

Executive Summary

Until 1990s, most development cooperation was carried out in the form of stand-alone projects. But as it gradually became apparent that these projects present numerous problems from the view of aid effectiveness, Programme-Based Approach(PBA) was introduced in this regard, in order to deal with these issues and to promote quality of aid. According to OECD DAC's definition, PBA is "a way of engaging in development cooperation based on the principles of co-ordinated support for a locally owned programme of development strategy, such as a national development strategy, a sector programme, a thematic programme or a programme of a specific organization", satisfying PBA's four principles(OECD DAC, 2006b)⁴⁾. PBA came into its own as it has contributed to paradigm transformation in terms of aid effectiveness from donors-oriented and fragmented projects in 1990s to an integrated programme-based approach. However, due to its ambiguousness of PBA's definition and duplication of the use of country system as one of PBA's principles and as an independent target in Busan Global Partnership for Effective Development Cooperation (GPEDC), PBA was not selected as an independent indicator in the GPEDC. Instead, it has been dealt specifically within the framework of the use of country system.

A discussion on the use of country system has been also initiated with the emergence of a PBA in the aspect of promoting aid effectiveness. It soon gained momentum in terms of country's ownership and donors' harmonization from the

4) PBA's four principles:

- ① Leadership by the host country or organization;
- ② A single comprehensive programme and budget framework;
- ③ A formalized process for donor co-ordination and harmonization of donor procedures for reporting, budgeting, financial management and procurement; and
- ④ Efforts to increase the use of local systems for programme design and implementation, financial management, monitoring and evaluation.

Paris Declaration, and therefore, the use of country system was selected as an independent indicator in the GPEDC in 2011.

Against this background, opportunities to use country system have been increasing as the international society seeks to diversify aid modalities in carrying out aid programmes. However, as using country means to provide financial assistance based on putting full confidence in and recognizing the validity of partner countries' systems, the need for donor countries to understand, mitigate and monitor the fiduciary risk has been greatly increased. This applies also to partner countries. The necessity and obligation to manage the fiduciary risk for partner countries have grown as they need to promote the quality and the use of their systems.

However, according to OECD's monitoring report on the Paris Declaration, 'Aid Effectiveness 2011: Progress in Implementing the Paris Declaration(2012),' it shows that while some progress has been made in promoting PBA and the use of country system recommended in the Paris Declaration, both of them fail to meet the target and only a small improvement was observed. In addition, OECD DAC reported that in case of the use of country system, its poor implementation performance was due to donor countries' tendency to avoid fiduciary risk such as donors' fears of financial misuse and donors' preferences to use parallel structures rather than managing it(OECD DAC, 2012). Likewise, the issue of promoting PBA and the use of country system brings to a conclusion that it is critical to assess the robustness of countries' systems and to keep monitoring and developing them in order to effectively manage and control potential fiduciary risks.

To keep up with the international discourse on the aid diversification, KOICA also endeavors to diversify aid programmes in order to promote aid effectiveness and therefore opportunities to use partner countries' systems are greatly increasing. However, due to a lack of a systemic modalities and procedures to

analyze and assess fiduciary risks, which limits actual utilization of country system, the need to closely examine and analyze fiduciary risks has arisen.

In this regard, this study deals with promoting the use of PBA and country system focusing on managing fiduciary risk, based on related preceding researches. Especially this study includes the case of DFID's guideline on managing fiduciary risk, which gives invaluable implication as one of the leading donors in understanding, mitigating, monitoring potential risks in using country systems.

This study is structured in six parts: the first part gives an overview on the concept of the study and the second part explains the definition of the PBA and its use and how the discussion of PBA has evolved after the Paris Declaration. In the third part, it also provides explanation on the definition and concepts of the use of country's financial and procurement system and also on the flow of its discussion. In the second and third parts, it includes the monitoring result of the Paris Declaration. The fourth part examines specific instruments to assess and monitor countries' systems and how grade system works in each instruments. The fifth part will examine and analyze DFID's case through DFID's 'How to note: Managing Fiduciary Risk when Providing Financial Aid(2011)' with its implication for KOICA and conclusion will be suggested in the final part. The implication for KOICA is as follows:

First of all, proper understanding on 'risk' should be based on before utilizing a PBA and country system. DFID specifies that as fiduciary risk can be treated and tolerated, the purpose of assessing fiduciary risk is not to eliminate fiduciary risk but to ensure that we understand, accept and own the risks we are taking, and manage risks effectively(DFID, 2011). Likewise, when carrying out aid programmes, managers should understand that the guideline on managing fiduciary risk is not to remove the risk or possibility of the risk but to understand the risk in advance so that the risk can be mitigated and prevented beforehand.

Secondly, country offices should take the lead in managing fiduciary risk. It is distinctive that DFID assesses and manages fiduciary risk under the leadership of its country offices. This is because countries' fiduciary risk tends to appear differently according to their own context in the aspect of governance, history, politics and economy. In this regard, country offices are placed more closely with partner countries and this facilitates interactive communication between the two, which leads to better management of fiduciary risk. KOICA has also implemented 'KOICA's Guideline on the Use of Country System(2014a)⁵⁾,' which specifies that country offices should take the lead throughout the project cycle from the selection of projects to report and monitoring. Furthermore, KOICA endeavors to promote aid effectiveness by promoting decentralized projects through 'KOICA's Decentralization Roadmap(3rd Action Plan)(2014b)⁶⁾'. It is recommended to include and consider fiduciary risk management in the 'KOICA's Decentralization Roadmap' in order to facilitate managing fiduciary risk and to promote effectiveness of the projects. In addition, in order for country offices to actually take the lead, it is imperative to give authority to country offices and to strengthen the given authorities.

Thirdly, managing fiduciary risk finally adds up to 'the issue of judgement' by relevant project manager and there is a need to understand that assessments through these instruments such as Public Expenditure and Financial Accountability (PEFA) and Methodology for Assessing Procurement System (MAPS), are only a groundwork for project managers to make decisions. For example, when DFID assesses fiduciary risk, they strongly recommend utilizing assessment instruments such as PEFA. But as the objective of the result of PEFA and DFID's Fiduciary Risk Assessments(FRAs) is different, DFID clarifies that the result of PEFA cannot be alternatives or direct results of DFID's decision-making. Moreover, DFID makes sure that there is no one-size-fits-all answer for all countries and circumstances.

5) KOICA. (2014a). KOICA's Guideline on the Use of Country System, Internal Document.

6) KOICA. (2014b). KOICA's Decentralization Roadmap(3rd Action Plan), Internal Document.

Therefore country offices and project managers should put efforts to gain not only information through assessment instruments but also country-specific information such as governance, politics, economics and etc. If needed, hiring local consultant or participating partner countries' officials in the project cycle can be helpful for in managing risks.

Last but not least, cooperating with partner countries is the most effective way when managing fiduciary risk. In order for countries' offices to understand, mitigate and monitor country systems' risks, a bunch of high quality information is needed from partner countries. To facilitate this process, solid cooperation with partner countries is critical. Especially, DFID highlights understanding a partner country's overall PFM(Public Financial Management) cycle when it comes to using safeguards, and also emphasizes building a partnership with partner country's government, civil society, NGOs, etc. In monitoring stage, utilizing performance indicators, targets and procedures based on a partner country's reform program is recommended when country offices need to set performance indicators, targets and procedures. Likewise, a close cooperation with partner countries is imperative in managing fiduciary risk. In this respect, a regular conversation with partner countries and participating officials from partner countries in the aid programme cycle are imperative for effective risk management.

This study focuses on the management of fiduciary risk when utilizing a PBA and country system in order to promote aid effectiveness and diversification through examining relevant instruments and DFID's case. As a fiduciary risk is ever-present and irregular, it is difficult to perfectly remove or manage, but understanding properly, mitigating and monitoring the fiduciary risk is critical for Korea's aid programmes to continuously advance and to contribute to promoting aid effectiveness. Therefore, in order for KOICA to promote using PBA and the country systems, it is time to actively consider implementing the system of managing fiduciary risks.