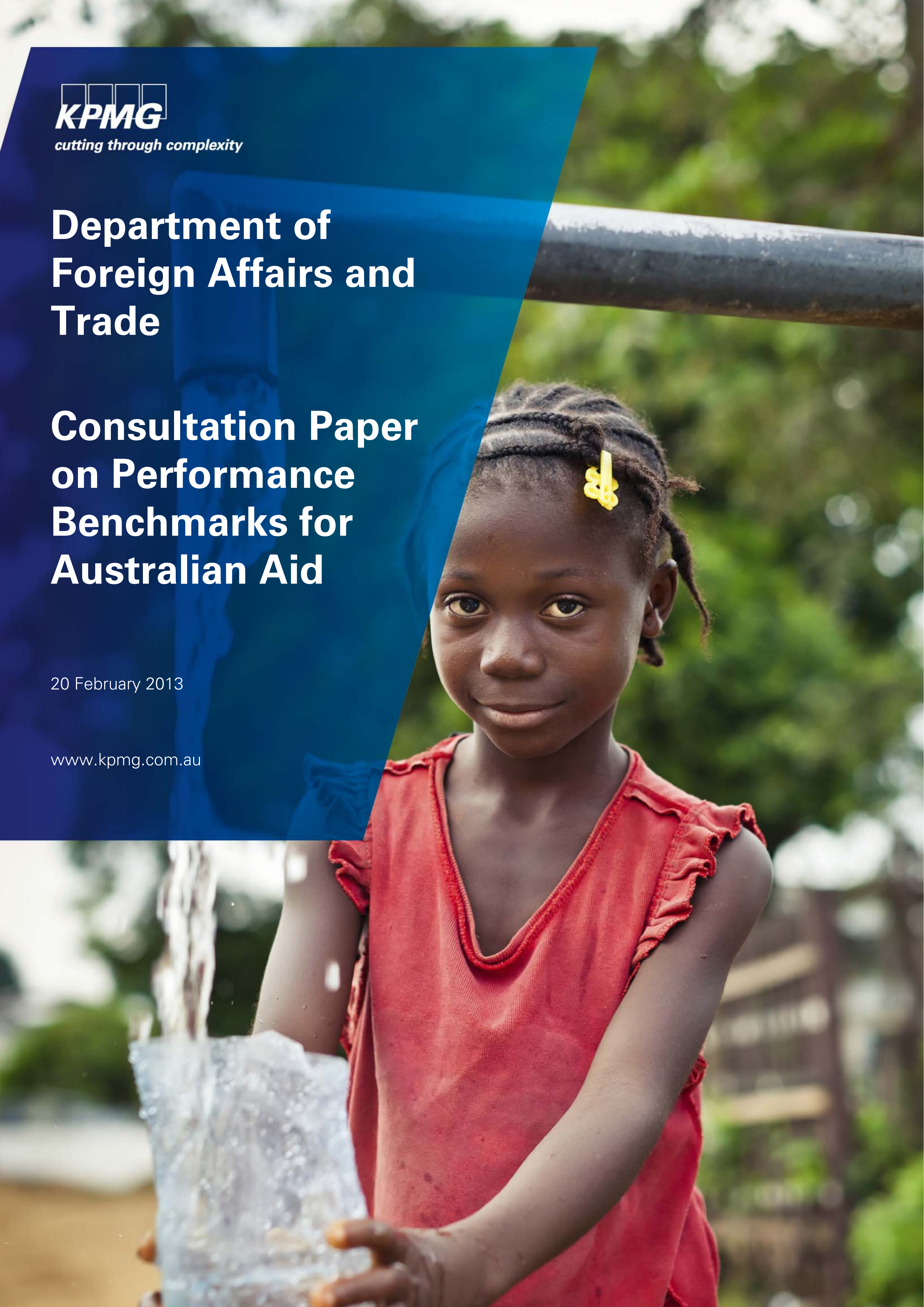

KPMG
cutting through complexity

Department of Foreign Affairs and Trade

Consultation Paper on Performance Benchmarks for Australian Aid

20 February 2013

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Mr Brett Mason
Parliamentary Secretary
Department of Foreign Affairs and Trade
By email – development.results@dfat.com.au

20 February 2014

Dear Mr Mason,

Consultation Paper on Performance Benchmarks for Australian Aid

KPMG wishes to thank the Parliamentary Secretary to the Minister for Foreign Affairs for his kind invitation to provide our informal observations on the DFAT Performance Benchmarks for Australian Aid Consultation Paper. KPMG commends the Australian Government's commitment to ensuring that Australian Aid is delivered effectively and efficiently. We support the intent to ensure that Aid is tied to measurable outcomes and that the utmost rigour with regards to the measurement of the effectiveness of Australia's Aid Program is important in ensuring integrity and providing Australian taxpayers and partner countries greater levels of confidence.

KPMG is committed to working together with community partners to help solve many of the serious problems confronting the world we all share. We try to do business in harmony with our natural environment.

In today's tight fiscal climate, the developing world faces a number of critical challenges, including:

- Strengthening sustainable capacity that supports clearly-defined outcomes; and
- Enhancing government accountability towards their citizens for the expenditure of each and every dollar through greater levels of transparency.

Within Australia, KPMG have a proud history of assisting the Australian Government deliver its strategic objectives for Australia's Overseas Aid Program, delivering a wide-array of high quality professional services to both AusAID and DFAT.

Internationally, KPMG's International Development Assistance Services (IDAS) professionals are on the front lines of the developing world. We work closely with emerging market stakeholders – government, civil society and the private sector – to create sustainable change and effective, accountable service delivery.

One of the ways KPMG adds value to our diverse clients is through the IDAS Global Centre of Excellence (COE), which brings together subject matter experts and highly experienced professionals from around the world to share best practices, knowledge and experience with our clients and development partners. Through the COE, KPMG's professionals are able to work across geographies to leverage the insights from professionals with a track record of providing development services across Africa, Asia, Eastern Europe, the Middle East and the Americas, and the insight needed to turn knowledge into value for our clients and the citizens they serve.

We would welcome the opportunity to discuss any aspects of our response with either Ministerial or Departmental officials and look forward to continuing to assist the Australian Government achieve both effectiveness, efficiency and a strong culture of accountability within Australia's Aid program.

Yours Sincerely,

Tony Hof
Partner

Introduction

The DFAT consultation paper is aligned to the stated policy position of the Abbott Government focusing on the theme of linking performance of the Australian Aid program to Aid allocations at multiple levels through the introduction of 'performance benchmarks'. The objectives of the benchmarks are "*to improve the accountability of the Aid program, link performance with funding, and integrate the Aid program with Australia's broader foreign and trade policies*". The Consultation Paper considers the usage of benchmarks targeted across a range of different levels and contexts, including but not limited to:

- The development program as a whole;
- Individual sectoral and thematic programs;
- Country programs;
- Multilateral Institutions;
- NGOs;
- Consultants/Implementing Organisations/Partner Governments; and
- Projects.

Our response begins with some of the more specific issues most relevant to DFAT. We have then included some general observations about the case for using performance benchmarks and practical considerations. We have made the assumption that the performance benchmarking being reviewed is restricted to the Australian Aid program rather than between Australian programs and those of other countries. The latter would require a common approach to performance benchmarking, which is beyond the scope of our observations.

Performance Indicators and Benchmarks for Country Allocation and Selection

As noted previously, country allocation is informed by a range of factors besides performance. In addition to those listed above, political and historical relationships play a major role, as does geographical location. For example, Australia allocates a significant proportion of its Aid budget to countries located in the Pacific and South East Asia.

International organisations, such as the World Bank, utilise a number of indicators to determine a country's eligibility for development assistance. This includes financial performance, risk, governance and corruption indicators. Once a country has been deemed eligible a detailed set of parameters are used to establish the funding window (base case and maximum).

A notable experiment in performance based selectivity was adopted by the Millennium Challenge Corporation of the US which set a range of eligibility requirements for a program through Compact agreements. The lessons learnt from the Compact evaluations may be useful for the Australian Government to validate the prospective approach as it is further developed. As an example, one criticism was the slow pace of disbursement in the initial years of the program as it takes time to implement this type of approach including the establishment of a new institution and associated programs.

A further challenge related to this area, is the question of country ownership, as set out within the framework of mutual accountability, following the Paris Agenda. Country performance indicators should not be imposed on recipients, but should be mutually owned. Ideally, they would measure the performance of the donor and the recipient and be jointly monitored leading to further complexity.

Finally, another important area for consideration by the Australian Government is the extent to which Australian foreign and trade policy plays a role in country allocation and the design of performance benchmarks. We acknowledge that the Australian Government has recognised that the focus for Australia's future Aid program will integrate the Aid program with Australia's broader foreign and trade policies. In order to establish meaningful benchmarks and performance indicators that measure outcomes through a diverse set of perspectives such as these, care will be required to strike a balance between pragmatism and complexity to ensure the indicators are robust. Should the Australian Government fail to strike the appropriate balance in the performance framework, it may not be possible to ascertain the effectiveness of Aid or the contribution to foreign and trade policy in a rigorous manner.

Performance Indicators for Programs

It is relatively conventional for governments to establish performance indicators for specific programs. One example is the use of budget support where there is a performance contract which triggers disbursements of Aid. There is extensive literature on the risks and benefits of this approach to assistance. Concerns have been expressed about the difficulties associated with coercive conditionality, which can represent an abuse of power by donor governments, undermining the legitimacy of the elected recipient government. Aid may become less predictable if linked to performance. Conditionality often focuses on policies, whereas the outcomes are material (recipients should arguably be free to decide how to achieve an outcome and donors should care about outcomes, not how they are achieved).

Monitoring and negotiating conditions has a high transaction cost so there should be a constrained use of conditions. In relation to budget support, we observe that the UK eschewed minimum standards to qualify for budget support in favour of an assessment of risk vs. benefit, thus allowing budget support to be provided in Sierra Leone and initially fragile Rwanda, but not in Kenya for example, which has relatively stronger systems (albeit also with high levels of corruption). This illustrates that eligibility based on past performance may not always be the preferred approach. Risks and rewards have to be assessed with rigour to achieve the best outcomes.

Globally, the development of new approaches to Aid allocation are emerging, including where the recipient is rewarded for the delivery of specific outputs with transparent payments. This approach is observed in the development of Output Based Aid, and more recently the innovation of Development Impact Bonds which have the potential to engage philanthropic donors. These approaches help to effectively mitigate or in some cases eliminate the risks for donors. Such contractual arrangements are not however suited for all types of issues and assistance. They work best where outputs are easily measured and unambiguous.

Regardless of the design mode selected for an Aid Program, it is important that programs are subject to independent review and assessment and oversight, providing ministers, bureaucrats and taxpayers authoritative evidence on value for money and results with which to hold the executive to account more effectively. KPMG provides consultancy support to the Independent Commission on Aid Impact in the United Kingdom. The Independent Commission adopts a standardised framework to assess the objectives, delivery, impact and learnings from different projects, programs, and institutional relationships. Whilst not specifically linked to allocation decisions, the reviews can lead to decisions to terminate programs or replicate them and identify valuable lessons to strengthen the design and delivery of future programs.

Performance Indicators for Multilateral Aid

Within a portfolio of contributions to multilateral agencies, there is some scope to make informed choices about allocations based on the assessment of institutional effectiveness. The UK for example has adopted this approach in the Multilateral Aid Review (MAR) update (2013). Following the 2011 MAR several organisations had their support from the UK terminated whilst others were flagged for potential termination if they failed to improve. The organisations were assessed against a fairly broad range of criteria, and it would be possible for the Australian Government to adopt a similar approach, varying the criteria to meet their own priorities.

Payments for multilateral contributions are either contractual as part of a treaty, or voluntary in support of a particular multilateral trust fund or project. It is within the control of the donor when making voluntary contributions to adjust the project expenditure. Contributions which are negotiated or related to a treaty may be changed periodically but will affect the donors influence and shareholding in some institutions. Development agencies can drive engagement around performance across the whole institution, for example through the SDG process with the UN, with the IDA replenishment discussions with the World Bank etc. Further consideration should be awarded as to whether this approach is more effective than seeking to impose performance related contracts around the donor's own individual contribution.

Performance Indicators for Non Government Organisation's (NGO's) and Civil Society Organisation's (CSO's)

Support to NGOs/CSOs is generally allocated for specific projects and programs and linking payments to the outputs and outcomes delivered by the organisation are also relatively prevalent. Where institutional or programmatic support is provided to an NGO or CSO, it is important to have a clear performance contract with the organisation that clearly articulates responsibilities. This approach has been adopted within the UK partnership arrangements/agreements (PPAs). In some cases, it has been useful for initial due diligence to be commissioned independently to assess whether the organisation is credible, has robust financial and administrative procedures, and appropriate governance arrangements. Consultants can be useful in conducting these assessments. KPMG has provided due diligence support for the UK's Civil Society Department support.

Project Performance

Most reputable development institutions have fairly well developed approaches to project lifecycle management based on performance indicators. The UK introduced the Logical Framework approach more than two decades ago. More recently steps were taken to improve the quantification and quality of the indicators. Procedures were strengthened to improve the quality of business cases for approval of new projects. As has been the case with AusAID, projects require an evidence based theory of change. Once approved, projects are subject to an annual performance review and projects which score badly are subject to improvement measures or termination. The scores are tracked at the portfolio or country program level which provides a basis on which to assess the performance of the program management team as well as the recipient country.

Increasingly, Aid agencies, including the UK Department of International Development (DFID) are appointing consultants to monitor and evaluate projects separately from the consultants who are implementing the project. For example, KPMG is the evaluation manager for DFID's Trade Advocacy Fund. The contract included refining the Theory of Change, developing the Evaluation Framework, regular annual reviews, a mid-term evaluation, and a final evaluation. With the launch of the Independent Commission on Aid Impact, DFID's evaluation department has focused on building the internal capacity of DFID spending departments to undertake evaluations.

Project level performance indicators are contracts which are particularly appropriate when working with the private sector, for example through public private partnerships. There is a wide body of experience and literature on better practices with regards to this area, although the challenges can be formidable where markets are weak and data is either unavailable, difficult to track, or where the risks are not well understood. As a result, the benefits from many of these arrangements has been somewhat limited in leveraging private sector capability through Aid programs in low income countries and fragile states in particular.

New technology will open the opportunity for innovation in project performance, for example using data generated by mobile devices, geospatial and big data is likely to help generate greater insights for stakeholders into the effectiveness and efficient delivery of Aid. As the Australian Government commences the design of the performance benchmarks, a strong consideration of the capability of both existing and new technologies should be made to ensure that the performance metrics can be automated where possible and collated in the most cost effective manner. Again, KPMG have significant recent experience of working with

AusAID before its integration with DFAT in examining the information and data that is currently generated through the information systems that support the delivery of Australia's Aid program.

Building a Coherent System of Performance Measurement

Performance measurement is an invaluable tool and approach for development effectiveness. It is an approach which can be built in at all levels, from individual projects to sectoral programs, country programs, and multilateral contributions. In some cases the approach can be made to be coherent for example by aggregating project level data to set targets for a portfolio or country program. In other cases the frameworks can operate independently in their respective contexts.

It should be appreciated however, that there is a complex range of factors besides performance that will and should determine allocations. Reacting to failures of performance will be a complex judgement that could include additional inputs, revision of targets, suspension of further Aid, or changes in management.

We note that the collection of performance data is not new for DFAT with the majority of Regional, Country and Thematic strategies including an annex that describes the performance assessment framework relevant to the specific area. As noted previously, the collection of meaningful data from some countries is limited by the quality and the availability of data, resulting in less than robust performance measurements.

When examining some of the performance measurement frameworks published previously by AusAID, particularly at the country level, we make the observation that whilst the frameworks describe "how we will know if we have achieved our objectives", some of the measurement criteria appear to be difficult to measure in a robust manner. For example, the performance measurement framework for the Australia, Laos Development Cooperation Strategy 2009-2015 includes measures such as "strengthened management capacity" and "enhanced private sector competitiveness". In order to confirm that these measures have been met there would need to be a baseline to measure the progress against. When the measurements are more granular at the country level, the data required to report against is drawn from such a varied array of sources that under the current performance management framework, there appears to be significant levels of effort required to collate and verify the data. Whilst it is unlikely that there will be a simple solution to the design of a coherent performance management framework, there are significant opportunities available to the Australian Government to design consistent measurement criteria that can be applied across the regional, thematic and country levels that are cost effective to manage whilst meeting the stated outcomes with regards to transparency and accountability.

General Observations on Performance Benchmarks for Aid Allocation

Performance as a Component of the Aid Allocation Model

The basis for allocating Aid between countries and programs is a complex subject, but it is important to appreciate that Aid allocation needs to take into account of a number of factors, with performance being but one. As an example of how jurisdictions other than Australia have approached this issue, DFID has used an Aid allocation model to inform country allocations, based on the work of Collier and Dollar. The underlying insight is that there is an optimal allocation of Aid which would maximise the overall impact of an Aid program in reducing poverty. Factors incorporated within the DFID model include:

- **Poverty levels** - poorer countries should be allocated more Aid than richer countries. The UK used Gross National Product per capita as a proxy;
- **Population** - larger countries should be given more Aid than smaller countries;
- **Other donors Aid -** neglected countries should be given more Aid than over-aided countries; and

- **Aid effectiveness** - countries which are effective at using Aid should get more than those which are less effective. The UK used the World Bank's International Development Association (IDA) Resource Allocation Index as a proxy (previously known as CPIA).

It is important to note that whilst performance is a key component in informing the decisions relating to Aid allocation, other components should be considered alongside importance to deliver effective and efficient Aid outcomes.

Aid Predictability

A second practical consideration is that the value of Aid to the recipient can be diminished if Aid volumes are unpredictable. This is especially the case for budgetary planning, where the recipient government needs to know in advance how much Aid is going to be provided if it is to be included in the government budget and program into government activities. If Aid is going to be reduced or suspended based on failure to achieve performance benchmarks, by definition that Aid is contingent, and hence less than fully predictable. We note that, whilst predictability is reduced, as the *Independent Review of Aid Effectiveness* (April 2011) stated in its recommendations, "Budget appropriations each year should be contingent on things going to plan and existing monies being spent effectively". Achieving a balance between predictability and linkages to performance is again, not a simple matter, however, squaring the circle of predictability with performance linkage may be addressed by having no link to performance benchmarks for the current year, with adjustments to Aid in future years on a cyclical basis, to provide and accurate budgetary view that takes into account performance adjustments.

Performance Measurement

Another practical challenge around the use of performance frameworks and key performance indicators is around measurement. Particularly if linked to a performance contract, indicators need to be timely, unambiguous, and not open to bias by interested parties. Control systems can be designed and implemented to reduce these risks, for example by appointing 3rd party independent agents to collect or quality-assure data. However, there are a number of challenges which include:

- **Relatively intangible objectives -** Some outputs and outcomes are inherently more difficult to measure than others. Reliance on performance contracts may tend to focus the attention on components which are easy to measure, rather than components which are difficult to measure, but which may nevertheless be material to the resultant outcomes. If too simplistic, targets and indicators can be counter-productive, introducing cost and complexity through the establishment and operation of measurement mechanisms that deliver low levels of value;

- **Attribution** - Performance indicators may capture a mixture of the effectiveness of the agents responsible for program and project delivery, and external factors. For example, a program focusing on improving agriculture and nutrition could be influenced by additional factors including the climate during the duration of the program. Therefore, contractual arrangements based on performance need to consider the inclusion of external factors that could influence a program's outcomes; and

- **Fragile States -** Poverty in fragile states has been largely persistent, meriting increasing volumes and proportions of Aid from donor countries. These countries in many cases also have the least developed statistical systems. Data may be absent or lagging several years. Management systems and processes are often weak and corruption can be endemic. All of these factors point to the need to develop specific indicators for fragile and least developed states. For example, in a fragile state the time to complete, cost per unit, security and other costs factors are likely to be higher than in other countries, and the likelihood of setbacks due to considerations outside the control of the program is often much greater. Any performance standards introduced at the program level need to take these challenges into account.

There is a strong case that at the program, project, or partner level, performance-based funding can promote funding decisions based on transparent assessments of results against time-bound targets. Performance-based funding promotes accountability for results by providing incentives for recipients to use funds efficiently and effectively. However, the success of a performance-based funding model is largely dependent on the ability of the organisation to:

- Modify a performance-based funding model to align with the organisation's culture, critical needs, goals, and priorities;
- Recognise an organisation's definitions of success and failure and the values of each to the organisation and its stakeholders;
- Utilise a risk-based approach to ensure an appropriate level of measurement aligned to the size, scope and complexity of the programs;
- Employ a system of incentives to the performance-based funding model that rewards for innovation rather than imposing penalties;
- Understand the impact of the program or lack of the program on society and ultimate beneficiaries and stakeholders of the program; and
- Adapt the results to new situations, circumstances, or unexpected results to move programs forward in a positive way.

Along with each of these points, we would emphasise that a key turning point in many organisations' adoption of a performance-based funding model is to recognise and accept that failure is necessary for success. Learning from failed projects/programs often leads to greater advances in future projects/programs than could have been achieved without the failure. The ability of the organisation to take this tenet as an important component of any performance based funding program and use this in working with implementers and stakeholders to determine how to develop and fund better future programs is key to its success.

Significant planning at the outset of any program or project is critical to identify not only the expectations for success, but also how the expectations will be measured, how to interpret the measurements, what portions of a successful program may be scalable, what factors or considerations may influence scalability, what are the possible challenges or obstacles, what are the potential lessons learnt from failure, what other complimentary programs are delivered, and so on.

Designing the measurement criteria that underpins the delivery of a program and the definition of key success factors should be determined at the outset, taking into account:

- What data is readily available? For what times periods is it readily available?
- Can baseline data be determined? Is the baseline data reasonable?
- Is the data reliable? Has the validity of the data been determined?
- How is the data measured? Is it precise or subjective?
- What are the components? Where do the components come from?
- Is the data subject to manipulation?
- Are there multiple ways to interpret the data?
- Are there consistent measurements already adopted by the development or other sectors relating to similar projects/programs/components?
- What global benchmarking data is available?
- Is the data coupled directly or indirectly to Aid funding?

Similarly, there is a recognised need to evaluate the overall impact of all programs and initiatives on a cumulative level. This level of assessment is more likely to be beneficial to the organisation based upon risk-based factors applicable to opportunity, availability of resources, and reputational/political considerations.

Establishing Targets

In principle, targets can be related to globally agreed targets such as the Millennium Development Goals (MDG's) and the emerging Sustainable Development Goals (SDG's). These can be used both to monitor progress at country and program level and inform multilateral contributions or as high-level outputs that specific programs are required to contribute to. One challenge of this approach centres on the aggregation of data, for example when a small number of very large countries can show the indicator to be on track when many individual countries and sub-groups are failing to make progress. Further, it is important to demonstrate caution when using aggregated data to link Aid outcomes to foreign policy objectives. At a foreign policy level the data may demonstrate pro-poor economic growth for disadvantaged communities. However, much of the GDP data at country level may not be disaggregated to a level that would adequately support this hypothesis.

Where key performance indicators are linked to allocation decisions, another challenge centres on how ambitious or aspirational the targets should be. If the targets are too unreasonable, the recipient or program will be penalised even though the targets may have been unrealistic from the outset. Conversely, if the targets are too easy to achieve, there is limited pressure on performance and the program can achieve the outcomes with inefficiencies in place. Issues with targets are further illustrated through the experience with the MDG's, which have proved overly ambitious for many countries, but relatively achievable for others, who have exceeded targets with minimal outside help. For the most part, targets should be informed by historical trend data drawn from achievements in the same environment to develop the most appropriate targets; however, in many cases there may be very limited trend data available on which to form the basis of optimised targets. Some issues are less easy to measure and target, but remain important, such as governance or increasingly, climate change resilience.

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