their attempt to lure local leaders ‘representing’ communities, aid agencies are ready to drop their safeguards against the appetite of these leaders. Money is disbursed quickly without paying much attention to the manner in which it is shared between  $L$  and  $G$ .

A less pessimistic scenario arises if we consider, perhaps more realistically, that aid agencies do not produce a homogeneous service but differentiated, multi-attribute services comprising the total aid budget on offer, the timing of its disbursement over the successive tranches, and the monitoring effort. Monopolistic competition would then prevail amongst donor agencies and Platteau and Gaspart’s analytical framework could be adjusted accordingly. This would imply that an exit option now exists for  $L$ , and that two critical parameters of the model, namely  $A$ ’s intertemporal preference, and the cost of recycling aid funds, can be re-interpreted as possibly reflecting the intensity of prevailing competition among donor agencies. Regarding these latter two factors, the comparative static of the model indicates that acute competition is an unambiguously regrettable feature of the aid environment. As a matter of fact, by driving aid agencies to disburse funds quickly in order to prevent rival agencies from de-stabilizing a particular aid supply relationship, and by increasing the cost of recycling funds in the event of fraud detection, acute competition causes the share of aid funds appropriated by local intermediaries to increase at the expense of the intended beneficiaries. In other words, intermediaries can skilfully play on inter-agency competition since they know both that aid agencies are keen to find partners through whom to channel their aid budget and that this budget is more or less tied to the initially chosen project or community.

It is also evident that the emergence of exit options following the proliferation of aid agencies has the effect of raising the share that local leaders are allowed to appropriate at equilibrium, that is, the share that will deter them from pursuing a shifting strategy. A shifting strategy is a strategy whereby  $L$  does not care about staying with the same agency over the whole course of the aid project because he or she is ready, if caught cheating, to shift to another agency and start cheating again. What is at work here is a so-called bilateral reputation mechanism (BRM): if caught embezzling funds, a local leader is

punished only by the aid agency that has actually provided the funds embezzled. Note, however, that if exit options are too attractive, it will be impossible to discourage  $L$  from shifting partners continuously after stealing the whole amount of the first tranches of aid money. As a result, no agency will release money for CDD.

There are apparently two ways whereby the ‘elite capture’ problem can be mitigated. Reducing competition through concentration of aid supply in the hands of fewer agencies is the first way. Indeed, by diminishing the exit options available to local intermediaries, especially if aid agencies are geographically specialized, such concentration in the market for aid would have the same effect as a reduction in the aggregate supply of aid. The presence of scale economies in the technology of fraud detection when projects are geographically concentrated would constitute an additional advantage of this first solution. The second solution consists of a coordination mechanism whereby aid agencies would mutually inform each other about fraudulent acts committed by intermediaries. If such a device, known as a multilateral reputation mechanism (MRM), is apparently more feasible than reducing competition, it is not devoid of serious practical difficulties as will become evident from the discussion below.

#### **4. Multilateral Reputation Mechanisms**

##### *Circulation of fraud-related information among aid agencies*

The MRM has been documented by Greif (1989, 1994) with respect to relationships between traders (see also Platteau 2000: Chap. 6; Aoki 2001: Chap. 4). Applied to our problem, the mechanism would work as follows. Operating within a repeated-game framework, an aid agency would adopt the strategy whereby its grants money to a local leader, but only provided that he (she) is not known to have cheated another agency some time in the past. If money is thus disbursed and the benefiting leader is later found to have cheated the agency, the latter dutifully reports the fraud and communicates the name of the malevolent leader to the other members of the donor community. Before embezzling funds, a leader would thus be incited to think twice because by cheating today he or she would spoil his (her) reputation for future interactions with the whole donor community. The multilateral reputation strategy can be shown to be an equilibrium strategy. That is, if a leader expects every donor agency to adopt such a strategy, his (her) interest is to share the aid fund equitably among the intended project beneficiaries. Knowing that reaction, the interest of all aid agencies is to cling to the multilateral reputation strategy. Honest behaviour therefore gets established as a (Nash) equilibrium.



There are several problems with the MRM, however. The first one stems from the fact that the information conditions that must be fulfilled for it to work are extremely stringent: information must circulate perfectly between donor agencies. This is unlikely to be the case in reality, because they are in large numbers, scattered around the developed world, and very heterogeneous in terms of several key characteristics (size, ideology, methods, time horizon, etc.). These are hardly ideal conditions for a dense information network to exist.

Is the establishment of a private third party charged with centralizing information (as suggested, for example, in the Law Merchant system analyzed by Milgrom, North, and Weingast (1990) the solution to the problem caused by the costliness of generating and communicating information? Such a system can effectively work only if donors have an incentive to detect fraud and report fraudulent experiences to the third party, so that the black list of dubious intermediaries in its hand is exhaustive and regularly updated (otherwise, donors would not be induced to consult it). Yet, in so far as the detection and reporting of a fraud once it has occurred entails costs but brings no benefits to the individual agency which has been cheated, such an incentive does not exist. Unless, of course, aid agencies are so genuinely committed to the cause of poverty relief that they are not concerned about whether poverty is reduced by themselves or by another aid agency.

To create the adequate incentive, the third party should be able to exercise pressure on the detected fraudulent leader so as to make him (her) return the stolen money. A provision that unless an aid agency makes appropriate queries with the third party about the reliability of its current partner, it will not be entitled to use the system to obtain compensation would also make it in the interest of donors to query about past dealings of the partner-leader considered before disbursing money. As a result, so the theory goes, the threat against potential leaders would be effective and, if caught, a fraudulent leader would be prompted to comply with the third party by returning the money stolen (so that his name is removed from the black list). This said, Milgrom, North and Weingast have nevertheless shown that honesty will be established as a (symmetric sequential) equilibrium under the above mechanism only if a number of conditions are met, in particular, the cost of information query, the cost of appeal to the third party, and the cost for the latter to recover the stolen money from fraudulent local leaders ought not to be too high. Unfortunately, these assumptions are likely to be violated in the case under concern, especially because the headquarters of aid agencies are located at great distances from one another, and all kinds of information are costly to acquire, including evidence of fraud in the opaque context of alien cultural environments. The mechanism is therefore not self-enforcing.

A second, equally important problem lies in the fact that local leaders may not be actually concerned with preserving their reputation because their time horizon is short and they could be quite happy with running away with the money

stolen from one single project. In other words, the payoff from dishonest behaviour is so large compared to the payoff from honest behaviour that honesty cannot be induced at equilibrium.

*Rating of aid agencies by ultimate fund purveyors*

Up until now, one key actor has been missing from our discussion, namely the ultimate purveyors of funds from whom aid agencies obtain their financial resources. These ultimate fund-providers create a further link in the game (see link (1) in Figure 1), giving rise to a new space of strategic relationships. As far as disciplining of local leaders is concerned, their contribution may be positive or negative depending on the way they interact with aid agencies.

The latter possibility arises if aid agencies expect them to react adversely to news of embezzlement, for instance, through revocation of funds. In such circumstances, an aid organization has no incentive to report the acts of malfeasance detected in its projects. In the words of Alnoor Ebrahim (2003: 818), evaluations that reward successes while punishing failures “encourage NGOs to exaggerate successes, while discouraging them from revealing and closely scrutinizing their mistakes”. What we have here is a genuine Prisoner’s Dilemma: an aid agency refrains from disclosing cases of embezzlement because it entertains the hope that other agencies would candidly reveal their own bad experiences, or because it fears that, should it convey the information, others might not have done it and would then exploit the situation to their own advantage. That the above risk is real is evident from the atmosphere of secrecy that surrounds the activities of many donor organizations, including NGOs. This atmosphere of secrecy is obviously detrimental to the effective functioning of a multilateral reputation mechanism such as discussed above.

On the contrary, ultimate fund-purveyors can play a positive role if their understanding of the complexity of CDD processes is sophisticated enough to make them aware of the inevitability of failures. Honest aid agencies which openly admit of cases of cheating would then not be unfairly sanctioned to the benefit of more opportunistic ones. They could even be induced to reveal embezzlement cases if the disbursement and monitoring procedures used by aid agencies, as well as the duration of their CDD projects, were used by fund-providers as a yardstick upon which ratings of these agencies are based. In this perspective, self-reported cases of fraud detection could be considered as indirect evidence of the effectiveness of monitoring activities rather than as signs of failure. Not only are such characteristics rather easy to observe, but they also offer the advantage of not creating perverse incentives for the rated agencies.

The same cannot be said of other, more conventional criteria used to evaluate the work of aid agencies. Resorting to measures of outputs, such as improvements in the levels of living of the poor inside the communities chosen, is an ideal procedure but is likely to be too costly to be feasible, especially in the

case of NGOs with their typically diverse and long-term objectives (see Edwards and Hulme 1996; Ebrahim 2003). Moreover, such measures could introduce biases in the selection of communities by the rated agencies. As a matter of fact, the latter would be induced to choose communities in which poverty can be more easily reduced for other reasons than the prevailing power structure (e.g., easy accessibility).

The need for a proper evaluation of aid agencies is all the more pressing as, side by side with serious agencies, there exist careless organizations that do not implement sequential disbursement mechanisms with a view to disciplining local leaders. Such organizations tend to disburse funds quickly either because they do not have a proper understanding of the one-period game being thus played<sup>4</sup>, or because they are not single-mindedly pursuing the objective of poverty alleviation. (For example, in spite of all their pro-poor rhetoric, they are also concerned with reproducing themselves as job- and income-providing organizations in the West). Their presence further complicates the problem of 'elite capture' not only because it has the effect of increasing the exit options available to local intermediaries but also because it makes the establishment of a MRM among all donor agencies impossible. In fact, in the same way that "bad money chases good money", the operation of these opportunistic aid agencies risks driving 'good' agencies out of business or, else, it will force them to relax or altogether give up their gradual and conditional disbursement procedures. Indeed, if offered the choice, local leaders will normally prefer to work with 'bad' agencies. And if the latter are numerous enough, 'good' agencies will not be able to attract partner communities unless they soften their approach to aid disbursement.

A crucial difficulty remains. As a matter of fact, it is easier for central funding bureaucracies (such as the European Community or the Cooperation administrations of national governments) than for the scattered contributors to fund-raising campaigns organized by NGOs, to use the sort of evaluations envisaged above and to condition their financial support on the results of these evaluations. The crux of the problem lies in the fact that many donors in the general public have a poor understanding of development issues, partly as a result of distortions carried through the media and the deceiving messages conveyed by aid agencies themselves. There generally prevails the simplistic idea that failures in development projects are necessarily the outcome of incompetence and mismanagement on the part of the aid agency concerned, all the more so if many other agencies claim repeated successes.

Development aid is seen by many as a simple transfer of equipment and know how to those in need. The important role of institutional arrangements, power relations, and organizational learning tends to be underestimated.

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<sup>4</sup> Imperfect knowledge of the game typically arises when aid agencies tend to underestimate the leverage of the local leader within the group, or to overestimate his or her degree of altruism as a result of the leader's cunning ability to deceive them or of their own naivety.

Therefore, failing projects are seen as an anomaly. Such a lack of proper understanding of the complexity of community-based development processes is actually worrying in so far as leakages about even a few cases of failure may cause public opinion to easily swing from an attitude of general optimism to one of general pessimism and distrust in aid agencies. If that happens, all aid agencies will lose. To get out of this dangerous situation created by the versatility of public opinion, there is no other way than to educate the public about the real challenges and difficulties involved in CDD. Development education is clearly a public good. Aid agencies that free ride on this effort by claiming easy successes may, in the end, do it at their own peril.

### *Alternative accountability mechanisms*

It could be argued that, of late, there has been a tendency among some aid agencies to organize collectively with a view to ensuring better conduct in the profession (Edwards and Hulme 1996). In the United States, for example, a set of standards was developed in 1993 by Inter-Action, a membership association of US private voluntary organizations. “These standards lay out, in some detail, requirements concerning governance, organizational integrity, finances, public communication and disclosure, management and hiring practices, programs, and public policy involvement... Implementation of these standards is based on self-certification, subject to review by a Standards Committee which is also empowered to investigate complaints about noncompliance” (Ebrahim 2003 : 820). In Bangladesh and India, likewise, associations of development agencies have come to life which have adopted their own code of ethics. Other mechanisms of accountability are also being tried, such as social auditing, which involves “a shift from highly circumscribed evaluations of individual projects or programs to a broader assessment of the organization as a whole” (ibidem : 823; see also Zadek and Gatward 1996). External verification of social audits seems essential if they are to be an effective means of tempering exaggerated claims by non-profit organizations about their own achievements.

Problems with such endeavours ought not to be underestimated, however. As a matter of fact, codes of conduct are typically statements about general principles that are not easily translated into operational guidelines and enforceable standards. It is hard to deny that lack of satisfactory evaluative mechanisms is a serious drawback when it comes to NGO accountability, and that indicators of the quality of their work are very rare, especially if their main aim is the empowerment of the poor (Edwards and Hulme 1996: 11). This situation often arises because it is easier to agree on general ideas than to converge on strict and externally verifiable rules. And if a satisfactory agreement is eventually reached, it is most likely adopted by only a restricted number of operating agencies. Devising and enforcing NGO codes at an international level appear to be fraught with particularly awkward problems of coordination. Note

also that, as pointed out above in connection with the MRM, uncertainty regarding the impact of social audits on the ultimate purveyors of aid funds is bound to make many NGOs reluctant to adopt them even though they may agree on their necessity in principle.

*Fraud detection and impact assessment studies*

It is evident from the whole analysis proposed in this paper that mechanisms of fraud detection have a key role to play in the disciplining of local leaders acting on behalf of target communities. Whether in the framework of bilateral reputation mechanisms based on sequential and conditional disbursement of aid money, or in the framework of multilateral reputation mechanisms based on good dissemination of information among aid agencies, local leaders cannot be induced to behave if the probability of their being caught and thereafter punished is too low owing to ineffective fraud detection. Platteau and Gaspart (2003b) have shown rigorously that the share of funds reaching the grassroots decreases with the ability of an aid agency to detect fraud. Moreover, a low intrinsic ability to detect fraud (because the fraud-detection technology used is rather inefficient) can be compensated only partly by the positive effect of an increase in monitoring expenditures. Bear in mind that the larger such expenditures the smaller the net amount of aid funds available for the project's objectives proper. It is therefore essential to devise and put into use satisfactory procedures aimed at assessing the extent to which the grassroots have benefited from CDD projects.

For well-focused interventions the outputs of which are easily observable (think, for example, of projects intended for distributing school manuals to rural pupils), such assessment does not raise many problems and a careful impact study can show whether the aid transfer has reached the intended beneficiaries. Yet, in the case of more complex interventions, it may be more difficult to arrive at a sound judgment about the real destination of aid resources. There are actually many subtle ways in which astute local leaders can divert funds destined for a collective project and to unmask these ways may prove quite tricky. Usually, the truth cannot emerge unless villagers are willing to speak out to agency's mission staff or to external evaluators. It is here that the main source of the problem lies. In point of fact, it is often in the villagers' best interest to remain silent about malpractices committed by the rural elite because, being in a dependent position, they have more to lose than to gain from revealing fraud.

Indeed, whereas they are involved in continuous long-term relationships (they play infinitely repeated games in various walks of their ordinary life) with their local patrons, the duration of an external intervention is necessarily of limited duration. In other words, the long-term cost of antagonizing a patron who can punish a non-compliant client in diverse ways is likely to exceed by a wide margin the short-term benefit of revealing facts about the sharing of aid

proceeds. It is a rule that external donors are considered by local beneficiaries as ephemeral actors who carry much less weight than powerful local figures.

Note that, if aid transfers to communities could be anchored in a framework of fiscal decentralization, such as is envisaged in many programs of decentralized development, there would be an endless round of disbursement periods and the situation would be akin to that of an infinitely repeated game. The outcome of the sort of cost-benefit calculus discussed above could then be reversed, but only if local patrons are not too active in other sectors of community life than the one affected by the money transfers.

As the case study material presented in the first part of Section 2 attests, factional competition within rural communities may incite some people to reveal facts of malfeasance if they have been committed by rival leadership figures or patrons. Confronted with the threat of such revelations, local leaders could thus be hopefully disciplined in their handling of CDD funds. This said, one must also reckon with the negative externalities of a mechanism that fosters intra-elite competition rather than cooperation when collective endeavours are necessary for local development. There is clearly a dilemma here: not-too-good relations between local leaders are necessary for effective fraud detection yet they are a liability threatening collective action at village or community level.

## 5. Conclusion

There are three main conclusions emerging from the above analysis. First, ‘elite capture’ is a serious problem for the CDD approach, at least in all the areas where the poor are not empowered enough to withstand the pressures and influence of the local elite. It must therefore be addressed explicitly lest this approach should yield disappointing results in the sense of proving unable to increase the effectiveness of aid absorption and to better reach the poor than past approaches to development.

Second, sequential and conditional release of aid funds is a useful approach to participatory development since it can help discipline local leaders or intermediaries. It obviously implies that fraud can be possibly detected *ex post*, which requires aid agencies to devote substantial resources to project monitoring, thereby substituting external control for missing internal democratic governance. If things go well, one might entertain the hope that in the process the poor will gradually learn to better defend their rights, monitor the actions of their leaders, compel them to enforce their promises and, hopefully, spawn new, alternative leadership figures able to compete with the existing elite.

In so far as it is unrealistic to assume that all aid agencies will rigorously apply a leader-disciplining mechanism, if only because some of them are opportunistic or ill-informed and inexperienced about field realities, coordination mechanisms are required at the level of either aid agencies or

ultimate purveyors of funds. And since coordination mechanisms, such as multilateral reputation mechanisms, are difficult to establish and implement effectively amongst aid agencies, due mainly to their large number and great heterogeneity, disciplining local leaders in the framework of CDD projects will require action on the part of the ultimate purveyors of funds. To send the right signal to aid operators, fund providers should carefully avoid to systematically reward successes and punish failures. As a matter of fact, detection of aid embezzlement may reveal a high degree of competence and rigor on the part of the aid agency involved. Since the general public provides substantial aid resources through various fund-raising campaigns organized by NGOs, it is also important that the population in donor countries be conscientized about the inevitable difficulties of external aid interventions in general, and the pitfalls of CDD projects in particular.

Third, and this directly follows from the above two conclusions, the problem as to how best to detect fraud in CDD projects is a critical dimension of the CDD approach and, unfortunately, one which has received only scant attention so far. The potential role of impact assessment studies in this regard ought to be thought over. More precisely, given the difficulty of getting people speak about the misdeeds of local elites, it is important to devise questions and measurements that are susceptible of revealing fraudulent acts in a roundabout manner. The natural way of doing this is by measuring what the poor got from a CDD project and then check out whether this more or less matches expectations derived from the project's design. In the case of simple interventions focused on easily observable outcomes, this should not be too difficult. In more complex cases, however, even to assess the benefits that the poor derived from a specific project may be an arduous task, if only because facts may be distorted in order to keep wrongdoings of the local elite away from sight. The issue is obviously a difficult one, all the more so if detection of fraud is to occur in the course of a project's cycle before the next tranche of money is being disbursed. For all these reasons, it is essential that best practices are well disseminated among the agencies concerned.

One thing is certain: evaluations need to go much beyond "bureaucratic" reports presenting financial accounts and "physical" achievements of CDD projects, such as they are required by many funding organizations (such as the European Commission and bilateral aid agencies). As a matter of fact, this kind of reporting tends precisely to encourage and allow distorted presentations of achievements that emphasize successes and minimize failures.

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