

# EVALUATION DEPARTMENT

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## Basis for Decisions to use Results-Based Payments in Norwegian Development Aid

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# 1. Introduction

## **BACKGROUND**

With the increasing attention that has been given to aid effectiveness and more predictable outcomes of development cooperation, various forms of results-based payment have attracted interest. Bilateral donors, multilateral development agencies and their developing country partners have all subscribed to the “managing for results” principles that emerged from the Paris Declaration on Aid Effectiveness (2005) and results-based payments are usually discussed in these terms. It may be useful to keep in mind that in addition to their reputed improvements in terms of aid effectiveness, results-based payments also seem to hold a political attraction by offering assurances to donor country electorates that expenditure of development funds is tied to results.

A common feature of traditional official development assistance (ODA) has been provision of inputs to the development process and a primary concern with the actions and processes that these would feed into. The emphasis on results-based payments has implied a shift

in focus from inputs and processes to outputs and outcomes further along the results chain. In 2011, ODA registered by OECD reached US\$ 133.5 billion, while total disbursements for results-based payments broke the US\$ 5 billion barrier in 2010 (Pereira & Villota, 2012:6). In Norwegian development cooperation, results-based payments were first used in the health sector (GAVI support). Two large results-based initiatives, the Health Results Innovation Trust Fund (HRTIF) and Norway’s International Climate and Forest Initiative (NICFI), were established in 2007 and 2008, respectively. Pilots have later been started also in the energy sector.

## **AIM AND CONTENT OF REPORT**

The aim of this report is to describe how the decisions to use results-based payments in Norwegian development cooperation were made and the considerations that formed the basis for these decisions. The report describes the political context and background for the decisions to use results-based payments in the health sector and in the climate and

forestry and clean energy initiatives. It discusses the extent to which evidence was used to inform decisions and asks whether the advantages and disadvantages of results-based payments were compared to traditional funding modalities. Finally, it provides an overview of the theoretical basis for results-based payments as it has evolved and been applied in relation to the Norwegian initiatives.

A companion report, *Experiences with Results-Based Payments in Norwegian Development Aid*, describes the characteristics of the various results-based initiatives in greater detail and summarizes the documented experiences to date.

The reports are written on the basis of a desk review, supplemented with interviews with key people involved in Norwegian results-based initiatives. A description of the methods used, including a list of people interviewed and a comprehensive bibliography is available in an annex to each report.

## 2. Decisions to use Results-Based Payments

A wide array of terms and designations are used to characterize and distinguish various forms of results-based payments, and the nomenclature is still not entirely clear. The common approach is to use payment by results (PBR) as the most inclusive term, encompassing all the various results-based approaches. The core aspects of payment by results mechanisms are that 1) payment is based on achieved results, and 2) the relationship between payment and results is pre-defined. PBR arrangements are usually classified either as results-based aid (when the recipient is a government) or results-based financing (when the recipient is a lower-level administrative unit, service provider, or user). For the purpose of this paper, we will focus on PBR mechanisms that primarily reward outputs and outcomes.

### HEALTH

The most widespread use of PBR mechanisms in Norwegian development cooperation is in the health sector. The first experience with results-based payments was the reward mechanism built into the Immunization Service Support (ISS) mechanism of GAVI (the Vaccine Alliance),

which provided recipient governments with 20 USD per additional child vaccinated.

The decision to link payments with the achieved number of vaccinations was a negotiated outcome among the donors. Initially, donors were discussing whether to provide budget support or more direct support to infrastructure to strengthen vaccination services, and the donors had different preferences. When the idea of paying per vaccinated child came on the table, however, it was a concept that all donors could buy into. It was realized that the approach was new and innovative, but the intuitive appeal of the concept compelled the donors.

Behind the idea was the leader of the GAVI secretariat, Tore Godal. His return to Norway in 2006 marked the start of Norway's engagement to promote results-based payment also in other areas of health sector support.

The idea of using results-based payments received a strong buy-in from Prime Minister Stoltenberg, and the decisions to promote these approaches in health were taken at high political level, without elaborate bureaucratic processes.

Norway's initial focus was on demand side incentives to promote the utilization of maternal and child health services. Driven by the political priority of channelling more resources through the multilateral system, Norway approached the World Bank to seek out a partnership to promote demand side incentives. At the time, the World Bank already supported various results-based approaches, but their focus had been more on supply-side incentives (performance based financing) in countries such as Rwanda, Cambodia and Argentina. Consequently, when Norway set up the Health Results and Innovation Trust Fund (HRITF) in the World Bank in 2007, the focus therefore came to be on results-based financing in general, including both supply- and demand-side incentives. The trust fund is currently the main mechanisms for implementation of results-based payments in Norwegian development cooperation, with projects in more than 30 countries.

Norway also embarked on results-based financing in bilateral development cooperation in the health sector in Tanzania, Malawi, India and Nigeria. In all cases, key decisions were

taken at the highest political level. For instance, the programme in Tanzania came as a result of a meeting between President Kikwete and Prime Minister Stoltenberg in Oslo in 2007, where Norway agreed to support efforts to reduce maternal mortality in Tanzania. It was quickly decided that the support would come in the form of results-based financing, and the subsequent work by the bureaucracy focused on how this could be implemented in the most effective way. The initiative in Malawi, funded jointly by Norway and Germany, was launched in a meeting between Jens Stoltenberg and Angela Merkel in 2011. At this time, Norway's role in promoting results-based payments had become more established, and Norad played a more active advisory role. Key decisions were again taken at a high political level, not as normal bureaucratic decisions.

A major motivation for adopting results-based payments as a strategy was the lack of strong evidence of results from traditional health sector support, combined with a much stronger focus on results in development cooperation in general.

## **CLIMATE AND FORESTRY**

The Norwegian International Climate and Forest Initiative (NICFI) was established in 2007 for the purpose of reducing global greenhouse gas emissions. NICFI was announced by Prime Minister Stoltenberg at the 13th Annual Conference of Parties (COP) of the UNFCCC in Bali as an initiative to support the REDD (Reducing Emissions from Deforestation and Forest Degradation) proposal that had been made in 2005 by the Coalition for Rainforest Nations at the 11th COP in Montreal. At the Bali meeting, issues closely related to REDD, like the sustainable management of forests and biodiversity protection, as well as conservation and enhancement of forest carbon stocks were added to the original list of concerns, resulting in the designation REDD+.

The Norwegian announcement was also intended as support to the efforts to get the REDD+ agenda incorporated into the on-going discussions on the Kyoto Protocol. This was important because the proponents of REDD+ believed that it offered a comparatively cheap, comparatively

uncontroversial and actionable strategy for reducing climate gas emissions quite quickly. At the heart of the REDD proposal was the idea of PES, or Payment for Environmental Services, which implied that forest dwellers should be rewarded for preserving the forests as carbon sinks for the common global good. The first proposals suggested that funding for PES should come from the carbon market, or the emissions trading scheme under the UNFCCC that was discussed at the time. The Bali meeting issued a 'Bali Action Plan' to carry forward actions on climate change mitigation and adaptation. This document in broad terms discusses the need to provide financial transfers and incentives to the rainforest nations to support the implementation of the forest conservation measured indicated by REDD+.

Norwegian support for REDD+ may be seen as an offshoot of the political debate in Norway on climate issues and ways to mitigate climate change. The domestic climate debate culminated with a broad-based climate agreement in the Norwegian Parliament, supported by almost all political parties, in January 2008.

Even though Norwegian support for REDD+ was announced in December 2007, the two decisions are closely connected. A point of contention in the political debate prior to the climate settlement was the extent to which Norway needed to take action to reduce domestic GHG emissions or if a better result (for the same cost) could be achieved by using the carbon market to buy carbon quotas to offset Norwegian emissions. The settlement reached the compromise that Norway needed to reduce domestic emissions as well as to contribute actively in various ways to the global common good of reducing GHG emissions.

Hermansen and Kasa (2014) have shown how the climate debates in the Norwegian Parliament opened an opportunity for two Norwegian environmental NGOs (Naturvernforbundet and Regnskogsfondet) to gain access to the political parties and to promote the REDD idea. The two NGOs were well aware of the proposal for PES made in 2005 by the Coalition for Rainforest Nations, that controlling deforestation and the degradation of rainforest was a cost-effective way of reducing GHG emissions.

The REDD emissions amounted to between 15 and 20% of global emissions and the REDD strategy could have a significant impact on global warming. Supporting REDD would also conserve biodiversity, increase local capacity to adapt to climate change and reduce poverty among rainforest dwellers. It was, furthermore, argued that Norway had a moral obligation to contribute, since Norway was a major oil exporter and thus a major contributor in various direct and indirect ways, to global climate gas emissions.

The influential Stern review from 2006 on the economics of climate change gave further support to the idea that climate change mitigation would become more expensive the longer the actions were postponed and that REDD was a feasible and practicable strategy for reducing climate gas emissions. The Norwegian government was familiar with the Stern review and Prime Minister Stoltenberg supported the central idea of carbon pricing and the use of some kind of market mechanism to promote forest conservation.

The initiative, when it was made, supported the REDD proposal that rainforest countries should receive payment for environmental services from the international community as a means to support forest conservation and reduce global gas emissions. The Norwegian contribution of US\$ 1 billion to be made available between 2008 and 2015 for this purpose, was primarily intended as a pump-priming contribution, because it was assumed that in the longer term PES would be paid for by the UNFCCC emissions trading scheme. One factor that has been mentioned as being very significant to the launching of the strategy is the source of NICFI funds, which came from Norway's comparatively sizeable development assistance budget. The economic repercussions within Norway would therefore not be noticed, since these funds already had been committed to a purpose with widespread political support. The argument from some political quarters that the Norwegian contribution to reduce GHG emissions should not be charged to funds intended to combat poverty, was flatly rejected at the time.

The results-based approach in the case of NICFI thus does not seem to have emerged from a development-effectiveness agenda, but rather from the idea of creating a carbon market that put a price on reduced deforestation, thus creating incentives to reduce deforestation.

### **CLEAN ENERGY**

The International Energy and Climate Initiative, known as Energy+, was launched jointly by the Norwegian government and the UN Secretary General in October 2011. The central idea in Energy+ is to establish an international partnership to contribute to development and poverty alleviation through improved access to energy, to improve the efficiency of energy technology, and to increase the proportion of renewable energy within the sector. Increased access to and use of these forms of energy would by implication reduce GHG emissions.

Hence, Energy+ was to contribute to low-carbon development solutions and so-called 'green growth' in developing countries, and helping prepare partner countries to qualify for financing from the Green Climate Fund.

The background to the Energy+ initiative must be sought both in Norway's well-established development assistance program within clean energy and in the central position that Norway had assumed in the global climate negotiations after the 2007 announcement of NICFI.

Prime Minister Stoltenberg additionally played a central role in the work to identify appropriate international mechanisms for funding climate mitigation and adaptation actions. Against this background the government made an active decision to establish a new initiative to address energy issues and climate challenges arising from poor access to modern energy technology. The overarching aim of the initiative is to promote development and poverty alleviation strategies that are compatible with the need to reduce GHG emissions.

Energy+ addresses a set of formidable challenges, which are compounded by the very high costs associated with developing energy services. It has been estimated that universal access to modern energy services by 2030 would require an annual investment of US\$ 48 billion, which is far more than could

be made available through ODA, and about 5 times more than the investments made in the energy sector in 2009. So in addition to increasing access to energy and decreasing GHG emissions, Energy+ would need to use available funds strategically to leverage greater commercial investments in the energy sector.

The Energy+ program had been under preparation/discussion since early 2010 and it was clearly inspired by the REDD+ program that NICFI had instigated. It is different from NICFI by being set up as an international partnership rather than a bilateral Norwegian venture. Energy+ was set up to supplement Norway's bilateral program for clean energy but was specifically designed to address energy issues at the sectoral level, on the basis of national energy- and climate strategies, rather than in a project-by-project mode. Like REDD+, the Energy+ program will support countries in a three-phase approach, through a readiness phase for strategic planning, capacity building and policy reforms, to be followed by the implementation of operational plans and programs, including the construction of robust systems

for measurement, reporting and verification – MRV. Finally, outcomes at the sectoral level, in terms of improved access to and use of renewable energy, will be paid for through a payment-by-results scheme. In one case (Ethiopia is so far the only country where the Energy+ agreement includes this clause), the reductions in GHG emissions resulting from the adoption of energy-efficient solutions will also be counted as a result to be paid for.

### 3. Evidence base for decision making

#### HEALTH

The decision to use results-based payments in the health sector was from the beginning perceived as an innovative approach. The scientific evidence base was weak, as by definition is the case with new ideas that have not been tested.

Norway's interest in promoting demand side incentives was however inspired both by practical experience and the general evidence on the importance on demand side constraints for low service utilization. For instance, the implementation of conditional cash transfers to promote births in health facilities in India was an important source of inspiration. At the time, operational data suggested that the scheme had a strong impact on facility based deliveries. These observations were later confirmed by more rigorous evaluations (CORT, 2007, Lim et al., 2010, Randive et al, 2013). The evidence of the effectiveness of conditional cash transfers in various Latin American countries was also an important reference point (Lagarde et al, 2007).

Practical experiences and emerging evidence on the use of performance-based funding by the World Bank also fuelled the process. Of particular importance were the results from a pilot in Rwanda, suggesting that incentives to service providers could increase the share of births at health facilities (World Bank 2007).

The acknowledgement of the innovative nature of results-based payments in health led to the establishment of the most comprehensive impact evaluation programme ever in Norwegian development cooperation. The purpose was to build the evidence along with the implementation of results-based financing (RBF). It became a basic premise for all pilots funded through the HRITF to also include an independent process and impact evaluation. Such evaluations have also been implemented in the bilateral programmes. A few evaluations have been completed, but most are still in process and will substantially enhance the evidence base on results-based financing over the coming years.

The decentralized nature of results-based financing mechanisms allows for the use

of control groups to assess the causal impact of the programmes. Unfortunately, from a scientific point of view, the implementation of the pilots has not always allowed for random assignment of participants to intervention and control arms, leading to less precise identification of causal impacts than what could otherwise be achieved. The consequence is that it will take longer to build a reliable evidence base.

Norad also commissioned several reviews of the international evidence on results-based financing. The first study, by Oxman and Fretheim (2008), summarized the findings from ten systematic reviews on issues of direct or indirect relevance for RBF, but it was not in itself a systematic review. Only one review addressed demand-side incentives in a low and middle income context, and none addressed supply-side incentives. A more ad-hoc search lead to the inclusion of four studies of specific results-based programmes. Apart from the observation that there is evidence on the impact of demand-side incentives, the main conclusion of the study is that there are few

rigorous studies of RBF and overall the evidence of its effects is weak.

The second study, by Witter et al (2012), is a systematic review of supply-side results-based financing. Only nine studies met the criteria for inclusion in the review, and the main conclusion was again that the current evidence based is too weak to draw general conclusions. Results-based financing is not a uniform intervention but encompass a range of different incentive mechanisms, different indicators and levels of payments, and are likely to have different impacts in different contexts. A substantial body of research is therefore needed to draw general conclusions.

Basinga et al (2011) is so-far the only study of seemingly high quality of a “typical” RBF programme. (Although the study is presented as a randomized controlled trial, the randomization procedure is not entirely convincing, leading to some uncertainty about potential bias.) A valuable property of the study is that it controls for the effect of additional resources coming with the RBF scheme, implying that the measured

impacts are only due to the incentives and the accompanying organizational reforms. The study finds that RBF caused an increase in some incentivized indicators (delivery at health facilities, preventive visits for children at health facilities, content of prenatal care) and no change in others (coverage of prenatal care and vaccination). The study provides no evidence on long-term effects, general quality of the services, utilization of non-incentivized services and other possible unintended effects.

Other international agencies have also commissioned studies about the evidence of RBF that has been utilized by Norad (e.g., Gorter et al 2013; USAID 2012; Cashin et al 2014).

#### **CLIMATE AND FORESTRY**

The PBR solutions in the environment, climate and energy nexus that have grown out of the REDD+ (and later Energy+) programs seem to have had very little solid evidence on which to base a preference for PBR when the programs were announced. As was pointed out above, the idea of Payment for Environmental Services – PES, was central to the REDD

proposal that was made by the Coalition for Rainforest Nations at the climate COP in 2005. PES was, at the time, a fairly novel concept and was seen as an alternative to the more common integrated conservation and development projects (ICDP) that were the favoured mode of natural resources conservation after the Brundtland report of 1987 and the Rio 1992 conference on environment and development. The ICDP approach, which assumed that alleviating poverty was the only way of conserving and protecting the environment had come under increasing criticism as perhaps a necessary, but certainly not sufficient condition for resource conservation. The attraction of PES was that it would only pay for the conservation result, which was the environmental service in question, if and when this result was obvious.

In 2005, there were in fact very few PES projects in developing countries, and the concept had been poorly tested (Wunder, 2005). None the less, the PES concept was no doubt known to the environmental NGOs that played such an important role in the 2008 ‘climate settlement’ in the Norwegian parliament and

in shaping the NICFI announcement to support REDD+. The core idea in PES is that some external beneficiary would make direct, contractual and conditional payments to local land users and forest dwellers, in return for adopting practices that would secure ecosystem conservation. PES was a promising innovation, which in 2007 was accepted more or less at face value as a viable alternative to other conservation strategies. There were a limited number of pilot-scale experiences available at the time, from various countries in Latin America in particular. One common problem that had been identified was the problem of finding a buyer for a global common good, like climate services (Montagnini & Finney, 2011). It is important to keep in mind that NICFI's support for the REDD+ strategy must primarily be seen as a climate-related, rather than a development-related measure, directed at reducing emissions. NICFI has later become more closely identified as a development initiative as well, primarily because the funding for NICFI came from the Norwegian development budget; development aspects have been recognized a 'co-benefit of the REDD+ strategy

and have become more visible in NICFI activities as the program was implemented.

### **CLEAN ENERGY**

Energy+ is also a program that since the beginning has emphasised the need to identify and extend novel and innovative solutions to meet its multiple objectives. It was designed to overcome some of the shortcomings of the existing bilateral energy program by addressing energy and climate issues at the sector rather than the project level. On the basis of its inspiration from the REDD+ program, Energy+ was meant to test out various results-based approaches. One of the perceived advantages of PBR, which in the case of Energy+ concerns payment to governments on the basis of sector-wide results, is that this approach would facilitate leveraging commercial capital for energy investments. The results that Energy+ is intended to reward could be either increased production of renewable energy, improved distribution and access, as well as improved efficiency through schemes for the distribution of improved technology.

When Energy+ was being set up, there were very few experiences of PBR from the energy sector. The two main sources of experience were the Global Partnership for Output Based Aid (GPOBA) established by DFID and the World Bank in 2003 and the Energizing Development Program launched by the Dutch and German governments in 2004. Norway has been a partner to EnDev since 2005. None the less, reporting on a literature review on results-based approaches, ESMAP writes that "there is relatively little literature on the use of RBAs in the energy sector, reflecting their limited application in this sector to date" (ESMAP, 2013:45) and even in a more recent report the lack of extensive evidence from the energy sector is brought out: "When and whether RBA may be preferred to conventional aid modalities will remain an open question until more evidence is available" (ESMAP 2015:2). So, in spite of some experience with results-based approaches, Energy+ was clearly designed to operate in uncharted waters; in addition to the 3-phase approach adopted from REDD+, it was set up only in four countries to begin work on the readiness phase.

Energy+ encouraged the early formation of a technical working group, recruited from within the 50 or so members of the Energy+ international partnership that is specifically charged with examining and developing the conceptual and practical aspects of designing PBR schemes for Phase 3. This gradual approach will specifically allow the piloting of different designs in different countries, assisting countries to design their own strategies for energy production and distribution, and develop adequate models for calculating emission reductions and establishing robust MRV systems. Most of the attention will be on the production and distribution of modern energy services, including improving the efficiency of available technology, and it is primarily sector performance in these terms that will be rewarded. The readiness phase will also include preparatory work (in one country) for the inclusion of emission reductions in the PBR scheme.

Energy+ will work to develop and test practical approaches to sector-wide energy development in a limited number of countries up to 2017, when the experiences will be thoroughly assessed and evaluated.

To sum up: The evidence base in terms of actual experiences with PBR schemes both within climate/forestry and energy sectors seems to have been weak when these initiatives were discussed. Payment for Environmental Services (PES) had been proposed in conjunction with REDD, but this approach had not been very much tried out in developing countries. None the less, results-based payments seem to have exerted a considerable attraction on decisions-makers, and PES seems to have been the direct inspiration of the PBR schemes set up within REDD+. Within Energy+ there seems to be even less direct evidence of how PBR schemes could work, but this seems to have been realised at an early stage so that Energy+ is set up with a considerable piloting component built into the 3-phase approach adopted.

## **CONSIDERATIONS CONCERNING ALTERNATIVE FUNDING MODALITIES**

In the projects that we have reviewed, there is little indication that the advantages and disadvantages of PBR modalities have been systematically weighed against traditional financing modes before the decision to go for PBR was taken. GAVI is perhaps an exception. In that case, other funding modalities were on the table in the negotiations among the donors, but we do not have any documentation of how arguments were weighed against each other and what made PBR a mechanism that everyone could accept.

The absence of an explicit discussion of traditional vs PBR funding can perhaps most easily be understood in the climate and forest initiative. In this case, the results-based funding mechanism did not grow out of an aid effectiveness logic, but was rather conceived as a precursor to a market based system for carbon trading.

Results-based financing in the health sector was more clearly explored as an alternative to previous, traditional funding modalities. However, the lack of empirical evidence of the benefits and costs of results-based financing made it quite difficult to make a decision based on a careful balancing of pros of cons. The lack of such a discussion is therefore not surprising.

During the implementation of PBR mechanisms, however, it has often been realized that they need to be combined with traditional funding modalities. Both GAVI, REDD+, and Energy+ are hybrid models. In these initiatives, there has been a clear understanding of the need to take context and preconditions into account and to prepare the ground carefully through policy work and capacity- and institution-building before introducing PBR.

Some of the pros and cons of results-based approaches are clearly exposed in the case of energy production, as recently discussed in a report from ESMAP (2015). Among the projects reviewed in connection with this study, the Uganda GET-FIT project illustrates some

of the dilemmas very well. One issue is the need for financial resources to invest in power production. PBR assumes that this financing can be obtained from elsewhere. Another issue is the duration of the project, as results will be produced over a period of several decades. It is not easy for a donor to commit to such a long time horizon. (If the REDD+ project were to reward achieved carbon sequestration through afforestation, there would be a similar timing issue there.) A third issue is the allocation of risk; PBR transfers more risk to the energy supplier, and this may require some kind of compensation, depending on the credibility of the payer. Finally, funders must be flexible enough to disburse payments quickly once results are verified, and must be flexible enough to absorb delays and variation in performance between the years.

## 4. Theoretical arguments

In the presence of weak empirical evidence for the impact of results-based approaches, one would perhaps expect a correspondingly strong emphasis on theoretical arguments and a thorough elaboration of the theories of change for the new PBR initiatives. This does not seem to have been the case, at least not in the early stages of the Norwegian initiatives. For example, an elaborate theory of change for results-based financing in the health sector appears to have been developed quite some time after the establishment of the HRITF, and in the forest initiative, the theory of change is yet to be properly documented.

This does not imply of course that decisions were made in a theoretical vacuum. The core idea of any results-based approach is that incentives affect behaviour. This idea has a strong intuitive appeal, maybe to the extent that it was not explicitly stated. The same holds for the other core property of results-based approaches (in particular results-based aid), namely the transfer of risk from donor to recipient as donors pay only after results have been achieved. The strong embracement

of results-based approaches among politicians is a testimony to the power of these ideas.

However, there is a long way from the intuitive idea of the effect of incentives on behaviour to the design and implementation of incentive schemes that actually contribute to desired results. There are three overarching questions that need to be addressed:

- How will incentives affect behaviour?
- In case incentives are linked to intermediary results, how will the outcomes of interest be achieved?
- What are the possible unintended effects of the incentives?

The breadth and depth of theoretical reflections on these issues have evolved over time; while some issues were discussed early before the implementation of results-based approaches, other issues have become more apparent as concrete projects have materialized, as well as through exploration of relevant academic literature.

This final section outlines some of the main issues in the current theoretical discussion about results-based approaches, while providing examples of how various arguments have been articulated at various stages of Norwegian decision making.

### **HOW WILL INCENTIVES AFFECT BEHAVIOUR**

The most obvious way that results-based approaches can affect behaviour is perhaps through pecuniary incentives. However, there is an increasing awareness that this is only one of several possible mechanisms. What mechanisms are at work depends both on the design of the scheme and on whether it targets governments, organizations or individuals.

Perakis and Savedoff (2015) summarize the main arguments why results-based aid can influence government behaviour as follows:

- *Pecuniary interest.* Governments take action to receive the pecuniary rewards.
- *Attention.* Governments take action because the PBR agreement draws attention to particular outcomes.

- *Accountability.* Government responds to enhanced civil society monitoring of their performance.
- *Discretion.* Increased government discretion on how to achieve results leads to better decisions though enhanced utilization of local knowledge. Governments are more committed to implementation strategies they have designed themselves.

They argue that both in the case of GAVI and in the forest initiative in the Norway-Brazil agreement (the Amazon Fund), pecuniary mechanisms have played a smaller role than other mechanisms.

Similar arguments as listed above are also used in discussions about why supply-side results-based financing may work in the health sector:

- In addition to the motivating effect of pecuniary incentives, the specification of results-indicators increases attention to results and has a motivating effect in itself;
- greater autonomy for frontline service providers in how to achieve results is motivating and leads to more informed decision making; and
- more emphasis on monitoring of results increases upward accountability and perhaps also accountability towards communities.

In energy production, on the other hand, where the agents typically are private firms, the main emphasis will naturally be on the pecuniary incentives.

A clear idea of the mechanisms through which results-based approaches affect behaviour is important for the design of the scheme: If the pecuniary incentives are important, it is crucial to get the size of the incentives right; they must be large enough to affect behaviour, they must target the key decision makers, and the indicators must be sufficiently within control of the agent. If attention is a main mechanism, it will be crucial to raise awareness about the indicators, while the level of the pecuniary incentives may play a more symbolic role. If discretion and autonomy is impor-

tant, a hands-off approach is required when it comes to the utilization of funds. And if accountability is thought to be important, credible data monitoring and verification is crucial.

In the case of demand side incentives used in the health sector, the following arguments have been discussed:

- The motivational effect, whereby incentives make it more attractive to use modern health services rather than other alternatives;
- the resource effect, whereby the extra resources makes it possible to overcome economic barriers in seeking care (e.g., transport costs); and
- the empowerment effect, whereby the recipients increase their power to negotiate against existing cultural practices and preferences of other household members.

The relative importance of these mechanisms may also here be important for the design; for instance, if the resource effect is the most important, a voucher scheme may be appropriate, while vouchers may be less powerful than cash in negotiating against cultural practices

### **THE CHALLENGE OF INCENTIVIZING INTERMEDIARY RESULTS**

While the idea of rewarding outcomes that matter for policy looks appealing on paper, it is not always possible or meaningful to link payments to such outcomes. For instance, linking health worker payment to population health outcomes would make health workers responsible for an outcome far beyond their control, which would seem both ineffective and unfair.

Results-based payments in health therefore typically reward intermediary results, such as service utilization and content/quality of care.

The potential risks of rewarding results at the intermediary level, including rewarding those that are easier to measure, have been prominent in the discussions about results-based financing in health (e.g. Norad, 2010; Olsen 2012).

Increased service utilization is thought to improve health outcomes through two mechanisms (e.g., HRITF 2013). First, higher service utilization does in itself lead to better health outcomes, as long as the quality of care remains above a critical level. Second, in order to attract more patients, health workers will be induced to provide services of higher quality, which will have a direct positive impact on health outcomes. Critics have argued that the first premise may be false as quality of care may be below the critical level. Moreover, asymmetric information between provider and client implies that what is needed to attract more clients (perceived quality) is not necessarily what produces better health outcomes (medical quality). Most RBF mechanisms in health therefore also provide direct incentives to improve medical quality, although monitoring and verification here is a great challenge.

The principal-agent literature, which has provided important inputs to the theoretical discussions on RBF, underscored the risk that linking incentives to only a subset of the intermediary results could draw attention away from other important

activities, perhaps with no or even a negative effect on the outcomes of interest. This problem arises when the agent is supposed to perform several tasks to achieve the desired outcome (“multi-tasking”). This is typical the case in health service delivery, and Norway’s preference for linking incentives to reproductive, maternal and child health services has made this a valid concern. It has been argued that this challenge might be addressed by ensuring that incentives “rotate” among services over time, but such dynamic approaches do not seem to have been implemented so far.

Political economy theories have also been put forward for why incentives at the output level might be effective. For instance, in connection with demand side incentives for women to deliver at health facilities, it has been argued that if utilization rates become sufficiently high, they will create stronger political pressure on the authorities to improve service quality, leading to better health outcomes.

## UNINTENDED CONSEQUENCES

The principal-agent literature also points at possible unintended consequences of incentives. Most of these arguments were on the table at the time when results-based financing in health was initiated (e.g., Mæstad 2007, Oxfam and Fretheim 2008, Olsen 2012), and some are now also being discussed in connection with energy projects (ESMAP 2015).

**Higher costs.** One possible effect is that results-based payments may be more expensive than traditional approaches because they transfer risk from principal to agent, or from donor to recipient, and the recipient may require compensation for the increased risk. For example, health workers who get their monthly salaries in the form of bonuses per patient face a higher risk than those who receive a fixed monthly salary and will normally not accept this without compensation. This question has however never been seriously debated in the health sector since in practice all RBF schemes have come with additional resources and thus placed incentives on top of existing fixed salaries.

In the energy production sector, if incentives are provided for the actual production and delivery of energy rather than for the construction of production plants, the risks for private energy producers will increase, and compensation will be needed. The risk premium may not be particularly large as long as subsidies are provided through contracts with international donors, but this picture may change if results-based approaches are financed by national governments.

In addition to the costs associated with risk, results-based approaches in some sectors require expensive data monitoring and verification procedures.

**Effects on intrinsic work motivation.** It was argued early on, based on empirical evidence from the principal-agent literature, that monetary incentives to health professionals might undermine intrinsic work motivation and potentially have a negative effect on performance, especially in the long run. More recently, a theoretical argument has been made that the opposite can also be the case; in health

systems where there is little recognition for good performance, incentives can be a means to express recognition for good work and induce processes leading to improved intrinsic motivation.

### **Unacceptable ways of achieving results.**

A key feature of results-based payments is a high degree of autonomy for the recipients in how to achieve results. The principal is however usually not indifferent as to how results are achieved; strategies that impose harm or violate human rights can be examples of unacceptable strategies. This issue has been discussed in the forest initiative, where the response has been to define a set of safe-guards that will ensure that recipients do not choose unacceptable strategies to achieve reduced deforestation. The issue does not seem to have been discussed much in the health sector, but it has received increased attention after reports about coercive behaviour to induce more patients to visit health facilities in Tanzania and Zimbabwe (Mutasa et al 2013; Chimhutu et al 2014).

**Unfairness.** An incentive system that is perceived as unfair will lose its legitimacy and may soon become ineffective. This issue has received considerable attention in the health sector, where outputs typically are the joint product of a number of health workers. The solution has been to rely on team incentives (each health facility is rewarded for the total output of the facility) and to give considerable discretion to each facility on how to allocate the incentives among themselves. Another fairness argument within the health sector is that incentives will make providers pick the low hanging fruit (“cherry-picking”), which for instance may result in less priority to reach hard-to-reach areas and thus to larger inequities.

Finally, there is a more ideological fairness argument, relating to the very nature of results-based payments. The core of the argument is that incentive based remuneration systems produce unfairness by default since they build on a meritocratic rather than an egalitarian fairness ideal. In Norway, the most forceful criticism against results-based payment seems to have come from ideological arguments of this kind, rather than from arguments about the effectiveness or efficiency of the schemes.

## 5. Conclusions

PBR is a fairly new approach in development cooperation and the amount of ODA that is delivered through this modality is still modest. In Norwegian development cooperation, PBR is mainly linked to high-profile initiatives where decisions have been taken at a high political level. In practice, there are few examples of pure PBR models, as PBR is mostly implemented in hybrid models, together with traditional funding.

Very limited evidence has been available to assess the benefits of PBR over traditional funding modalities. The innovative nature of the initiatives has been explicitly acknowledged, and this has in some cases (the health sector) led to considerable investments to enhance the evidence base. The evidence is however still fairly limited, and further investments are needed both in the health sector and in other sectors to establish to what extent and under what circumstances results-based approaches lead to results.

Clear theories of change were not formulated at the initial stages of the PBR initiatives. This may seem peculiar given the paucity of empirical evidence and is probably partly explained by the fact that decisions were made primarily at a high political level, detached from normal bureaucratic processes. More explicit theories have evolved over time in relation to some initiatives (health), but less so in others (climate and forestry). Several of the initiatives might have gained from a clearer articulation of the theories of change at an earlier stage, as the theory of change may have important implications for the design of the PBR mechanisms.

PBR schemes seem to be inherently attractive to politicians, aid practitioners and the general public as they may seem to reduce the development process to the simple principle of paying for what you get. This is of course a gross oversimplification of the comparative strengths and weaknesses of traditional development financing versus results-based payments. There are now a number of attempts to establish more clearly, on the basis of theoretical analyses

as well as empirical experiences, the conditions and situations under which one may expect results-based payment to work better than traditional financing modalities.

# Appendix

## **METHODS**

The two reports *Experiences with Results-Based Payments in Norwegian Development Aid* and *Basis for Decisions to use Results-Based Payments in Norwegian Development Aid* are the results of a desk review based on written documentation, supplemented with interviews with selected key people involved in the initiation and implementation of results-based payments in Norwegian development cooperation.

Projects and programmes using a results-based funding modality were identified by Norad on the basis of the Norad statistics portal and consultations with relevant departments in the Ministry of Foreign Affairs and Norad.

The research team conducted semi-structured interviews with key programme officers and key people behind the identified projects and programmes to better understand the basis for decisions to use results-based payments and to obtain a proper account of the experiences to date. The interviewees were asked to make available relevant documents (project documents, discussion notes, reports, evidence reviews, evaluations etc.).

The team also searched the web pages of key multilateral agencies involved in the implementation of Norwegian results-based initiatives and contacted their secretariats to obtain documentation on the programme logic as well as the experiences obtained.

One should note that the projects that are the subject matter of this study are mainly high-profile projects set up by high-level political decisions, rather than the outcome of regular bureaucratic processes. This has limited the extent of documentation available, particularly on the discussions and deliberations that presumably took place before the initiatives were launched.

Note that since this study is confined mainly to written documentation, we have been unable to capture much of the detailed practical experience from implementing results-based payments. Neither does the study include experiences made by other funding agencies.

## PERSONS INTERVIEWED

Name	
<b>Elisabeth B Clemens</b>	Policy Director, Department for Climate, Energy and Environment, Section for Renewable Energy, Norad
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<b>Andreas Tveteraas</b>	Policy Director, Department of Climate Change, Ministry of Climate and Environment
<b>Øyvind Dahl</b>	Senior Adviser, Department of Climate Change, Ministry of Climate and Environment
<b>Hans Olav Ibrenk</b>	Policy Director, Energy+ Secretariat, Ministry of Foreign Affairs
<b>Kari Bjørnsgaard</b>	Senior Adviser, Energy+ Secretariat, Ministry of Foreign Affairs
<b>Joakim Arntzen</b>	Consultant Engineer, Multiconsult

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## Abbreviations and acronyms

<b>COP</b>	Conference of Parties	<b>ISS</b>	Immunization Services Support
<b>DFID</b>	Department for International Development	<b>MRV</b>	Measurement, Reporting and Verification
<b>EnDev</b>	Energizing Development	<b>NGO</b>	Non-Government Organisation
<b>ESMAP</b>	Energy Sector Management Assistance Program	<b>NICFI</b>	Norway's International Climate and Forest Initiative
<b>GAVI</b>	Global Alliance for Vaccines and Immunization	<b>ODA</b>	Official Development Assistance
<b>GET-FIT</b>	Global Energy Transfer - Feed-in Tariffs	<b>OECD</b>	Organisation for Economic Co-operation and Development
<b>GPOBA</b>	Global Partnership for Output Based Aid	<b>RBF</b>	Results-Based Financing
<b>GHG</b>	Green-House Gases	<b>PES</b>	Payment for Environmental Services
<b>HRITF</b>	Health Results Innovation Trust Fund	<b>PBR</b>	Payment by Results
<b>ICDP</b>	Integrated Conservation and Development Project	<b>UNFCCC</b>	UN Framework Convention on Climate Change