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**Post-Conflict Recovery:  
Resource Mobilization and Peacebuilding**

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# **Post-Conflict Recovery: Resource Mobilization and Peacebuilding**

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## **Abstract**

Societies embarked on the fragile transition from war to peace face enormous economic, social, and political challenges. In attempting to support this transition, the international community often provides substantial amounts of external assistance. This aid can play an important and constructive role in meeting pressing social needs and building a durable peace, but it would be naïve to assume either that positive effects are the automatic result of good intentions or that donors are motivated entirely by the objective of peacebuilding. This paper reviews evidence on the impact of aid in “post-conflict” settings and offers suggestions for making aid more effective in supporting efforts to build a durable peace. Part I discusses how economic assistance and conditionalities can be realigned to better serve peacebuilding objectives. Part II considers the other side of the coin: how peacekeeping operations and peacebuilding assistance can better support economic recovery, in particular by helping to build state fiscal capacities. Finally, Part III examines the interests and incentive structures that shape the behavior of aid donors, suggesting that their actions can be part of the problem as well as part of the solution.

*Key words:* Peacebuilding; post-conflict reconstruction; conditionality; revenue mobilization; horizontal equity; polarization; foreign aid.

*JEL codes:* F35, F53, H2, O19, O23.

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## **Introduction**

Wartorn societies embarked on the fragile transition from violent conflict to a durable peace face enormous economic, social, and political challenges. In attempting to support this transition, the international community often provides substantial amounts of external assistance. This assistance can play an important and constructive role in meeting pressing social needs and building a durable peace, but it would be naïve to assume either that positive effects are the automatic result of good intentions or that donors are motivated entirely by the objective of peacebuilding. This paper reviews evidence on the impact of aid in what are optimistically called “post-conflict” settings, and offers some thoughts as to how aid can more effectively support efforts to build a durable peace.

The paper has three parts:

Part I, “Aid for Peace,” examines the interaction between the twin objectives of building peace and fostering economic recovery. The two objectives are mutually supportive: without a successful transition from war to peace, economic recovery is unlikely or impossible; and without economic recovery, a successful war-to-peace transition is less probable. Yet it would be a mistake to infer from this complementarity that political efforts to implement peace accords and economic efforts to promote reconstruction and recovery can proceed along separate tracks, oblivious of each other and secure in the knowledge that each assists the other. Experience demonstrates that effective aid for peace requires that economic reconstruction and recovery efforts explicitly address the political imperatives of peacebuilding. At the same time, peacekeeping and peacebuilding efforts must explicitly address economic imperatives. The first part of the paper focuses on the first issue: how economic assistance can be tailored to the special challenges of war-to-peace transitions. In particular, I discuss how aid conditionalities can be realigned to better serve peacebuilding objectives.

Part II, “Building Fiscal Capacity,” considers the other side of the coin: how peacekeeping and peacebuilding assistance can better support economic recovery. In particular, I focus on measures to build the fiscal basis for a sustainable state – that is, capacities to mobilize domestic revenue, allocate resources through the budget, and manage public expenditure. All too often, members of the international community have regarded the building of fiscal capacities as a specialized “niche issue” that can be left to the international financial institutions (IFIs) – notably the International Monetary Fund (IMF) and World Bank – to address through technical assistance. This stance of benign neglect can have malign results, if external assistance “crowds out” domestic fiscal capacities rather than helping to build them.

Part III, “Interrogating Donor Behavior,” examines the motives and *modus operandi* of external assistance actors in post-war countries. Donors often assume that ‘the problem’ is located entirely in the societies on the receiving end of their assistance, and that they themselves are intrinsically part of ‘the solution.’ Experience provides good reasons to question this comfortable assumption. The motives and priorities of donor governments are not always congruent with the objective of building peace, and the incentive structures within the aid agencies themselves are not always conducive to making aid an effective instrument for this purpose. Donor behavior can be part of the problem, too.

### **Part I: Aid for Peace**

Official development assistance (ODA) generally comes with strings attached. Multilateral and bilateral donors use conditionality to advance a variety of goals, some noble, others less so. The conditions sometimes are spelled out in formal performance criteria, as in the economic policy targets in IMF loan agreements. Other times the conditions are communicated informally in the process known as ‘policy dialogue.’ Whether formal or informal, conditionality makes assistance contingent on actions by the recipient. Aid seldom is a blank check.

The objectives of conditionality typically do not include the prevention or resolution of violent conflict. The IMF and World Bank primarily use conditionality to pursue short-term macroeconomic stabilization and longer-term structural adjustment. Bilateral donors often use conditionality for commercial purposes, as when aid is tied to purchases of goods and services from the donor country. They also may use it to advance geopolitical aims, as illustrated in the United States government's efforts to enlist support for the war in Iraq.<sup>1</sup> In addition, donors have also attempted, albeit rather sporadically, to use conditionality to promote political reforms under the rubric of 'good governance.'

Such conditionalities may affect the likelihood of war or peace indirectly. Proponents of conventional macroeconomic conditionality sometimes claim, for example, that neoliberal policies serve the cause of peace by fostering economic growth. On the other hand, critics argue that these same policies not only often fail to promote growth, but also exacerbate income disparities and social tensions (Pastor and Conroy 1996). At the same time, trade liberalization – a standard reform pressed by the IFIs – results in the loss of tariff revenues, squeezing the fiscal capacity of governments to fund peace-related programs.<sup>2</sup>

In principle, conditionality can also be harnessed directly to the objective of promoting peace. Where there is a risk of violent conflict, the aid 'carrot' can be designed to provide incentives for steps to reduce social tensions. In war-torn societies, aid can serve as an inducement for conflict resolution. And where a negotiated settlement has been achieved, donors can use 'peace conditionality' to encourage the implementation of peace accords and consolidation of peace, outcomes that are far from a foregone conclusion.<sup>3</sup>

In practice, efforts to reorient conditionality to these ends have been the exception rather than the rule, and where attempted, the results have been mixed. Three constraints have contributed to this spotty record. First, domestic parties may not wield sufficient authority, or enjoy sufficient legitimacy, to strike and implement aid-for-peace bargains. Second, the amount of aid on offer may be inadequate to provide a compelling incentive for the adoption of pro-peace policies. And finally, donor governments and agencies themselves may not put

peace at the top of their agendas, ahead of other geopolitical, commercial, and institutional objectives.

*Economic versus Political Stabilization? Balancing the budget deficit*

Attempts to build a durable peace often require fiscal measures that fly in the face of conventional IFI policies. For example, the IMF, in its pursuit of the objective of macroeconomic stabilization, often requires the borrower government to cut its budget deficit to specified percentages of GDP before successive installments of an IMF loan can be disbursed. Whatever the wisdom of these deficit-reduction targets – itself often a matter of debate<sup>4</sup> – in regions emerging from civil war their feasibility and desirability must be viewed through the distinctive lens of the requirements of establishing a viable peace. Insofar as the IMF's usual macroeconomic prescriptions clash with the aim of building peace, there is a compelling case for rethinking those prescriptions.

The need to rethink conventional wisdom emerged quite clearly during in the early years of Cambodia's reconstruction efforts. Following the initial period of UN administration, the IMF and World Bank pressed the country's new coalition government to downsize the civil service by 20%. A senior UN official explained:

*The IMF just applied its standard ratio: your population is 11 million people, so the size of your civil service should be x. But the historical circumstances here are almost unique. In 1979 Cambodia was a wasteland. It had no civil service, no banking, no money. Ninety per cent of the intelligentsia was dead. The new government put together a system, starting from nothing. They paid people in rice to teach. The fact that these people were not trained teachers is not their fault. You can't tell them now, 'You're useless,' and throw them on the scrap heap. It's not decent, and it's not possible politically.<sup>5</sup>*

Instead of cutting public employment, the coalition government expanded it by about 15% to accommodate jobseekers from the erstwhile opposition. In an effort to appease the donors, the government trimmed the budget deficit by cutting non-salary expenditures. 'The outcome was "remarkable progress" on the macroeconomic balances,' a subsequent World Bank evaluation dryly observed, 'combined with continued erosion of non-maintained

infrastructure and of health, education and other services' (World Bank 1998a, emphasis in original).

Similar tensions between fiscal austerity and reconstruction efforts arose in post-war Mozambique. Asserting that macroeconomic stabilization was an 'absolute prerequisite,' the IMF pressed in 1995 for spending cuts and a rollback in a scheduled increase in the minimum wage. Fearing that these moves would jeopardize the long-term goals of economic recovery and political stabilization, the ambassadors of the US, the Netherlands and Canada, and the resident representatives of the EU, UNDP, Finland and Switzerland, took the unusual step of writing a joint letter to the Fund to voice their concerns (Hanlon 1996; Ball and Barnes 2000).<sup>6</sup> In the end, a compromise was hammered out: the spending cutbacks were slowed and the minimum wage increase remained in place.

Proponents of macroeconomic discipline argue, quite rightly, that rampant inflation can undermine political stability as well as economic recovery, and that inflation often hits especially hard at the real incomes of the poor. These are good reasons to control inflation by means of fiscal and monetary discipline. But policy makers do not face an all-or-nothing choice between hyperinflation and draconian austerity: fiscal and monetary stringency is invariably a matter of degree. It is true that beyond a certain point, profligate spending and soaring deficits could trigger rapid inflation and spark economic distress and political unrest. In the range between moderate deficits and none at all, however, a tradeoff often exists between the size of the deficit on the one hand and the social tensions generated by inadequate public expenditure on the other. Within this intermediate zone, higher government budget deficits can *reduce* social tensions by financing peace-related expenditures (Pastor and Boyce 2000).

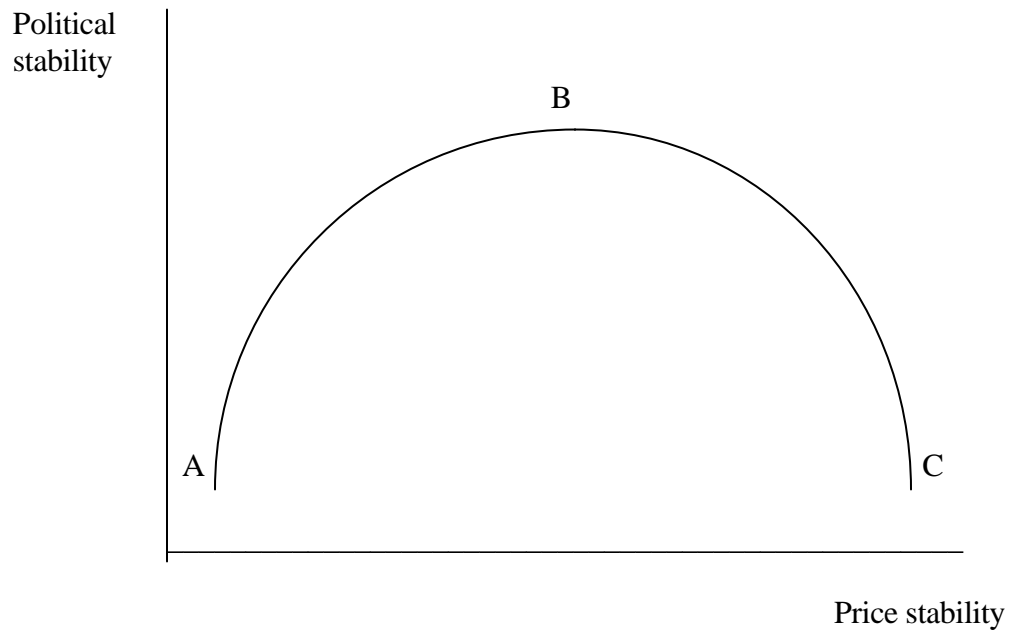
In other words, the relationship between the macroeconomic stability and political stability may take the shape of an inverted 'U', rather than a straight line. This is depicted in Figure 1. The horizontal axis represents price stability, with movement away from the origin denoting lower inflation. The vertical axis represents political stability, with movement away from the origin denoting lower social tensions. Supporters of stringent



anti-inflation policies assume that the country is on the upward-sloping part of the curve, segment  $AB$ , where greater macroeconomic stability fosters greater political stability. On the other hand, in asserting that there is a tradeoff between the two, critics of these policies assume that the country is on the downward-sloping segment,  $BC$ .

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**Figure 1: Price stability and political stability**



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Both scenarios are plausible. Research at the interface between macroeconomics and conflict impact assessment is needed to estimate where the turning point is located in any given time and place. Equally important is to explore policies that might shift the curve, easing potential tradeoffs between macroeconomic and political stability. If, for example, there is scope for shifting public expenditure from items that do little to consolidate peace to other uses that are central to this goal, this would help to reconcile the two stability objectives.

Although some relaxation of budget-deficit targets may be warranted to advance the goal of political stabilization, the scope for financing public spending by this route is limited:

at some point, price instability will feed into political instability. Printing money may increase the government's room for maneuver at the margin, but it is not a 'soft' substitute for domestic revenue mobilization. As Coats (2007, p. 215) remarks, 'the possibility of central bank lending to the government historically has often proven an irresistible temptation.' Opening the door a crack can let in flood of inflationary finance. Moreover there are some cases in which very strict monetary policies – or even a straightjacket on the central bank's ability to print money, in the form of 'dollarization' or a currency board – can enhance political stability, by taking a bone of contention off the table. Coats (2007) argues that was the case in Bosnia, where a currency board arrangement was mandated in the Dayton peace agreement. There may be good arguments for recalibrating monetary discipline in light of the political demands of war-to-peace transitions, but there is no good argument for abandoning it.

### *Peace Conditionality*

The term 'peace conditionality' was coined in a UN-sponsored study of economic policy in El Salvador in the mid-1990s (Boyce *et al.*, 1995).<sup>7</sup> The study suggested that in 'postconflict' settings, following a negotiated peace accord, donors can and should tie reconstruction and development aid to concrete steps to implement the accord and consolidate the peace. In the case of El Salvador, the government's failure to implement key aspects of the 1992 peace accord – including the provision of adequate funds for high-priority peace programs, such as the land transfer program for ex-combatants and the creation of a national civilian police force – jeopardized the peace process (de Soto and Castillo, 1994).<sup>8</sup> Hence the study recommended that the IFIs should apply peace conditionality to encourage the government to mobilize domestic resources to fulfill its commitments.

The aid pledged at international donor conferences after the signing of a peace accord is conditional from its inception, in the sense that the accord is necessary to unlock the pledges. Subsequent aid disbursements are inherently conditional, too, insofar as resumption of violence would trigger suspension of aid, and failure to make progress

toward building peace would jeopardize future aid commitments. Peace conditionality moves beyond these all-or-nothing choices, in which the aid tap is either ‘on’ or ‘off.’ Instead it seeks to calibrate the flow of support the peace process by tying specific aid agreements to specific steps to build peace.<sup>9</sup>

Peace conditionality can be applied to reconstruction and development aid, but most observers agree that it should not be applied to humanitarian assistance for both ethical and practical reasons. Ethically, it would be untenable to punish vulnerable people for the sins of their leaders. And practically, the leaders may not be terribly sensitive to humanitarian needs. Since conditionality usually involves specific aid agreements rather than across-the-board cutoffs, there is room for flexibility in deciding what types of aid will carry what conditions. A starting point for the application of conditionality is those types of aid that are most valued by political leaders and least crucial for the survival of at-risk populations (Boyce, 2002a).

Aid officials sometimes disclaim responsibility for engaging with the political issues of war and peace. At the World Bank, for example, officials at times invoke their mandate to make loans ‘with due attention to considerations of economy and efficiency and without regard to political or other non-economic influences or considerations.’<sup>10</sup> Yet violent conflict has profound economic implications. For this reason, in the case of El Salvador an internal World Bank evaluation concluded that ‘if tax effort and the pattern of public expenditures have a direct bearing on post-conflict reconstruction, as they did in El Salvador, it is legitimate to include these parameters in the conditionality agenda’ (World Bank, 1998b, p. 51).

The application of peace conditionality to fiscal policy is not a great stretch for the IFIs, institutions with a long history of applying conditionality to issues such as budget deficit reduction and trade liberalization. In the fiscal arena, peace conditionality simply involves a reorientation of objectives toward the goal of building peace. In some cases, this may mean relaxing budget deficit targets to permit governments to finance high-

priority peace programs. In others, it means paying more attention to the composition of public expenditures, the level of tax revenues, and the distributional impacts of expenditure and taxation (Boyce, 2002a, ch. 3).

Donors occasionally have pushed the envelope further, applying peace conditionality in arenas beyond their usual concerns. At a donor conference on aid to Bosnia, soon after the 1995 Dayton Peace Agreement, European Commissioner Hans van den Broek and World Bank president James Wolfensohn declared:

*Developments on the ground should be constantly reviewed to ensure that aid is conditional on the thorough implementation of the obligations undertaken by all parties, in particular, full co-operation with the international tribunal for the prosecution of war criminals* (European Commission and World Bank, 1996).

In keeping with this stance – and spurred by US legislation that instructed the US representatives on IFI executive boards to oppose loans to countries or entities not cooperating with the International Criminal Tribunal for former Yugoslavia – the World Bank and IMF blocked loans to Croatia in 1997 until the Tudjman regime turned over ten indicted war crimes suspects to stand trial in the Hague (Boyce, 2002a; Dinmore, 1997), an episode that demonstrated that where there is the will to apply peace conditionality, even for unconventional purposes, ways to do so can be found. In recent years, formal and informal conditions attached to the European Union accession process have emerged as another powerful lever for political reforms and peace implementation in the former Yugoslavia.<sup>11</sup>

In some quarters, ‘conditionality’ is a dirty word. It is portrayed – sometimes with good reason – as an intrusion on national sovereignty, a device for powerful aid donors to impose their preferences upon hapless aid recipients. Partly for this reason, and partly for the pragmatic reason that experience shows that externally imposed conditions often fail to produce real reform, many donors, including the IFIs, now embrace the need for domestic ‘ownership’ of reform agendas. The practical counterpart to this shift in rhetoric has been a move from conditionality to ‘selectivity,’ whereby aid is preferentially

allocated to governments that already have embraced the policies preferred by the donor.<sup>12</sup>

Whatever the merits of this stance, it fails to come to grips with the challenges often posed in post-conflict settings for two reasons. First, in the aftermath of violent conflict, ‘good policies’ and state capacities to implement them tend to be in short supply. If donors choose simply to wait until these emerge, they may have to wait a very long time. In the meantime, a wait-and-see attitude could impose high costs on innocent people within these societies, and on others if renewed violence spills beyond national borders.

Second, once we recognize that countries are comprised of diverse individuals, groups, and classes with divergent interests, it is impossible to speak unequivocally of ‘country ownership’ of policies. Instead we find a variety of policy alternatives supported by contending forces, both inside and outside the government. The ownership and implementation of any given policy mix requires a political process of domestic coalition building. External assistance widens the scope of the coalition-building process to include international allies.<sup>13</sup> The challenge for donors, therefore, is not to select *countries* should receive aid, but rather to select *who* within the recipient countries should receive aid, and *what* policy objectives the donors should support.

In Liberia’s Governance and Economic Management Assistance Programme (GEMAP), initiated under the transitional government in 2005, addressed to the problem of mismanagement of public finances and the attendant threat to peace implementation by providing international representatives with co-signatory authority in selected ministries and state-owned enterprises (an example of ‘dual control’ as a strategy to address problems of corruption, an issue discussed below in the context of building fiscal capacity). This unusual external intervention was a response to malfeasance in the Liberia’s transitional government; as such, as Dwan and Bailey (2006, p. 21) remark, it was ‘unlikely to be wholly “owned” by it.’ Conditionality played a key role in persuading the government to accept GEMAP: the United States threatened to withhold security sector reform assistance, the EU warned that it would shelve a planned aid package, and the World Bank threatened

to follow the IMF which had already pulled out of the country; and the threat of a travel ban on top officials under U.N. Security Council sanctions provided further leverage.<sup>14</sup>

Peace conditionality can be applied at the local level, too. In its ‘Open Cities’ program in Bosnia, for example, the UN High Commission for Refugees allocated reconstruction aid to municipalities that demonstrated a commitment to the right of refugees and internally displaced persons to return to their homes. The aim was to use aid to reward local authorities who sought to implement the Dayton accord, penalize those who obstructed implementation, and encourage vacillators to get off the fence (Boyce, 2002a, p. 18).<sup>15</sup>

In addition to supporting ‘post-conflict’ peacebuilding, conditionality can be used in efforts to promote the resolution of ongoing conflicts and to prevent conflict from breaking out in the first place. There is an important difference, however, between the situation following a peace accord and cases where violent conflict is actively underway or where there is a high risk of it breaking out. In ‘postconflict’ settings, the peace accord furnishes a set of benchmarks that have been formally accepted by the warring parties. Donors can judge performance against these benchmarks. In pre-conflict or conflict settings, donors do not have ready-made criteria on which to base conditionality, so they must develop the benchmarks themselves. In this respect, countries with negotiated peace agreements are especially suitable for the application of conditionality for peace-related ends.

## **Part II: Building Fiscal Capacity**

External assistance during the war-to-peace transition can help to finance economic recovery, social expenditures, and peace implementation programs including the establishment of new democratic institutions. Sooner or later, however, the flow of aid will diminish, and responsibility for ongoing public expenditures must be shouldered by the government. A crucial issue during postwar transitions is the building of state capacities to mobilize domestic revenue and to allocate and manage expenditure.

In this part, I analyze four issues at the interface between external assistance and the public-finance dimensions of postwar statebuilding: (i) Can the pathologies of a ‘dual public sector’ – one funded and managed by the government, the other by the aid donors – be surmounted by channeling external resources through the government, with dual-control oversight mechanisms to curtail corruption? (ii) Can postwar external assistance do more to prime the pump of domestic revenue capacity? (iii) How should distributional impacts enter into revenue and expenditure policies? (iv) Lastly, how should long-term fiscal sustainability enter into short-term expenditure decisions?

*(i) Dual public sector or dual control? External support for domestic expenditure*

The international community often seeks to help postwar governments to develop fiscal capacity to allocate and manage expenditure by providing technical assistance. More could be done, however, if donors were to channel a greater share of their resources through the state rather than bypassing it. Key stumbling blocks to doing so are the problems of combating corruption and need to ensure fiduciary responsibility.

The current practice of routing the lion’s share of external assistance outside the government gives rise to a ‘dual public sector’: an internal public sector that is funded and managed by the government, and an external public sector that is funded and managed by the donors. In sheer money terms, the latter frequently dwarfs the former. This has several adverse consequences:

- Most evident is the opportunity cost of failing to tap these resources to build state capacities to allocate and manage public expenditure.
- Less obvious, but no less serious, is the ‘crowding-out’ effect as professionals are recruited into the external public sector, often at salaries that the government cannot match.<sup>16</sup> Ironically, aid donors then point to lack of capable government personnel as a rationale for continuing to bypass the state.

- The fact that the external public sector is managed by numerous agencies, each with their own priorities, poses enormous coordination problems. This leads to the waste of scarce administrative resources, as government ministries cope with the different reporting systems of multiple funders.
- Last but not least, there are no institutional mechanisms that make donor agencies accountable to the local citizenry.<sup>17</sup> No matter how imperfect the degree of democratic governance, the state arguably has a comparative advantage in this respect.

When pressed on this issue, donors maintain that they (and the non-governmental organizations and private contractors on whom they often rely) do a more effective job than the government in delivering goods and services. This is not an argument that can be dismissed lightly. There undoubtedly are situations in which the short-run advantages of circumventing the state are compelling. But once we recognize that the long-run aim of aid is – or ought to be – to *build state capacities* as well as to deliver services, the argument loses at least some of its force.

Moreover, experience shows that the ‘short run’ invoked by donors can last a long time. In Cambodia, where more than a decade has elapsed since the United Nations transitional administration handed power to a new government, Smoke and Taliercio (2007, pp. 69, 81) observe that the donors’ focus on delivering results still leads them to ‘bypass when possible—and capture when not—the Cambodian civil service,’ and that spending on technical assistance remains two to three times greater than the total wages paid to government civil servants. One cannot help feeling that something is wrong with this picture.

Concerns about corruption in the internal public sector are often a significant impediment to channeling more external assistance through the state. Corruption saps the delivery of public services, deters private investment, and fuels popular discontent (Rose-Ackerman 1999). But efforts to combat it are complicated where corruption helps to maintain



political cohesion by redistributing resources through informal channels. Not all corruption is equally corrupt, or equally corrosive: in some it is driven entirely by individual greed, but in others it provides patronage resources for wider networks. An example of the latter is the use of government revenues and profits from state-sanctioned monopolies to lubricate ‘neopatrimonial’ governance in the Palestinian Authority under Yasser Arafat (see Brynen 2000, 2007).

Donors often adopt an avoidance strategy for dealing with this problem: avoid ‘leakages’ by bypassing the government, and avoid public discussion of the topic for fear of ruffling political feathers. This strategy is dysfunctional for three reasons. First, aid that is routed outside the government is insulated from neither the perception nor the reality of corruption.<sup>18</sup> Indeed, the lack of transparency and accountability mechanisms can fuel public perceptions that externally administered projects are even more prone to corruption than government projects.<sup>19</sup> Second, the avoidance strategy fails to harness aid to build state capacity to budget and manage public expenditure effectively. Third, the refusal of donor agencies to route resources through the government sends an unmistakable signal to the populace: the government cannot be trusted. This has a negative feedback effect on domestic revenue mobilization, insofar as willingness to pay taxes hinges on perceptions that the state will deliver services in return.

An alternative strategy for addressing problems of corruption would have two prongs. The first is to devise transitional adjustment assistance programs for people who have been dependent on patronage networks, recognizing that corruption for such “neopatrimonial” purposes differs from personal corruption. Such assistance would be analogous, in a sense, to job training programs for workers displaced by the effects of trade liberalization in industrialized countries, and – closer to home – to the disarmament, demobilization, and reintegration (DDR) programs for ex-combatants that are often implemented in postwar countries.

The second prong of an alternative anti-corruption strategy is the use of dual-control systems to build institutions for accountability and transparency alongside public

expenditure capacities. The Afghanistan Reconstruction Trust Fund (ARTF), a World Bank-administered account through which donors help to fund to the government's recurrent budget, offers an instructive model for how donors can route aid through the government – in effect, helping to internalize external resources (Ghani *et al.* 2007). The Afghan government allocates these external resources through its internal budgetary process, reinforcing the budget as the central instrument of policy. When the ministries spend the money – for example, paying teachers – an external monitoring agent appointed by the World Bank verifies that the accounting standards of the ARTF and government (which are the same) have been met, and releases the funds. The ARTF thus is like a bank account with a fiduciary screen, similar in this respect to the dual-control arrangements established in Liberia under GEMAP. Approximately two-thirds of the Afghan government's non-security recurrent budget is now being funded by the ARTF, although this amount remains small relative to total external assistance (Scanteam 2005).

Channeling aid through the government in this fashion does not imply that the donors abdicate control or responsibility for how their resources are used. The ARTF does not issue blank checks. Two signatures are required to release funds, one from the government and one from the external monitoring agent. The result is a dual-control system – a setup analogous to the dual-key system used to prevent an accidental launch of nuclear missiles.<sup>20</sup>

*(ii) Priming the pump? External support for domestic revenue mobilization*

In many postwar settings, a central task is to raise domestic revenue to provide sustainable funding for new democratic institutions and for expenditures to improve human well-being, strengthen public security, and ease social tensions. The size of government revenue relative to gross domestic product in wartorn societies typically is far below the average for other countries with similar per capita income.<sup>21</sup> Yet the needs for government expenditure are, if anything, greater. Hence concerted efforts are needed to increase revenues.

Experience has shown that aid can ‘crowd out’ domestic revenue mobilization, reducing the incentive for the government to tax its own populace.<sup>22</sup> If aid instead is to ‘crowd in’ domestic revenue, conscious efforts are needed to this end. The international community can support government efforts to mobilize domestic in four ways: (a) by providing technical assistance; (b) by linking some of its aid to progress in domestic revenue performance; (c) by helping to curb extra-legal revenue exactions; and (d) by reducing tax exemptions on postwar aid.

(a) *Technical assistance* (TA) is the most common type of support. The IMF, World Bank, and bilateral donors have helped to develop revenue capacities, ranging from drafting tax codes to setting special tax administration units within finance ministries with special training and higher pay in an effort to insulate them from corruption.

In some cases, TA providers have shown an impressive ability to cast aside orthodoxies and adapt their policy advice to local realities. For example, despite the aversion of the IFIs to trade taxes, import duties were recognized as the most feasible source of revenue enhancement in Timor-Leste, Kosovo, and Afghanistan. In the case of Timor-Leste, the IMF even supported introduction of a levy on coffee exports (see Pires and Francino 2007, p. 131), a policy that verges on the heretical. In other cases, however, orthodoxy has triumphed over pragmatism. In Guatemala, for example, even as the IMF gave rhetorical support to the revenue-enhancement goal mandated by the peace accords, the Fund’s staff urged the government to cut tariffs.<sup>23</sup>

The effectiveness of TA could be further strengthened by efforts to adopt technologies and procedures that build on existing capacities, rather than opting for off-the-shelf imported solutions. In Afghanistan, for example, Ghani *et al.* (2007, p. 175) recall that computerized information systems introduced at the Ministry of Finance were ‘unsuitable in terms of complexity and language,’ prompting subsequent efforts to retool with Persian-language systems from Iran. More attention to training local personnel, rather than simply substituting for them, could also foster capacity building. In Timor-Leste, Pires and Francino (2007, p. 147) remark that the concentration on expatriate advisory

services was accompanied by ‘some neglect for formal training programs for national staff.’ The ultimate goal of technical assistance is to become redundant.

(b) *Conditionality* is a second way that donors can encourage domestic resource mobilization. On the expenditure side of fiscal policy, it is not unusual for donors to require ‘counterpart funding’ by the government as a condition for aid to specific projects, a strategy intended to ensure domestic ‘buy-in’ and to counteract fungibility (whereby aid merely frees government money for other uses). But on the revenue side, conditionality of this type has been rare. It would be a straightforward matter to link certain types of aid – notably budget support – to progress in meeting domestic revenue targets. Such a policy is akin to the provision of ‘matching grants’ by private foundations. In both cases, the aim is to strengthen incentives for aid recipients to seek further resources, counteracting the disincentive effects of unconditional aid.

Visiting Guatemala in May 1997, a few months after the signing of that country’s peace accords, IMF Managing Director Michel Camdessus took a broad step in this direction when he stated that the Fund’s only condition for a stand-by agreement would be that the government comply with its peace-accord commitments, including a 50% increase in the revenue-to-GDP ratio.<sup>24</sup> Making a tighter linkage, the European Union conditioned its budget support to the government of Mozambique in 2002 on increases in domestic revenue.<sup>25</sup> One of the benchmarks in the Afghanistan Compact signed in London in early 2006, which sets out the framework for international assistance to that country over the next five years, is to increase the revenue/GDP ratio from 4.5% in 2004/05 to 8% in 2010/11.<sup>26</sup> But conditionality with respect to revenue mobilization remains the exception, not the rule (for discussion, see Carnahan 2007).

(c) *Curbing extra-legal revenue exactions* is a task located on the cusp between public finance and security. When profits from the exploitation of nominally public resources, like Cambodia’s forests, flow into the private pockets, this not only deprives the state of revenues but also often finances quasi-autonomous armed groups that threaten the peace (Le Billon 2000). When local warlords levy ‘taxes’ on trade, sometimes including trade

in narcotics, as in Afghanistan, they undermine the state's monopoly not only on revenue collection but also on the legitimate exercise of force. Curtailing such activities may require international assistance. Yet peacekeeping forces, even those with a relatively expansive mandate like the International Security Assistance Force (ISAF) in Afghanistan, typically have not seen this as a part of their job.

Even more problematic, powerful members of the international community may be reluctant to crack down on extra-legal revenue exactions when they regard those involved as political allies. In Afghanistan, for example, efforts to consolidate revenue in the hands of the state and to fight drug trafficking have been complicated – to put it lightly – by the decision of the United States government to enlist anti-Taliban warlords as partners in its 'global war on terror.' Such marriages of convenience, reminiscent of U.S. support to the anti-Soviet *mujahadeen* in the 1980s, may serve short-run security objectives, but do so only at the expense of undermining the legitimacy and effectiveness of the state – and ultimately security too – in the long run (for further discussion see Sedra and Middlebrook 2005; Ahmad 2006).

(d) *Reducing tax exemptions on postwar aid flows* could do much to prime the pump of domestic revenue-collection capacity. In the first postwar years, aid often is the single biggest component of the formal-sector economy. Yet today aid flows, and many of the incomes generated by them, are tax-exempt. The incomes of expatriate aid officials and aid workers are often tax-free.<sup>27</sup> The incomes of their local staff, often quite high by local standards, are often tax-free too. The goods imported by the aid agencies, ranging from Toyota land cruisers to cases of Coca-Cola and whiskey, are often tax-free. The rents paid by expatriates for office space and housing – again, often exorbitant by local standards – are often tax-free. So are other services provided to them, such as hotels and restaurants.

These pervasive exemptions have several adverse consequences. Most obvious is the opportunity cost of foregone government revenues. In addition, scarce administrative capacity is devoted to administering different rules for different people. Goods that enter

the country as aid may wind up on sale in local markets, undercutting legitimate competitors who pay import duties. Last but not least, the special treatment accorded to expatriates again sends an unmistakable message to the local populace: rich and powerful people do not have to pay taxes. The result can be ‘the creation of a culture of tax exemptions,’ in the words of a recent IMF review of postconflict experiences (Gupta *et al.* 2005, p. 12). This demonstration effect runs precisely counter to efforts to establish effective and progressive revenue collection systems. It also undermines the credibility of international agencies when they argue that governments should reduce tax loopholes and ‘tax incentives’ for local businesses.

Efforts to tax aid bonanzas have run into adamant resistance from aid donors. In Timor-Leste, efforts to tax the floating hotels in the Dili harbor that accommodated the postwar influx of foreigners were rebuffed by lawyers at United Nations headquarters in New York, on the dubious grounds that diplomatic ‘privileges and immunities’ extend to those who provide services to U.N. personnel (Pires and Francino 2007, p. 136). In Afghanistan, the introduction of a tax on rental incomes generated by expatriates in Kabul likewise met resistance; as Ghani *et al.* (2007, p. 174) remark, ‘the international community’s declarations on the importance of enhancing domestic revenue mobilization have not been matched by willingness to consider new initiatives to tap the revenue possibilities generated by their own presence.’

This issue has often pitted the IMF and World Bank, along with national officials, against other donor agencies. In Timor-Leste, Pires and Francino (2007, p. 136) recall ‘bitter fights between international officials at the Ministry of Finance and international officials of donor organizations ... with the latter winning’:

*Generally the donors and the UN, who disagreed about many things, were as one on their inviolable right to a complete exemption from taxes, not only for themselves as individuals or for goods imported for their direct use, but also on their contractors and goods imported for reconstruction.*

Similarly, non-governmental organizations (NGOs) ‘ferociously defended every inch of ground’ in resisting taxation of even their local employees: ‘Even when UNTAET offered to pay the taxes of international staff working with NGOs provided they were prepared to declare the income they were receiving, the answer was still “No”.’

Donor officials make three arguments against paying taxes. The first is that this would be equivalent to budget support. This is true. But its implicit premise – that the government cannot be trusted to use tax revenues well – again sends a clear message to the local populace. The second argument is that expatriates were already paying taxes in their countries of origin. In cases where this is so, existing tax treaties allow credits for taxes paid elsewhere, avoiding the problem of double taxation. The third argument is that other countries do not tax them, so why should any country be different? The answer to this objection is that all desirable changes have to begin somewhere.

Income tax payments by expatriate or local aid personnel would need not to come from their own pockets. Those who pay taxes could be given salary ‘top-ups’ to maintain their after-tax incomes. This is the current practice for U.S. citizens employed by the United Nations, World Bank and IMF, who must pay income taxes (unlike their non-U.S. co-workers) but who then receive compensating pay increments in interest of horizontal equity.

Initiatives to tap aid inflows for domestic revenue could also take the form of ‘payments in lieu of taxes’ (PILOTs), a solution that has been adopted in many college towns in the U.S. where municipal governments understandably want tax-exempt institutions of higher education to contribute to funding public schools, police and fire protection, and other local services. PILOTs maintain the legal privileges of those who make them. At the same time, they open the door for those donors who are serious about building domestic revenue capacity to act without waiting for across-the-board solutions.

*(iii) Who pays taxes & who benefits from expenditure? Fiscal policy through a conflict lens*

Fiscal policy making in postwar settings requires careful attention to questions of *what* and *to whom*.

The ‘what’ question is about priorities. Faced with many pressing needs – for spending in areas such as public safety, the demobilization and reintegration of ex-combatants, health, education, and the rehabilitation of economic infrastructure – how should scarce resources best be allocated? The aim must be not simply to maximize returns defined in terms of conventional development indicators, but also to get the most ‘non-bang for the buck’ in terms of building a durable peace.

Underscoring this point, the synthesis report emerging from the World Bank’s research program on violent conflict observes that this ‘creates the potential for trade-offs between policies that promote growth and those that promote peace’ (Collier *et al.* 2003, p. 166). In particular, a strategy focused exclusively on short-term economic returns might concentrate spending on the capital city and developed regions, leading to ‘a trade-off between the growth-maximizing geographic distribution of public expenditure and a distribution that might be regarded as fair.’ Where such trade-offs exist, the report concludes, ‘the government may need to give priority to policies for peace building.’

When viewed through a conflict lens, the ‘what’ question in public expenditure cannot be divorced from the ‘to whom’ question. As Murshed and Tadjoeeddin (2007, p. 35) observe, not only are grievances rooted in distributional inequalities often important drivers of conflict, but also inequalities often worsen during conflict:

*The already poor often lose the few assets they have, and looting adds to the number of poor. In contrast, warlords and their followers accumulate assets, and so while the early years of peace may see quite rapid growth it can be very narrow in its benefits – unless policies are put in place to restore the productive assets and human capital of the poor.*



Two sets of distributional issues are particularly relevant in public expenditure. The first is how to incorporate vertical and horizontal equity concerns into spending decisions. The second is how to allocate expenditures across the political landscape so as to bolster incentives for the implementation of accords and the consolidation of peace.

Conflict impact assessments could address both sets of issues. These are analogous to environmental impact assessments, first introduced in the 1970s, with the difference that here the concern is the social and political environment rather than the natural environment. Just as environmental impact assessment aims to incorporate ‘negative externalities’ of pollution and natural resource depletion into expenditure policies, so conflict impact assessment aims to incorporate the ‘negative externalities’ of social tensions and violent conflict.

International aid agencies increasingly recognize the need for conflict impact assessment as an input into policy making and project appraisal, and some have begun to put this recognition into practice (see, for example, World Bank 2002; DfID 2003; USAID 2005, SIDA 2006).<sup>28</sup> Yet efforts to incorporate distributional considerations into expenditure decisions in postconflict countries are still at a very early stage. Information on vertical equity – the distribution of benefits across the poor-to-rich spectrum – is sometimes collected and sometimes used as an input into policy making. In many cases, however, even such basic data are not available.

In the case of horizontal equity – distribution across regions and groups defined on the basis of race, ethnicity, language, or religion – the paucity of information is even more severe. In the past decade, researchers have analyzed the role of horizontal equity in the genesis of civil wars (Stewart 2000, 2002; Østby 2004), and economists have begun to think hard about how to measure it, starting with spatial inequalities across regions (Kanbur and Venables 2005; Stewart *et al.* 2007). But at best, conflict impact assessment today is roughly where environmental impact assessment was three decades ago, its importance accepted in principle, but with a long way to go in developing the tools and capacities for implementation in practice.

Collection of regional data on expenditures in administrative units, such as states, provinces, and districts, would seem to be relatively straightforward, both practically grounds (since ministries often allocate their funds across regional units) and politically (since regions often can serve as a proxy for more sensitive categories such as ethnicity). Yet today even such data are remarkably few and far between.<sup>29</sup> Afghanistan's former finance minister and his colleagues recount their experience:

*Obtaining the figures on provincial expenditures from line ministries required months of intense discussion and analysis of manual systems of recordings. When the figures were first presented to the Cabinet, it came as a shock that the ten poorest provinces of the country were receiving the smallest amounts of allocation. (Ghani et al. 2007, p. 179).*

The only unusual feature of this experience is that the finance ministry went to the trouble to request this information.

The 'who' questions that need to be addressed by conflict impact assessments of fiscal policies may involve more than inequalities. Some researchers have been suggested that conflict is better understood as being driven by *polarization* rather than inequality *per se*. Polarization refers to the interaction between alienation across groups and identification within groups; income polarization, for example, is higher when the gap between rich and poor is greater (resulting in greater alienation between the two) and when income inequalities among the rich and poor are lower (resulting in greater identification with others in the same income group). More generally, polarization is greatest under a symmetric bimodal or 'twin-peak' distribution. Esteban and Ray (1999, p. 401) make this argument on theoretical grounds:

*Polarization, not inequality as it is commonly measured, holds the key to our understanding of social tension and conflict. Briefly, polarization is a feature of distributions that combines elements of equality and inequality in a particular way.... Intra-group homogeneity, coupled with inter-group heterogeneity, lies at the heart of a polarized society, and this feature is correlated with social conflict.*

Montalvo and Reynal-Querol (2005a, b) offer empirical support for the proposition that what they term ‘ethnic polarization’ – which attains a maximum when the population is divided into two ethnolinguistic groups of equal size – is a statistically significant predictor of the likelihood of civil war.

When economic polarization (in the distribution of income, wealth, or other attributes such as employment, education, and health) aligns with social polarization (in the distribution of the population into identity groups based on race, ethnicity, language, religion, or region), the potential for violent conflict may be multiplied. Duclos, Esteban and Ray (2004) speculate that a ‘hybrid’ measure of polarization, that combines social and economic considerations, may be a better predictor of social conflict than ‘pure income’ or ‘pure social’ measures confined to distribution measured on a single attribute. Ravi Kanbur (2007, p. 3) remarks:

*Polarization of society into a small number of groups with distinct identities is an incubator of conflict on its own. But add to this the dimension of average income differences between the groups, and a combustible mix is created.*

This insight brings us back to the importance of horizontal inequality, a concept that as noted above is distinct from vertical inequality, or ‘inequality as commonly measured’ in Esteban and Ray’s phrase.

The phenomena of between-group alienation and within-group identification also have implications for the role of ‘social capital’ in the dynamics of conflict and peacebuilding. Social capital – trust, norms, and networks that facilitate coordination and cooperation – is often regarded as an entirely wholesome and beneficial thing. But social capital can also have a ‘dark side,’ insofar as it enables some groups to cooperate more effectively to the detriment of others. Drawing a distinction between ‘bonding’ social capital that promotes trust and cooperation within groups and ‘bridging’ social capital that promotes these between groups, Putnam (2000, p. 362) acknowledges that ‘some kinds of bonding capital may discourage the formation of bridging social capital and vice versa.’<sup>30</sup>

During civil wars, bonding social capital can be deployed for purposes of expropriation, pillage, rape, and murder. Meanwhile, bridging social capital is destroyed, with consequences that can be just as serious as losses of physical capital.<sup>31</sup> During war-to-peace transitions, therefore, an important aim of public expenditure, and of public policies more generally, is not simply to build generic social capital but rather to build specifically those types of social capital that reduce inter-group alienation, or what Putnam (1993, p. 175) terms ‘networks of civic engagement that cut across social cleavages.’ The potential importance of this bridging social capital is illustrated by Ashutosh Varshney’s (2002) analysis of Hindu-Muslim tensions in urban India, which points to the role of associational ties across communities in reducing the likelihood of communal violence.

As Kanbur (2007, p. 6) observes, tensions may be present between the goal of promoting cross-group associational ties and other goals of economic policy. To illustrate, he notes that labor unions can serve as important arenas for cooperation across ethnic and religious cleavages; hence ‘reducing the power of trade unions is an example of a policy that is often put forward in the name of increasing efficiency, but could have the long run result of increasing group tensions.’ Where trade-offs exist, once again there are compelling grounds ‘to give priority to policies for peace building’ (Collier *et al.* 2003, p. 166).

A further dimension of the ‘who’ question in postwar settings relates to balances of power among and within competing political parties and their supporters. This requires attention not only to community-wide characteristics such as living standards and ethnicity, but also to the stances of individual political leaders who often vary in their commitment to peace. Some leaders are enthusiastic about implementing peace agreements, others are lukewarm, and still others are prepared to resume war rather than make concessions for peace. Selective allocation of public spending can be one instrument to reward those who are committed to peace, penalize spoilers, and encourage the undecided to back peace implementation.<sup>32</sup> If, instead, public spending strengthens the hand of hardliners, this can contribute to an unraveling of the peace process.<sup>33</sup>

Distributional impacts need to be considered on the revenue side of fiscal policy, too. This issue sometimes is slighted by economists who were taught in graduate school that distributional objectives are tackled most efficiently on the expenditure side of fiscal policy. Inattention to ‘who pays?’ questions in revenue policy is dysfunctional, however, for the three reasons: first, the axiom that distribution can be relegated to expenditure alone rests on a textbook ‘optimal planner’ model that does not fit the real world; second, even optimal planners would need full information on the distributional impacts of revenue policies to achieve their targets; and third, if the public believes that the distributional effects of revenue policies matter, then politically they do.

Yet little has been done to bring distributional concerns to bear on revenue policies. The primary revenue goal of postwar government authorities, and of the international agencies that seek to assist them, has been to increase the volume of collections; the secondary goal has been to do so as ‘efficiently’ as possible. To be sure, increasing the volume of revenue is no small task. And efficiency – if understood in terms of the realities of wartorn societies, as opposed to textbook axioms – is desirable. But neglect of the distributional impacts of taxation can subvert both of these goals.

The starting point for any effort to address this lacuna must be careful documentation of the distributional incidence of revenue instruments both vertically and horizontally. Collecting the necessary data will be a non-trivial task, for today there is a paucity of such information even in ‘normal’ developing countries, let alone in wartorn societies.<sup>34</sup> This can be contrasted with the situation in the industrialized countries, where the distributional impacts of proposed taxes typically are subjected to intense scrutiny by politicians and policy makers alike. Ironically, it is precisely where the need for such analysis is greatest – in societies embarked on the fragile transition from war to peace – that these issues receive the least attention. Technical assistance from the international community could play a valuable role in filling this information gap.

Documentation is only the first step. The second is to incorporate this information into policy making. In choosing the mix of revenue instruments – the balance between tariffs, value-added taxes and income taxes, for example – their distributional incidence must be considered alongside their revenue potential, administrative feasibility, and efficiency effects. One option that would be likely to receive much more attention, once revenue is seen through the distributional lens, is luxury taxation. Taxes on items such as private automobiles and private aircraft can combine the attractions of administrative ease, distributional progressivity, and substantial revenue. Remarkably, these rarely feature in discussions of postwar revenue policies.

Finally, information on the distributional impacts of revenue instruments, and on the ways that government policies are taking these into account, must be disseminated widely to the public, so as to guard against misperceptions and facilitate compliance by legitimizing the policies. The importance of this was demonstrated vividly in Guatemala, where the peace accords set explicit targets for increasing government revenue and social expenditure. To this end, the first postwar government attempted to increase the tax on large property owners. This effort was scuttled, however, in the face of protests not only from estate owners but also from small-scale indigenous farmers who thought that the tax would burden them (Rodas-Martini 2007, p. 90; Jonas 2000, pp. 171-172). The lesson is clear: successful revenue policymaking cannot be a purely technocratic preserve; it must be part and parcel of the democratic process.

*(iv) Thinking about tomorrow, today? Getting serious about fiscal sustainability*

External resources that are spent today – regardless of whether they are channeled through the state or around it – often have implications for how domestic resources must be spent tomorrow. This is true both for recurrent expenditures, including salaries, and for capital expenditures that will require spending for operation and maintenance in future years. Hence there is an evident need to think about the long-term fiscal implications of current decisions.

In the aftermath of war, attention to pressing short-term needs is perfectly natural, and perfectly valid. But this does not imply that the future consequences of today's decisions can or should be shunted aside for others to handle later. The long run begins in the short run. Myopia not only postpones getting serious about long-run problems, but also can make them worse.

Although much can be done to enhance domestic revenue capacities, the sky is not the limit. Prudence demands recognition that budget constraints will always be a fact of life. When building new government institutions and infrastructure, this reality must be borne in mind. It would be a mistake to rely on a transitory flush of external funds to create structures that are not fiscally sustainable. The point may seem obvious, but past experience suggests that it is often ignored.

Consider, for example, security spending in Afghanistan, where the Afghan National Army has been built with large-scale funding from the United States government. Security-sector expenditures in the three-year period from 2003/04 to 2005/06 were equivalent to 494% of the Afghan government's revenue, or roughly one-third of the country's GDP (World Bank 2005a, p. 42).<sup>35</sup> 'Total security expenditures will exceed forecast domestic revenues for some years to come,' warns a recent World Bank study (2005a, p. 47) that describes the situation as 'unaffordable and fiscally unsustainable.' As Ghani *et al.* (2007, p. 182) remark:

*Even under very optimistic projections for domestic revenue, such an expenditure on security would imply a totally inadequate allocation of resources for human capital, infrastructure, and other vital functions of government.*

Even from a security standpoint, unsustainable expenditures are shortsighted. A well-equipped army that isn't getting paid ceases to be a security force. Instead it becomes an insecurity force.

A recent operational note prepared jointly by the United Nations Development Group and the World Bank (2005, p. 4) draws the clear lesson from such experiences: 'It is

important to ensure that security issues are treated as an integral part of the national planning and budgetary process, rather than through separate forums which may lead to a lack of transparency or the taking of decisions which are fiscally unsustainable or undermine other reconstruction efforts.’

The problem of unsustainable expenditure is not confined to the security sector. Salary supplements for civil servants – including ‘sitting fees’ for attending donor-funded workshops, where ‘the daily rates can exceed regular monthly salaries’ (Moss *et al.* 2005, p. 7) – likewise can create problems for fiscal sustainability. Citing studies showing that additional remuneration to civil servants in Cambodia far exceeds their regular salaries, a recent UNDP study concludes that ‘the principal incentive to work in public employment is the prospect of access to external salary supplements’ (Beresford *et al.* 2004, p. 33).

Capital investments with high operation and maintenance costs also generate fiscal burdens down the road. In Palestine, Brynen (2007, p. 199) reports, aid donors have often ignored the development plans of the Palestinian Authority (PA), ‘undercutting any PA effort to monitor the cumulative long-term costs of donor-financed investments.’ Again he points to the resulting distortion in incentives: the ‘lure of donor money’ encouraged government officials to put forward projects ‘not because they were a real priority, but because they seemed most likely to attract some external funding.’

A famous example of a costly, donor-driven project with high ‘flagpole value’ but problematic fiscal implications is the Gaza hospital financed by the European Union (Brynen 2000, pp. 196-197). ‘Donor-driven investments in public hospitals are sometimes referred to as “Trojan horses”,’ notes a recent World Bank report (2005b, p. 52), ‘because of their large operating costs which crowd resources out of priority areas such as the basic package of health services.’

Closely related to this problem is the bias of many aid-funded projects in favor of excessive reliance on imports. In deciding to the extent to which the goods and services



purchased for relief, recovery, and reconstruction should be imported, as opposed to being procured locally, donors face another tension between short-run expediency and long-run capacity building – the capacity in this case being in the private sector. Again there are undoubtedly cases where the former trumps the latter: for example, where local sourcing would require large investments with long gestation periods. But there are also cases where local procurement could do more to stimulate economic recovery, and perhaps save money in the process.<sup>36</sup>

To cite an example of the pervasive bias against local suppliers, during the United Nations Transitional Administration in East Timor, some quarter of a million desks and chairs for local schools were purchased with money from the World Bank-administered Trust Fund for East Timor. At the time, some officials suggested that some of these be procured locally to spur the growth of small and medium woodworking enterprises. Others rejected this on the grounds that local procurement would be too slow (Pires and Francino 2007, pp. 141-2). This was not a life-or-death case of emergency food supplies where time was of the essence; the goods in question were school furniture.<sup>37</sup>

The interwoven challenges of building an effective state, a robust economy, and a durable peace all require thinking about tomorrow, today. Postwar inflows of external assistance cannot be sustained indefinitely. The success of this aid ultimately will rest on whether the structures built with it can be sustained without it.

### **Part III: Interrogating Donor Behavior**

Efforts to make external assistance a more effective tool for peacebuilding face two sorts of obstacles. First, peace is not the sole objective of donor governments, nor is it always the dominant one in shaping their interventions in war-torn societies. Competing objectives can not only divert attention and resources in other directions, but also pose obstacles to building a durable peace; in other words, policy objectives may be not only divergent but contradictory. Second, aid agencies have their own internal dynamics shaped by incentive structures, ideological biases, and inter-agency rivalries. These can

undermine agency effectiveness even in pursuit of more familiar development objectives, let alone in responding to the novel challenges of building peace. This part of the paper examines these issues.

*Competing 'national interests'*

In addition to peace, donor governments often pursue other objectives in war-torn societies. These include (i) geopolitical aims, (ii) economic and commercial interests, (iii) the repatriation of refugees, and (iv) responding to public opinion.

*(i) Geopolitical aims:*

The Cold War rivalry between industrial democracies and the Soviet bloc helped to fuel violent conflicts across Asia, Africa, and Latin America. Aid was one weapon in this global contest. For example, because Cambodia's government in the 1980s was backed by the Soviet Union and Vietnam, the United States not only withheld aid and diplomatic recognition, but went so far as to insist that the country's UN seat should remain in the hands of the murderous Khmer Rouge. Former UN Secretary-General Kofi Annan (2002, p. 8) described the situation candidly: 'Corruption and waste – indeed, results of any kind – were secondary to what donor countries wanted most, namely political allegiance.'

Despite the end of the Cold War, geopolitical considerations continue to exert profound impacts on the policies of external assistance actors, particularly those of bilateral donors. For example, the French government's willingness to support the Habyarimana regime in the crucial months preceding the 1994 Rwandan genocide appears to have been driven, in no small measure, by the aim of backing the 'Francophone' Hutu against the 'Anglophone' Tutsi (see, for example, Prunier 1995).

Such biases have affected the policies of the IFIs, too. A World Bank study concludes: 'Between 1970 and 1993 aid allocations – by bilateral and multilateral donors – were dominated by politics – both the international politics of the Cold War and the internal

politics of aid agencies' (World Bank 1998c, p. 40). The study cites aid to Mobutu's Zaire as 'just one of several examples where a steady flow of aid ignored, if not encouraged, incompetence, corruption, and misguided policies.' The World Bank itself was among the biggest lenders to the Mobutu regime, accounting for \$1.4 billion of Zaire's \$12.3 billion external debt in 1994 (Ndikumana and Boyce 1998). Indeed, in the late 1980s the pressure from powerful governments with a preponderant share of voting power in the IFI boards to lend to corrupt allies was so intense that a senior IMF official warned that the Fund's assistance was in danger of becoming 'indistinguishable from political support' (Finch 1988).

*(ii) Economic and commercial interests*

Economic interests routinely influence foreign policy. For example, securing access to key raw materials, such as oil, has long been seen as a major concern of the industrialized countries. More surprising, perhaps, is the extent to which more mundane commercial motives – for instance, the pursuit of contracts for building bridges or leasing aircraft – can drive donor decisions. A substantial proportion of bilateral aid has been 'tied' to imports of goods and services from the donor country (de Jonquières 1996). In effect, tied aid is a vehicle by which donors subsidize overseas sales by their domestic private-sector constituents. Defenders of the practice argue that this builds 'essential political support' for foreign aid back home (Rothkopf 1998). At the same time, aid becomes a means to win foreign political support for business constituents in the donor country.

This quest for short-term commercial advantage can erode the willingness of donors to exercise peace conditionality. In the mid-1990s, for example, the Cambodian government retaliated against the Australian government's criticism of its human rights record by canceling business deals with several Australian firms. The lesson was not lost on other donors. 'What is important for many of these ambassadors is to defend their few miserable contracts,' a United Nations official in Phnom Penh observed. 'It is as if they represent their companies rather than their countries.'<sup>38</sup>

Recipient governments play on these fears, at times quite openly. ‘Japan is taking a lead,’ a Cambodian commerce ministry official declared in 1999 when denouncing political conditions on U.S. aid. ‘By the time the U.S. shapes up, if a U.S. company is bidding on a contract against a Japanese company, do you think the U.S. will win? I don’t think so’ (quoted by Piore 1999, p. A35).

More recently, the rise of China as sub-Saharan Africa’s single largest aid donor – with its policy of ‘no political strings’ – has sparked new concerns as to potential tensions between economic and commercial objectives and peacebuilding and ‘good governance’ objectives.<sup>39</sup>

*(iii) Refugee repatriation*

The desire to repatriate refugees can be another important objective of aid donors – particularly when refugees are living in the donor countries. For example, some 345,000 Bosnians had taken refuge in Germany by the time of the Dayton peace agreement, and their support was costing German state and local governments approximately 1,000 DM per refugee per month, or four billion DM (more than \$2 billion) per year (International Crisis Group 1998). To expedite refugee returns, the German authorities deployed incentive packages, repatriation assistance, and threats of deportation. There is a tension, however, between this objective and the aim of consolidating a lasting peace. The quickest way to repatriate refugees to Bosnia was not to return them to their former homes, where those who expelled them often continued to wield power, but instead to send them to territories under the control of their ‘own’ people. As a result, war-damaged houses rebuilt with donor aid are often occupied not by their original owners, but by returnees of the ‘right’ ethnicity – a practice that, in effect, converted refugees into internally displaced persons. This not only failed to advance the Dayton principle of ethnic re-integration, but also made this goal still more difficult to achieve, since the return of the original owners to their homes now would require relocating the new occupants. Instead of using aid to encourage local authorities to accept minority returns, repatriation-driven reconstruction aid helped consolidate the demographic results of ethnic cleansing.

*(iv) Public opinion*

Donor respond, to some extent, to public opinion within the donor countries. In some cases, public opinion pushes donors to support peacebuilding, but in others it may operate against this goal. The United States government, for example, has been reluctant to exercise conditionality in its dealings with Israel – the top recipient of U.S. foreign aid – in order to encourage progress toward a peace settlement with the Palestinians. ‘If in the end Israel cannot accept our ideas, we will respect that decision,’ US Ambassador Edward Walker assured leaders of the American Israel Public Affairs Committee (AIPAC) in 1998, ‘and it will not affect our fundamental commitment to Israel by a single jot or tittle’ (quoted in Gellman, 1998). This unconditional support is often ascribed to the power of the pro-Israel lobby in the US, and AIPAC in particular, which *Fortune* magazine rates as the second most influential lobbying group in Washington (Erlanger 1998; Mearsheimer and Walt 2007). But the deep-rooted antipathy towards the Palestinian side among some US politicians has acquired a momentum of its own. This was demonstrated in the mid-1990s, when in keeping with the official Israeli policy immediately after the Oslo accords, AIPAC arranged for senior international officials to brief key US Congressmen to urge them to fund the newly created Palestinian Authority. Despite the fact that AIPAC itself was lobbying of behalf of the funding, Congress refused. ‘We’re not paying those terrorists!’ an influential Congressman exclaimed to his visitors.<sup>40</sup>

On other occasions, public opinion has been a force for interventions in the name of peace. When his aides brought him news of the Srebrenica massacre in July 1995, US President Bill Clinton reportedly exploded, ‘I’m getting creamed!’ A few days later, he complained to his foreign-policy advisers that the war in Bosnia was ‘killing the US position of strength in the world’ (quoted in Woodward 1996, pp. 260-261; see also Danner 1997). Ending the war had become identified with the president’s own stature and with the US national interest. Yet this same example suggests that it would be a mistake to overstate the impact of the so-called ‘CNN effect.’ For three years prior to Srebrenica, the international news media had carried vivid news reports of the carnage in the former Yugoslavia, yet this failed to prompt

decisive action by the international community. It is not raw images that drive policy, Michael Ignatieff (1988) observes, but the ‘stories we tell’ about these images. Political will to intervene in Bosnia emerged only when the war came to be seen not just as a story of human suffering, but as one of failed American and European leadership.

Nevertheless, the Bosnian case showed that when public opinion is sufficiently mobilized – and political leaders are sufficiently accountable – it can lift peace to the top of the policy agenda. In the wake of a negotiated ending to a civil war, this can translate into backing for proactive peacebuilding assistance, helping to overcome the obstacles posed by competing geopolitical and economic objectives. In effect, public opinion can make a ‘necessity of virtue’ (Sherman 1998).

### *Reforming donor agencies*

Even if governments make peacebuilding their overriding priority war-torn societies, the internal dynamics of the aid agencies themselves can pose additional impediments to the effective use of aid for this purpose. Peacebuilding requires aid agencies to move beyond business-as-usual practices in several ways. First, they must reorient their internal incentive structures to reward performance not in terms of the quantity of aid disbursed, but rather in terms of the effects of aid on the objective of building peace. Second, they must overcome ideological biases that single-mindedly favor ‘efficiency’ over equity and the ‘free market’ over state interventions. Third, they must work to achieve greater coordination with other donors, tempering their impulse to protect their own autonomy. Finally, they must become more transparent and accountable to the public.

#### *(i) Changing incentive structures*

Aid donors often measure their own success in terms of the amount of money they disburse. More aid is axiomatically better than less. In the early decades of foreign aid, inadequate investment in physical and human capital was widely seen as the main barrier to economic development. ‘If money was the problem,’ a recent World Bank study observes, ‘then

“moving the money” was an appropriate objective for aid and aid agencies’ (World Bank 1998c, p.10). This translated into internal incentive structures that emphasized the quantity of aid disbursed over the quality of results achieved. Despite much discussion of the need to shift to outcome-based performance measures, the baneful effects of the ‘approval and disbursement culture’ persist. The World Bank study concluded, for example, that project managers continue to see the volume of loan commitments as an end in itself and appear to be willing to permit ‘substantial’ sacrifices in quality in return for modest increases in the quantity of lending (World Bank 1998c, p. 142).

The incentives facing individual staff members often reflect those facing their employers. ‘Both donor and recipient have incentive systems that reward reaching a high volume of resource transfer, measured in relation to a predefined ceiling,’ a study for the Swedish International Development Authority remarks. ‘Non-disbursed amounts will be noted by executive boards or parliamentary committees and may result in reduced allocations for the next fiscal year’ (Edgren 1996, cited in World Bank 1998c, p. 117). The result is sometimes characterized as a ‘use-it-or-lose-it’ syndrome.

When aid is provided in the form of loans, as opposed to grants, there is an added incentive: new lending helps ensure that recipients continue to service past debts. In December 1995, for example, the IMF heralded a \$45 million loan to Bosnia – the first loan issued under the Fund’s new emergency credit window for ‘post-conflict’ countries – as ‘a new beginning’ (*IMF Survey* 1996). But the loan’s purpose was simply to allow the new Bosnian government to repay a bridge loan from the Dutch government, which in turn had been used to repay Bosnia’s assessed share of the former Yugoslavia’s arrears to the IMF. Old Yugoslavian debt was thereby transformed into new Bosnian debt. A similar exercise has been repeated in other postwar countries. In 2002, for example, the Democratic Republic of Congo’s arrears to the World Bank were cleared through a bridge loan from Belgium and France that was repaid with an Emergency Recovery Credit provided by the Bank (Alvarez-Plata and Brück 2007, p. 266).

Peace conditionality, in particular, does not fit happily into these incentive structures. If institutions face penalties for withholding aid, but not for disbursing it unwisely, they can be expected to put a premium on ‘moving the money.’ If individual staff members are rewarded for saying ‘yes’ but not for saying ‘no,’ they will act accordingly. Effective peacebuilding assistance requires that the performance of individuals and agencies be judged not in terms of how much aid they disburse, but in terms of how effectively this aid supports the goal of building a viable peace.

*(ii) Overcoming ideological biases*

Ideological fashions within the aid agencies can pose an additional impediment. In keeping with the precepts of neoclassical economics, for instance, donors frequently focus narrowly on the goal of economic ‘efficiency,’ neglecting distributional issues. This approach is singularly ill-suited to war-torn societies, where the prospects for peace often hinge on fragile balances of power. In assessing development projects and economic policies, donors must ask not only whether total benefits will exceed total costs – the usual bottom line in terms of efficiency – but also how the distribution of these benefits and costs will affect vertical disparities of class and horizontal cleavages of ethnicity, religion, race, and region. These distributional consequences may be hard to measure, as noted above, but this does not mean that they can be safely ignored.

The ideological antipathy in some donor agencies to state interventions in economic affairs can also prove to be counter-productive in the wake of a civil war. If, for example, donors insist on tariff reductions in pursuit of the Holy Grail of free trade, this may reduce government revenues that are urgently needed to finance the costs of peace. Moreover, in some cases tariffs can help ease social tensions by protecting the livelihoods of vulnerable domestic producers. In postwar El Salvador, for example, producer prices for maize and beans, the mainstays of peasant farming, were undercut by cheap imports. Nevertheless, the World Bank lauded the government’s steep reductions in agricultural tariffs, arguing that ‘to reintroduce protection could set precedents that could be extremely difficult to reverse in the future’ (World Bank 1998b, p. 41). This doctrinaire stance not only ignored the possibility



that tariffs can be a ‘second-best’ remedy for market imperfections (including foreign agricultural subsidies and overvalued exchange rates that artificially depress world market prices), but also ignored the importance of an economically viable small-farm sector for the sustainability of the country’s peace process. Policies ought to be judged in light of their impact on economic and political reconstruction, not on the basis of *a priori* ideological dogma.

*(iii) Improving inter-donor coordination*

Effective aid for peace also requires donors to grow beyond business as usual by improving coordination among themselves.<sup>41</sup> If one donor insists, for example, that local authorities take steps to encourage minority returns in order to receive housing reconstruction aid, while another offers similar aid with weaker conditions or none at all, the lowest common denominator will prevail.

Inter-donor coordination may be more feasible following a civil war than in ‘normal’ circumstances. In addition to the potential rewards being higher, international engagement in the peace process often leads to the creation of some coordination mechanisms inside and outside the country. The most ambitious examples of in-country coordination to date have been the Office of the High Representative (OHR) in Bosnia, and the Joint Liaison Committee and Local Aid Coordination Committee in Palestine. These were complemented by external coordination via the Peace Implementation Council steering board in the case of Bosnia, and the Ad Hoc Liaison Committee (AHLC) in the case of Palestine. The establishment of these coordination mechanisms was far from smooth, however, and their success in overcoming inter-donor rivalries has been a matter of degree.

Although the OHR’s powers in Bosnia are about as close as the contemporary world comes to a colonial administration, its ability to impose consistent policies on the donors is quite limited. The Dayton Peace Agreement specified that in dealing with aid agencies, the High Representative shall ‘respect their autonomy within their spheres of operation, while as necessary giving general guidance to them about the impact of their activities on the

implementation of the peace settlement.’<sup>42</sup> In other words, the OHR must rely on persuasion, not authority.

The difficulty in creating the AHLC to oversee aid to the Palestinian Authority is another telling example. The major powers decided to establish the committee in October 1993, shortly after the Oslo accord between Israel and the PLO. Intense rivalries immediately emerged over the make-up of the committee. Tensions over who would chair the AHLC became so acute that at one point the Israelis and Palestinians jointly offered to mediate between the US and the EU – a rather striking turn of events. The battle ended with a compromise: Norway became the chair.

In choosing the extent to which they will coordinate their programs and policies, donors must weigh the benefits of greater coherence against the costs of reduced autonomy.

*(iv) Increasing donor transparency and accountability*

The reforms in donor practices that are suggested above could be facilitated by moves toward greater transparency and accountability in decision-making. The credibility of donor calls for ‘good governance’ in aid-receiving countries will be strengthened if they practice what they preach. Stronger public oversight could encourage the agencies to elevate results above disbursements, question ideological presuppositions, and better coordinate their activities. Increased transparency and accountability will not guarantee these reorientations, but they could help them along.

*Priorities and sequencing*

Policy coherence requires not only inter-agency coordination but also agreement on common goals and priorities. This requires agreement on ends of policy as well as harmonization of the means. Policy coherence at this deeper level poses profound challenges.

Much policy discourse about war-to-peace transitions centers on two policy goals: ‘security’ and ‘development.’ The relation between the two has attracted a great deal of attention in the wake of the September 2001 attacks in New York and Washington, DC, but the issue has a much longer history. In his memoir *The Essence of Security*, published as he left the helm of U.S. Department of Defense to assume the presidency of the World Bank, Robert McNamara (1968, p. 149) argued that development is crucial for security. ‘In a modernizing society security means development,’ he wrote. ‘Without internal development of at least a minimal degree, order and stability are impossible. They are impossible because human nature cannot be frustrated indefinitely.’

Yet a recent operational note on policies in ‘fragile states,’ prepared jointly by the United Nations Development Group and World Bank (2005, p. 4), points out that a single-minded focus on economic development ‘has in cases led to serious shortfalls in funding for critical interventions in the political and security spheres, interventions that are critical to creating an environment for economic and social programs to deliver benefits for the population.’ Moreover, not all development policies are equally supportive of security: ‘Well designed economic and social programs can contribute to political stabilization; ill-timed or badly targeted programs can undermine it’ (*ibid*).<sup>43</sup>

By the same token, a single-minded preoccupation with security can undermine development. In Afghanistan, as discussed above, fiscally unsustainable security expenditures threaten to overwhelm long-term development needs. In Palestine, Brynen (2007) depicts the tensions between efforts to shore up the PA’s patronage-based political order and the need for an economic environment conducive to investment and growth. In Cambodia, Smoke and Taliercio (2007) similarly delineate a divergence between a ‘peace and security’ approach to public finance, which regards the existing patronage system as necessary for political stability, and a ‘developmental’ approach that advocates reform in the name of economic growth and poverty reduction.

At first blush, these examples simply pit short-run expediency against longer-run goals. But there are deeper contradictions that are grounded in competing visions of both

security and development. Is security merely the absence of violent conflict, sometimes termed ‘negative peace’? Or is it the absence of social tensions that threaten to precipitate conflict, sometimes termed ‘positive peace’? The former often can be achieved, at least for a time, by means of repression and intimidation. The latter demands political inclusion and shared perceptions of justice. Similar questions can be posed about development. Is this defined simply as economic growth? Or to qualify as genuine development, must growth be inclusive?

A further source of divergence arises from the differences between the priorities of donor governments and those of the people who are on the receiving end of aid. When international actors intervene in the name of security, whose security is paramount: the ‘human security’ of the populace, the ‘national security’ of the government, or the ‘security interests’ of the donor governments? Similarly, is success of the development front to be measured in terms of local livelihoods, or GNP, or benefits to external commercial interests?

Once we recognize the divergences among these goals, getting priorities right cannot be seen as merely a technical challenge. It is a political challenge, too, posing fundamental choices about values and the kind of world in which we want to live. The premise of this paper is that in wartorn societies, building a durable peace should be the top priority for public policy, the goal around which diverse policies must cohere.

Yet even if there is general agreement on this premise, there is considerable disagreement as to the proper sequencing of policies, or what might be termed prioritization amongst priorities. These disagreements do not simply reflect the great uncertainties and lack of adequate information that characterize post-conflict environments; they also reflect the competing interests within donor governments and the prevailing incentive structures within aid agencies that have been described above. Three systematic features of donor behavior contribute to poor sequencing:

(i) *Coordination failures*: Some sequencing problems result simply from the division of labor amongst multiple agencies and the failure to share information and coordinate actions. A recent study offers the common-sense recommendation that donors should “pay attention to vital prerequisites before launching any ambitious reform programs,” noting as an example that “sweeping civil service reform and rapid military downsizing can be counterproductive if effective compensation and assistance packages are not in place” (Timilsina and Dobbins, 2007, p. 3). The problems of inter-agency coordination are compounded, however, by inter-agency competition and rivalry. A recent review of post-conflict needs assessments, conducted jointly by the United Nations and the World Bank, observes that “the dramatic needs in post-conflict settings generate pressure towards a comprehensive rather than a strategic approach,” generating over-ambitious plans and unrealistic expectations (United Nations and World Bank, 2007, p. 5). The review calls for steps to “re-engineer” the needs assessment process “by building in mechanisms, clearly articulated criteria, and incentives for ‘real’ prioritization and sequencing” (*ibid.*, p. 12). Yet it recognizes that political timing “puts a premium on the assessment generating a costed report that carries an impressive ‘price tag’” so as to “harvest significant support from donor countries while the ‘CNN effect’ is still active” (*ibid.*, p. 31). The result is a scramble to stake claims in the post-conflict aid rush, a dynamic that militates against selectivity and sensible sequencing.

(ii) *Misplaced priorities*: The competing interests of donor governments and the ideological biases of aid agencies further compound the problem. An example of competing interests is the current policy of putting a high priority on poppy eradication in Afghanistan in the name of combating the illicit narcotics trade. As Richard Holbrooke (2008) recently wrote, eradication “pushes farmers with no other source of livelihood into the arms of the Taliban without reducing the total amount of opium being produced.” By putting the eradication cart before the security horse, the drug-control policy yields perverse results. An example of ideological bias is the over-zealous promotion by international financial

institutions of privatization and ‘liberalization’ (e.g., sharp reductions in tariffs), which as Timilsina (2006, p. 91) concludes, on the basis of case studies of Haiti, Mozambique and Cambodia, “may not be an immediate priority in every post-conflict country.”

(iii) *Myopia*: Sequencing problems are also exacerbated by the tendency to let short-run demands crowd out long-run needs. This helps to explain the bias against local suppliers, illustrated earlier by the example of foreign sourcing of school furniture in East Timor. It helps to explain the ‘dual public sector’ syndrome, in which the bypassing of the state is rationalized on the basis of short-run efficiency while neglecting the longer-term tasks of building the capacities needed for an effective and legitimate state. It also helps to explain the common failure to engage with civil society and enlist broad public participation in decision-making, processes that are seen as desirable in theory but too time-consuming to implement in practice.<sup>44</sup>

In sum, the obstacles to successful postwar reconstruction and peacebuilding are not only located within the wartorn societies themselves. There are also deeply rooted obstacles located in the policies and priorities of the international community and the donor agencies. In the end, more effective aid for the reconstruction of wartorn societies will require the reconstruction of aid itself.

## Notes

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<sup>1</sup> There is ample precedent. For example, in 1990 the U.S. retaliated for Yemen's vote against a resolution authorizing force against Iraq by cutting off aid. See Zeller (2003).

<sup>2</sup> It is now widely recognized that other revenue sources (e.g., value-added taxes) seldom succeed in replacing lost tariff revenues on a one-for-one basis. See Khattry and Rao (2002) and Baunsgaard and Keen (2005).

<sup>3</sup> A World Bank study estimates that in the first five years after a peace accord, a country has a 44% chance of reverting to war (Collier et al., 2003, p. 83).

<sup>4</sup> 'The neoliberal recommendation to national policy makers is that they should insist on maintaining inflation rates of 3-5 per cent,' writes McKinley (2006, p. 352), 'even though there is little empirical evidence to suggest that inflation rates above that level, or even above 10 per cent, have an adverse effect on growth.' For discussion of alternatives to inflation targeting, based on 'real-economy' targets such as employment, see Epstein (2003).

<sup>5</sup> Personal interview, Phnom Penh, November 1998.

<sup>6</sup> 'Donor Statement' dated 6 October 1995, cited by Christian Michelsen Institute, *Evaluation of Norwegian Assistance to Peace, Reconciliation and Rehabilitation in Mozambique* (Oslo: Ministry of Foreign Affairs, 1997), p. 49.

<sup>7</sup> A revised version of Boyce *et al.* (1995) was published as Boyce, ed., *Economic Policy for Building Peace*.

<sup>8</sup> Some observers attributed funding shortfalls to fiscal austerity measures demanded by IMF and World Bank conditionalities (see, for example, Orr, 2001, p. 167). A careful analysis of policy formation in the early years of the Salvadoran peace process suggests, however, that the core problem was the unwillingness of the government to fund these programs, rather than its inability to do so (see Wood, 1996 and Boyce, 1996).

<sup>9</sup> For further discussions of peace conditionality, see Frerks (2006) and Goodhand (2006).

<sup>10</sup> International Bank for Reconstruction and Development, *Articles of Agreement*, Article III, Section 5(b).

<sup>11</sup> In November 2007, for example, the carrot of EU accession helped persuade Bosnian Serb leaders to accept new parliamentary voting rules, resolving "the most serious political crisis since the end of the 1992-1995 war" (Associated Press, 2007).

<sup>12</sup> For discussion, see Pronk (2001) and Boyce (2002b).

<sup>13</sup> For an analysis that represents IMF conditionality as an alliance in which the Fund supports a reformist government in the face of domestic interest groups opposed to reform, see Drazen (2002). More generally, there donors also could ally with like-minded domestic groups outside the government or within a heterogeneous government. For further discussion of aid and cross-national coalitions, see Milder (1996).

<sup>14</sup> See the UNDPKO/World Bank joint review of GEMAP by Dwan and Bailey (2006, pp. 20-21). Referring to the issue of domestic allies, the authors argue that more could have been done to engage with civil society in Liberia: 'While caution in appearing to circumvent national authorities is an important consideration, international partners could have done much more to facilitate public debate on economic governance as well as to build more informal, off-line strands of support among key actors.'

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<sup>15</sup> A ministerial meeting of the Peace Implementation Council endorsed this principle in May 1997, recommending that ‘assistance for housing and local infrastructure should be dependent on the acceptance of return’ of refugees and displaced persons (*Political Declaration from Ministerial Meeting of the Steering Board of the Peace Implementation Council*, Sintra, Portugal, 30 May 1997, paragraph 46).

<sup>16</sup> In the case of Rwanda, for example, Obidegwu (2003, p. 20) observes, ‘With the flood of international NGOs, relief and development agencies into Rwanda after the genocide, the government service could not compete for the few qualified people available.’ In the case of Afghanistan, Ghani *et al.* (2005, p. 10) contrast the salaries of \$1000 per month paid by donor agencies to \$50 per month paid by the government, and remark: ‘Unsurprisingly, there has been a brain drain from the managerial tier of the government to menial positions in the aid system. The people might have judged it to be fair had the disparity in wages resulted from a competitive market; however, the problem is that both bureaucracies are funded from the resources of the aid system and the rules for remuneration are arrived at by bureaucratic fiat rather than by open processes of competition.’

<sup>17</sup> Voicing the last two of these concerns in an analysis of aid to Mozambique, Arndt *et al.* (2006, p. 1) conclude: ‘[T]he proliferation of donors and aid-supported interventions has burdened local administration and there is a distinct need to develop government accountability to its own citizens rather than donor agencies.’

<sup>18</sup> In USAID’s program for building schools and health clinics in Afghanistan, for example, ‘Employees of a Maryland-based nonprofit relief agency hired to monitor construction quality demanded a \$50,000 payoff from Afghan builders – a scene captured in a clandestine videotape obtained by *The Washington Post*’ (Stephens and Ottaway 2005).

<sup>19</sup> In Afghanistan, the former planning minister ‘has become one of the most popular politicians in the country by campaigning against NGOs [non-governmental organizations], which he has said are more dangerous than al-Qaeda’ (Rubin 2005, p. 101).

<sup>20</sup> In exceptional circumstances, dual-control systems can also be applied to domestic revenues (for discussion, see Le Billon 2003). An example is the Governance and Economic Management Assistance Program (GEMAP) instituted in postwar Liberia in 2005.

<sup>21</sup> Gupta *et al.* (2004) find a negative relationship between government revenue and conflict in a sample of low- and middle-income countries. Addison *et al.* (2004) report that the intensity of conflict, as well as its presence, negatively affects the tax/GDP ratio.

<sup>22</sup> Examining evidence from a large sample of developing countries, Gupta *et al.* (2003) find that grant aid, in particular, tends to lower revenue efforts; in countries with high levels of corruption, ‘the decline in revenues completely offsets the increase in grants.’ A recent IMF study (Heller 2005, pp. 4, 21) cites disincentives to mobilize domestic resources as a ‘moral hazard’ of external aid flows, observing that ‘some African countries with among the highest ratios of aid to GDP are also those that have stubbornly low tax ratios.’

<sup>23</sup> Thus at the 1998 meeting of the Consultative Group for Guatemala, the IMF representative urged the government to ‘resist pressures to increase import duties or delay the scheduled reduction in customs tariffs,’ arguing that ‘these actions will have adverse effects on output growth’ (quoted in Boyce 2002a, p. 47).

<sup>24</sup> Camdessus warned that without a significant increase in the tax effort Guatemala could not expect to receive substantial international aid, and noted that the IMF would have preferred an even more ambitious revenue target. See Boyce (2002a, pp. 41-42) and Jonas (2000, pp. 185-186).

<sup>25</sup> Thus among dozens of examples of EU budget-support conditionality listed in a report by the European Commission (2005), the Mozambique case is the sole example of revenue-side conditionality.



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<sup>26</sup> ‘The Afghanistan Compact,’ London Conference on Afghanistan, 31 January – 1 February 2006, p. 12. Available at <http://www.unama-afg.org/news/londonConf/docs/06jan30-AfghanistanCompact-Final.pdf>.

<sup>27</sup> Under the Convention on the Privileges and Immunities of the United Nations, UN officials are ‘exempt from taxation on the salaries and emoluments paid to them by the United Nations’ (United Nations 1946, sec. 18b). The United States did not sign the Convention (whereas virtually all other member states did so), and hence US citizens and permanent residents employed by the UN are liable for US income taxes. To redress the resulting disparities, a ‘staff assessment’ is deducted from the nominal gross salaries of UN employees and paid into a Tax Equalization Fund. The Fund is used for two purposes: (i) to reimburse income-tax payments by US citizens employed by the UN, so that net salaries of UN personnel are unaffected by the employee’s US tax status; and (ii) to offset the UN budget dues of the other member states that are signatories to the Convention, while the US government receives no offset by virtue of the fact that it taxes UN employees. The staff assessment is sometimes characterized as an ‘internal tax’ administered by the UN, a description that is misleading in that its purpose is ‘to place United Nations staff members subject to taxation [i.e., US citizens and permanent residents] in the position they would have been if their official emoluments were not taxed’ (United Nations Secretariat 2007, p. 5).

<sup>28</sup> For an example of an assessment, see Goodhand (2001).

<sup>29</sup> For an exception, see the data on the provincial distribution of revenue and expenditure in Burundi that are presented by Ngaruko and Nkurunziza (2005).

<sup>30</sup> For further discussion of the ‘dark side’ of social capital, see also Putzel (1997), Ostrom (1999), and Field (2003, ch. 3).

<sup>31</sup> The two can go together. In the war in Bosnia, the destruction of the magnificent medieval bridge between east and west Mostar came to symbolize the breakdown of trust between Muslim Bosniaks and Catholic Bosnian Croats.

<sup>32</sup> For a discussion of ‘spoilers,’ including the distinction between ‘limited’ and ‘greedy’ spoilers who are responsive to changing incentives and ‘total spoilers’ who are not, see Stedman (1997, 2002).

<sup>33</sup> For discussion, see Boyce (2002a).

<sup>34</sup> For a review of the rather sparse literature on the distributional impacts of taxation in developing countries, see Gemmill and Morrissey (2005).

<sup>35</sup> This figure excludes counter-narcotics expenditures, which would push the ratio closer to 600%.

<sup>36</sup> The supposed efficiency advantages of foreign sourcing can be illusory. In Afghanistan, for example, where USAID funds for rebuilding schools and health clinics were routed through a New Jersey-based private contractor, press reports have revealed inordinate delays, shoddy construction, and ‘extraordinary costs’ in the words of a USAID official (Stephens and Ottaway 2005; see also Rohde and Gall 2005).

<sup>37</sup> In the end, some of the school furniture was procured locally, albeit with delays. For discussion of the scope for greater local procurement in postconflict operations, see Carnahan, Gilmore and Rahman (2005).

<sup>38</sup> Interview with a United Nations human rights official, Phnom Penh, November 1998.

<sup>39</sup> For discussions of Chinese aid to Africa, see Davies (2007), McGreal (2007), Zafar (2007), and Huse and Muyakwa (2008). Similar issues have arisen in Cambodia, where Chinese aid in 2006 undermined an initiative by other donors to attach anti-corruption conditions to a new aid package (Hauter 2007). For recent signs of shifts in Chinese policy, see Kleine-Ahlbrandt and Small (2008).

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<sup>40</sup> Personal interview with a senior international official who participated in these meetings, Gaza City, March 1998.

<sup>41</sup> In addition to coordination across different donor governments, there are often serious coordination problems among the various agencies of any single donor government; see, for discussion, Patrick and Brown (2007).

<sup>42</sup> *The General Framework Agreement for Peace in Bosnia and Herzegovina*. Annex 10, Article II, Sections 1(a) and 1(c).

<sup>43</sup> In a similar vein, Smith (2004, p. 44) warns: 'It is, unfortunately, likely that where development cooperation is the default conceptual and planning mode, the specifics of peacebuilding – the war-defined context – will slip out of focus. The results of that could be serious.'

<sup>44</sup> Underscoring this point, a recent critique of security sector reform programs concluded, "As difficult or seemingly counterproductive as it may seem in the short-term, participatory reform processes involving a broad range of local actors with a stake in security governance are critical in order to embed reform in wider social structures" (Bryden, Donais and Hanggi, 2005, p. 29).

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