



CENTRAL INSTITUTE FOR  
ECONOMIC MANAGEMENT



JAPAN INTERNATIONAL  
COOPERATION AGENCY

# Study on Donor Practices in Vietnam ~ Grant Aid and Transaction Costs~

Listen to the Voice of the Recipient



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## Acknowledgement

Recently, donors at both the international and country levels have begun discussing harmonization and the simplification of donor practices. However, most of the concepts and the new ODA modality, including approaches such as sector-wide approaches with pooling arrangements and budget support, have been based on the experiences of African nations. We therefore consider it necessary to adapt these concepts to the Asian context. Accordingly, we propose to individually study ODA transaction costs within each country. Based on these study results we will present suggestions to improve the current donor provision situation.

This current paper outlines the results of the JICA Study of Donor Practices in Vietnam and focuses on grant aid. In the case of Vietnam, a number of donors have already conducted similar studies related to ODA transaction costs. This JICA/ CIEM study takes on a new format and is conducted from a multi-dimensional viewpoint. As a result of preliminary studies, JICA hopes to identify tendencies concerning the incidence of transaction costs at the pre-implementation and implementation stages of ODA projects. Through this study, we have realized the importance of identifying the present situation concerning transaction costs in ODA in Vietnam. However, at the same time, we have come to recognize how difficult it is to identify such problems.

At first, we faced a number of difficulties in defining transaction costs. We defined these costs as follows, in a very simple manner from a practical and realistic viewpoint.

*“The difficulties and burdens recipient countries encounter in dealing with donors. However, we recognise two types of transaction costs: necessary transaction costs and unnecessary transaction costs. In the discussion here, we would like to focus on unnecessary ones which decrease aid effectiveness and efficiency”*

As this report goes on to say in the Chapter 1, if we were to try to elaborate this definition more technically and in greater detail, many people, including interviewees and government officials would be unable to grasp the resulting definition. We therefore chose to define it simply. From this viewpoint, the approach adopted by the World Bank in its “Voice of the Poor” study in 1999 is a good example. It took an approach of collecting the voices of the poor first, asking: why are they poor? How do they assess the social services? Then responses were stylized. Finally, they gave commentaries to each case, and drew some fruitful implications for future work. They made great efforts to listen to the voices of the poor instead of trying to adhere to or understand the problems from purely a quantitative direction. This report follows such an approach.

The conclusion to this report is very simple. We wished to suggest to donors and recipient agencies a set of simple and basic actions that could be implemented in a uncomplicated and steady manner. With such an approach, both the Vietnamese and the donor side might be able to avoid implementing new, special or complicated procedures in attempting to reduce their transaction costs. Unfortunately, we have not yet carried

out such simple tasks ourselves. We have found the more ordinary and basic problems are the more difficult they often are to put into practice.

Finally, we would like to thank and highly appreciate the efforts of the Central Institute of the Economic Management, especially Dr. Vo Tri Thanh as team leader and Ms. Dinh Hien Minh as project coordinator, and, of course national consultants from sectoral ministries, namely, Dr. Nguyen Loc (Ministry of Education and Training), Dr. Dang Kin Son (Ministry of Agriculture and Rural Development), Ms. Tran Thi Giang Huong (Ministry of Health), Mr. Nguyen Dang Vung (Ministry of Health), and Ms. Doan Thi Phin (Ministry of Transport). They participated in this study as national consultants. Without their involvement, we might have not been able to access the real voices of Vietnamese ODA recipients.

After the High-Level Forum on aid effectiveness held in Italy in February 2003, these issues are increasingly popular at both a country level as well as at an international level. In relation to this, we understand from the mid-term Consultative Group Meeting in Sapa that the Ministry of Planning and Investment (MPI) is to launch a new initiative, entitled “Comprehensive Capacity Building for Aid Management”. We hope this report can contribute to further discussions on upgrading aid effectiveness and efficiency in Vietnam, and to provide a set of good practice tools for the identification of the current situation of transaction costs for partner countries around the world.

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## Chapter 1 Background and Objectives of the Study

During the late 1990's, the international donor community began discussing aid effectiveness issues in a different manner. This was initiated by the *Helleiner* report in 1995<sup>1</sup> on Tanzanian aid effectiveness. This report described several factors in aid dispersal such as the lack of coordination amongst donors, the large number of un-coordinated missions and stand-alone projects, and the large amount of administration procedures in the donor community which led to multiple procedures by a variety of donors which created transaction costs and deprived recipient agencies of time to devote themselves to more productive work.

Thus it recommended (1) the promotion of improved coordination amongst donors, and (2) the introduction of harmonization (including sector-wide approaches, pooling arrangements, budget support, and so on). In January 2001, the International donor community set up a task force on donor practices at the OECD-DAC to hold a series of discussions, and commissioned Birmingham University of the United Kingdom to conduct a Needs Assessment Survey in 2002. It was found that huge ODA transaction costs were created by donors due to poor coordination at the pre-implementation and the implementation stages. It also highlighted that the complicated, multiple level procedures of a large number of donors hampered aid effectiveness and efficiency. In past discussions, donors had only emphasized transaction costs in terms of the overlapping of projects and the inefficient use of scarce ODA resources. After the OECD-DAC task force was set up, the donor community started to collectively discuss the issue of transaction costs in detail at each stage of the project cycle. The donor community began attempting to upgrade aid effectiveness and efficiency by introducing a new ODA modality based on the program approach and harmonizing the procedures of each donor, for example, common formats of financial management, monitoring & reporting.

### 1. Vietnam Context

In Vietnam, from late 1990s, the Government has been making great efforts to enhance ODA effectiveness, particularly through a series of the Consultative Group (CG) meetings, etc. To this end, they issued Decree No. 17 in 2001. And many donors are now exploring the possibilities of ODA harmonization for upgrading ODA effectiveness.

Three studies on transaction costs have been done in the past: UNDP/DFID (2000), the Like-minded Donor Group developed through Grant Thornton (2001), and the OECD-DAC (2002) developed through Birmingham University. These were very meaningful studies that found that transaction costs do exist and should be reduced. In addition, these studies created a momentum for the donor community in Vietnam to

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<sup>1</sup> Helleiner, Gerald, K. et al. (1995) Report of the Group Independent Advisor on Development Cooperation Issues Between Tanzania and its Aid Donor, Royal Danish Ministry of Foreign Affairs

address the question of “how we should discuss these issues?”

Each study identified key constraints; the UNDP/DFID (2000) study addressed basic questions such as, where are transaction costs incurred? Why are transaction costs incurred? Who creates transaction costs? And how can transaction costs be reduced? On the other hand, the Like-minded Donor Group (2001) conducted a comparison of six donors’ practices and presented options for harmonization. This report provides basis to the on-going efforts of the Like-minded Donor Group in Vietnam. The OECD-DAC (2002) is very controversial in that it says Vietnam’s technical assistance is problematic.

## **2. Definition of Transaction Costs**

One problem in conducting any study on ODA transaction costs is that most of the ODA recipient countries are not familiar with this term. According to the UNDP’s definition (UNDP – DFID 2000) and Bartholomew and Lister 2002, transaction costs are:

*“The costs arising from the preparation, negotiation, implementation, monitoring and enforcement of agreements for the delivery of ODA” and consist of administrative costs, indirect costs, and opportunity costs<sup>2</sup>.*

In this JICA study, transaction costs are defined as follows:

*“The difficulties and burdens recipient countries encounter in dealing with donors. However, we recognize two types of transaction costs: necessary transaction costs and unnecessary transaction costs. In the discussion here, we would like to focus on unnecessary ones which decrease aid effectiveness and efficiency”<sup>3</sup>*

Through this study, we came to recognize that any definition of transaction costs should be as simple as possible so as to aid understanding and incorporation into procedures, with a complicated or sophisticated definition only adding to the possibility of confusion. In that sense, to meet the practical and pragmatic requirements of

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<sup>2</sup> Transaction costs take three forms:

- *Administrative costs*: They arise from inputs of resources needed for the transaction. Main costs include administrative overheads, in particular staff time.
- *Indirect costs*: They result from the impact of the delivery mechanism on the achievement of development goals. Examples of indirect costs are costs emerging from undermining government ownership and policy consistency of ODA and public expenditure more generally; disbursement delays (and possible effects on future commitments), reduced effectiveness (as resources may go to lower priority areas), and over-financing of capital vis-à-vis recurrent expenditure.
- *Opportunity costs*: They measure the benefits forgone from alternative applications of the resources consumed in the transaction. For instance, senior officials need to trade off their time between aid management and policy development.

<sup>3</sup> Note that burdens are not completely synonymous with transaction costs. Some transaction costs are inevitable, and they have positive benefits that outweigh the costs. Burdens must be understood as costs that are in some senses unnecessary or excessive. Burdens are also relative to administrative and other capacities of the recipient: increasing those capacities, as well as reducing the burdens themselves, may be a legitimate response.



practitioners such as those who are actually engaged in ODA on both the Government of Vietnam and donor sides, too complicated or sophisticated a definition maybe interesting but will be less meaningful.

Transaction costs are incurred at various stages of the project cycle, for example, pre-implementation (strategy designing, project formulation and designing, and appraisal), and implementation (procurement of equipments and international & local consultants, financial management, auditing, monitoring and reporting). Donors have also tended to identify its causes through a project-type approach and through project management units (PMU), etc. These units and projects define solutions in the new ODA modality in areas such as the program approach (with or without pooling arrangement), and also through untied aid. Although groups such as the Like-minded Donor Group have been discussing the reduction of transaction costs and harmonization of donor practice among member countries since 2001, it is still a controversial topic among donors. However, in the future its work is likely to ensure that a pre-condition of ODA is to consider aid effectiveness. Thus, transaction costs should be carefully examined from a multi-dimensional viewpoint. To answer this, JICA decided to conduct a study of Donor Practices in Vietnam in terms of transaction costs.

### **3. Objectives of the Study**

This study focuses on the transaction costs of ODA grant aid projects, produced and imposed by different donors on recipient government agencies. It will be conducted with a neutral point of view towards ODA harmonization, enabling further constructive and productive discussions. The objectives of the study are as follows:

1. To identify the present situation of donor practices in Vietnam: including what problems Vietnamese recipient agencies are facing in order to receive ODA, especially grant aid from donors, and
2. To assess its causality and to draw some implications for improving donor practices in Vietnam, for example, through reducing unnecessary and excessive transaction costs in dealing with ODA projects in general.

### **4. Approach**

We have considered multi-dimensional viewpoint very important and necessary to thoroughly examine this topic carefully, how to do this is a key question. The concept of transaction costs is very complicated and difficult to analyze both quantitatively and qualitatively<sup>4</sup> as stated already. In this report, we adopted the following approach:

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<sup>4</sup> During our survey, we have realized how difficult and complicated the concept of transaction cost is. We have heard from many of our survey respondents that ODA transaction costs do not exist in Vietnam and transaction costs are viewed only as only as time, staff and administrative costs, as well as the difficulties arising during the whole project preparation and implementation process, which is related to the staff's mental health, and recipient's concerns on the long term effectiveness of the ODA projects.

1. *Listen to the voice of the recipient.* We focused our efforts on listening to the needs of donor recipients rather than measuring transaction costs in a complicated manner. We then stylized the recipient's replies into a story A technique in the "Voice of the poor study" conducted by the World Bank and others.
2. A wide range of case studies were collected through many interviews with government officials and project managers in the following sectors: Agriculture and Rural Development, Health, Education and Training, and the Transport sector. These four sectors are the top four ODA recipients in Vietnam. This study focuses on grant aid projects (not loans), which include not only Japan's grant aid, but also other donors<sup>5</sup>.
3. A National consultant team also held frank informal discussions and exchange opinions on the study

The remainder of the study is organized as follows. Chapter 2 gives an overview of ODA delivery in Vietnam during 1993-2001 and the efforts by Vietnam and donors to improve the effectiveness and efficiency in using ODA resources. Chapter 3 describes the methodology used for this study, which is mainly based on a sample survey consisting of 4 sectors, namely, transport, agricultural and rural development, education and health sectors. Chapter 4 analyzes the ODA transaction costs from different angles. The analysis is undertaken not only for the sample as a whole, but also provides an insightful look at ODA transaction costs by project stages/cycles. Chapter 5 examines ODA transaction costs through the collection of the views of ODA recipients on the Vietnamese side. With the key points withdrawn from our analysis, Chapter 6 tries to draw some implications for improving the donor practices in managing ODA projects in Vietnam.

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<sup>5</sup> Initially, we planned to focus on mainly Japan's grant aid, and compare this with a number of other donor examples to identify the characteristics and differences. Based on the results of our survey, we decided to publish this report with a focus on transaction costs created by other donors as well as Japan. Moreover, this study is more representative of donor practice in providing grant aid in Vietnam.

## Chapter 2 Overview of ODA Delivery in Vietnam

Since 1993, a large amount of overseas assistance from the international donor community has poured into Vietnam with the target of supporting her socio-economic development. These funds have played an important role in generating opportunities for the nation to attain its desired economic growth, alleviate poverty and improve Vietnamese people's living standards<sup>6</sup>.

During the period 1993-2001, donors committed USD 19.94 billion in ODA to Vietnam. Several ODA projects have concluded, accounting for USD 14.72 billion or 73.8% of the total ODA commitments by the end 2001. About 84% of this amount or some USD 12.35 billion (84%) was provided under credit schemes, while the rest of about USD 2.37 billion (16%) was grant aid. Among donors, Japan is the largest, and has accounted for 43.2% of the total concluded ODA, followed by the World Bank (20.9%) and ADB (13.7%)<sup>7</sup>.

### ODA Commitment and Disbursement, 1993-2001

Year	Commitment (USD Million)	Disbursement (USD Million)
1993	1,810	413
1994	1,940	725
1995	2,260	737
1996	2,430	900
1997	2,400	1,000
1998	*2,200	1,242
1999	**2,210	1,350
2000	2,400	1,650
2001	2,400	1,500
total	19,940	9,571

*Source:* Ministry of Planning and Investment web site.

*Note:* (\*) excluding USD 0.5 billion for budget support for economic reforms  
(\*\*) excluding USD 0.7 billion for budget support for economic reforms

In recent years, the performance of ODA projects has considerably improved, which is illustrated by annually increasing levels of disbursements when compared to commitments. The total amount of disbursed funds from 1993 to the end of 2001 reached some USD 9,571 million, which accounted for approximately 55.5% of total ODA commitment.

ODA resources have been allocated in direct support of the Government's priority

<sup>6</sup> According to a study by IDCJ (2003), Japanese ODA pushed up the Vietnamese GDP by 1.57%, capital stock by 4.65%, imports by 5.94% and exports by 3.84% in the year 2000.

<sup>7</sup> Data provided by the MPI. The shares of concluded ODA are for the period 1993-2000.

sectors; these include power (24%), transportation (27.5%), agriculture and rural development including fisheries, forestry, irrigation (12.7%), water supply and drainage (7.8%), social development, health, education and training, science, technology and environment (11.8%). A number of ODA-funded projects have been completed, put into operation and have thus made significant contributions to the economic growth and poverty alleviation. Broadly speaking, over the past years, ODA resources have been used in an efficient manner to support Vietnam's socio-economic development goals.

Meanwhile, we should draw attention to some characteristics of Vietnam's ODA delivery:

1. Low rates of aid dependency: for example, its percentage of ODA to the Gross National Income accounts for only 4.4% (14.1% in Uganda, 13.3% in Tanzania, 12.7% in Ghana, 28.1% in Mozambique, which are the countries commonly discussing aid harmonization issues in the OECD-DAC Task Force on Donor Practices.)
2. Higher ratio of loan aid rather than grant aid
3. Four large donors for loans with, in contrast, a great number of small and medium sized donors in grant aid. Through this study, we could not identify any significant difference of the size of transaction costs amongst donors, regardless of the size of donor assistance projects. Naturally, the size of transaction costs created by the larger size of projects should be bigger than that created by smaller sized projects. In spite of that expectation, transaction costs are similarly incurred in each case.

In considering aid effectiveness issues, we need to take into consideration the above features.

Nevertheless, there remain certain problems to be tackled in order to better use and manage ODA resources in Vietnam, especially with regard to the stages of project preparation, implementation, monitoring and evaluation.

To solve these problems, the Government and donors have closely collaborated to minimize inefficiency in using and managing ODA resources. For example, the Government has proposed a number of solutions such as:

1. the issuance of a joint circular by the Ministry of Planning and Investment and the Ministry of Finance providing guidelines on implementing Decree 17/2001/ND-CP (4 May 2001) with respect to financial issues of ODA funded project and programs.
2. To soon promulgate an ordinance on resettlement and land compensation to efficiently deal with current bottlenecks faced by many investment projects financed from ODA resources.
3. To sustain efforts to further harmonize the recipient and donor procedures for better aid reception, utilization and management.
4. To adopt a multi-approach method in capacity building for project management

where training can be complimented by other sorts of capacity strengthening exercises to achieve the ultimate goal of improving the quality of aid management.

5. To strengthen project monitoring and evaluation systems at all levels and introduce information technology to a broader extent to improve the work quality in this area.

In the abovementioned situation, the Ministry of Planning and Investment (MPI), at the regional workshop of OECD-DAC Task Force held in May 2002, classified efforts three-fold as follows: (1) the efforts between the government and an individual donor, (2) the efforts between the government and a group of donors, and (3) the efforts between the government and all donors.

In the first category, government and individual donors, France is now in discussions with MPI, while AusAid has provided support to strengthen the Government's capacity to monitor and evaluate aid projects. The alignment of this capacity with the monitoring and reporting requirements of individual donors and the increasing focus on results needs to be more fully explored. As for the second group, government and groups of donors, the 3-banks (now 5-banks such as ADB, AFD of France, JBIC, KfW, and the World Bank) belong to the second category. In grant aid, the "Like-minded" bilateral donor group has identified a range of actions that they can take to simplify and harmonize their procedures<sup>8</sup> and has begun work towards the development of a glossary and common vocabulary in ODA.

We can show the following activities in the third category, government and all donors:

1. Partnership groups including around 20 Government-NGO-Donor organizations have been formed. Most have made an active, coordinated contribution to the Government's 10-year plan and 5-year strategy, and to the Comprehensive Poverty Reduction and Growth Strategy (CPRGS), and are now moving from vision to action.
2. In some particular sectors, new ways of doing business in particular sectors have been developed with more formalized relationships and a move toward sector wide approaches. Examples of this are the Poverty Working Group/Poverty Task Force, the Forestry Sector Support Partnership, Ho Chi Minh ODA Partnership, Natural Disaster Mitigation, Small-and medium sized Enterprise Development, Transport, and Education Forum. In some of which donors try to support a common program through common mechanisms.
3. Most donors have shown their intention to align their programs with Vietnam's CPRGS, in essence the national Poverty Reduction Strategy (PRS), though this needs to be more concretely operationalized.

Moreover, at the preparatory workshop for the High-level Forum in Hanoi in January

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<sup>8</sup> The identification and comparison of the Government's and six bilateral donors' ODA management procedures was finalized in October 2001

2003, the Vietnamese government and the donor side came to share the necessity of three principles: (i) respecting national ownership, (ii) a country-based approach, and (iii) ensuring diversity of aid modalities.

In line with this, we understand that MPI will launch a “Comprehensive Capacity Building for ODA Management” program in June 2003.

## Chapter 3 Methodology of the Study

**D**ue to the conceptual and practical difficulties arising from quantifying transaction costs, this study is largely qualitative. Vietnamese project authorities in various sectors gave their views on several issues in relation to transaction costs and burdens, which were both subjectively and objectively imposed on their projects. These are illustrated as case studies here. The main stages of the study include selecting ODA projects, designing questionnaires, conducting the survey and preparing the casebook.

### 1. Projects Selected

Four sectors including transport, agricultural and rural development, education and training and health have been selected based upon two pre-set criteria:

1. The sectors that the majority of donor agencies are now interested in implementing technical assistance projects and programs, and where GOV-Donor-NGO partnership groups are very active;
2. The sector receiving the largest amount of ODA in Vietnam.

Then for each line ministry (for each corresponding sectors), 20 grant-aid projects will be selected with close consultation. These projects will be categorized by the level of transaction costs imposed on the projects, by the type of ODA forms (training courses, seminars, projects, and equipment, etc.), by the type of aid (tied and untied procurement conditions), by donors and by the line departments in each line ministry.

### 2. Questionnaire Design

The questionnaire is divided into four parts:

1. The first part asks the respondent to describe the project by project stage (according to Article 4 of the Government Decree 17/2001/ND-CP) and by the transaction costs/burdens incurred (according to the definition of transaction costs/burden developed by UNDP).
2. The second part asks the respondents to complete a table detailing all the burdens incurred at each project stage. This part focuses on questions such as: (1) Where and at what stage are ODA transaction costs incurred? (2) To what extent are ODA transaction costs incurred at each stage of the project cycle? (3) Who creates the ODA transaction costs? (4) Who will actually bear ODA transaction costs? (5) Why are these considered a burden?
3. The third part is used to qualitatively assess the transaction cost/burden in each stage and the emerging costs and burdens resulting from the transactions.
4. Recommendations for improving the efficiencies of ODA projects will be recorded in the fourth part of the Questionnaire.

### **3. Survey Execution**

Based on a Questionnaire prepared by CIEM (and approved by JICA), the survey is then carried out by a team of national consultants. These consultants are then in charge of conducting surveys in four sectors (transport infrastructure, agriculture and rural development, health, and education and training). Cases have been selected based on the recommendations of each line ministry in consultation with JICA. They developed case studies from the surveys and then submitted theses to CIEM for inclusion in a synthesis report.

### **4. Overall Description of the Survey Sample**

The survey started in November 2002 and interviews were completed in February 2003. The total number of projects surveyed was 80, which were divided equally between each of the 4 sectors. The following highlights some stylized facts concerning the survey sample by donor, by type, by form, by budget:

1. By donor: There are 23 projects funded by Japan's partners (transport infrastructure: 9 projects, agriculture and rural development: 2 projects, health: 10 projects, and education: 2 projects). The other projects were funded by other donors which enabled a comparison of Japan's ODA transaction costs with other donors. [NOTE: Not All cases introduced in this report had equal transaction costs to Japan's ODA and of course it is not always equal to transaction costs created by within a single donor].
2. By type: All projects are in the form of grant aid projects.
3. By form: The majority of the projects (76% of total surveyed projects) were either research projects, equipment supply projects or cooperation projects.
4. By budget: On average, each project had a budget equivalent to USD 5.6 million. The smallest project had a budget of USD 40,000 and the biggest project had a budget of USD 40 million.

### **5. Assessment of the replies of the recipients**

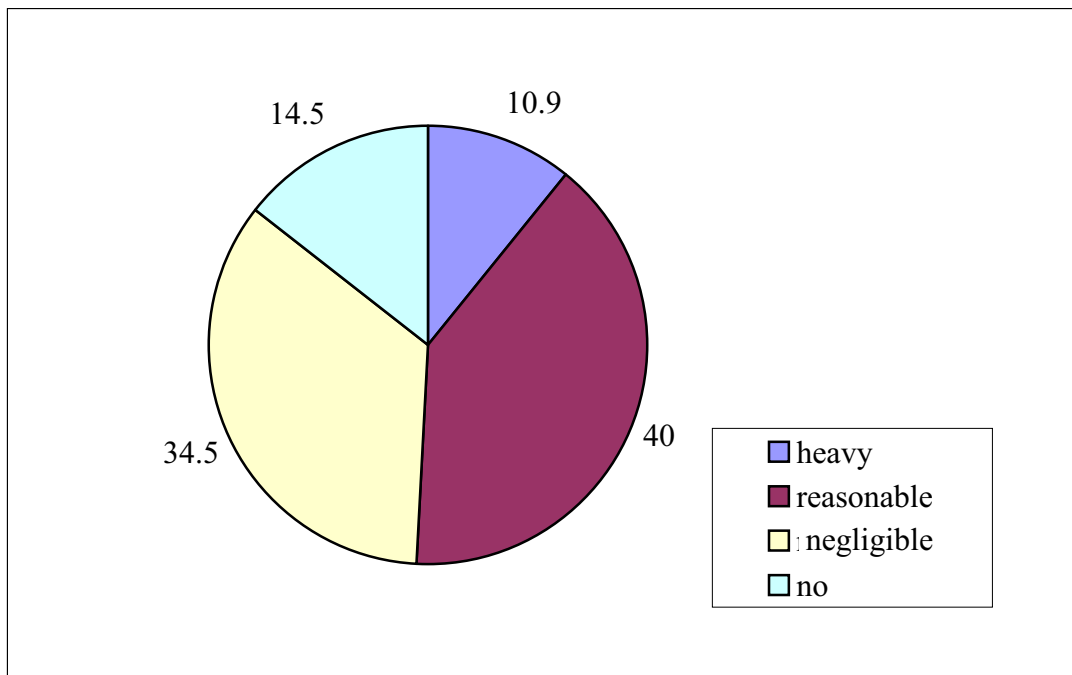
In examining the replies and views of the ODA recipients, we recognized a number of difficulties which the recipient agencies are now facing. These difficulties originate from both the donors and the Vietnamese Government. The latter is also a considerably heavy problem than that felt by donors according to the survey replies. Thus, we classified them into two areas, and finally tried to draw some implications for improving the donor practices in Vietnam in the future.



## Chapter 4 ODA Transaction Costs: A Survey-based Assessment

### 1. ODA Transaction Costs: A General Observations

Based on the results of the questionnaire, it is certain that transaction costs do exist in most ODA projects. Only 14.5% of interviewees thought transaction costs did not occur in their projects, from the very first stages to the end of the project. More than half of the projects (50.9%) reported that transaction costs are either reasonable or heavy, while 34.5% of the projects have negligible transaction costs. Though over 80% of those surveyed recognized there were transaction costs in their projects most of these felt indifferent about the levels of the costs themselves with 14.5% seeing no transaction costs, 34.5% facing negligible costs and 40% feeling costs were reasonable.



In addition, we also need to emphasize that we did not observe any clear correlation between aid effectiveness and efficiency with (1) existence of ODA transaction costs or cost size, (2) procurement conditions (tied/untied), which some donors try to link with costs. We should examine these observations more prudently because the definition of transaction costs is complicated and often difficult to understand for both interviewers and interviewees, and results should not be simply compared.

## **2. Burdens felt at Each Project Stage<sup>9</sup>**

The Figure below shows the percentage of respondents (projects) reporting the levels of transaction costs incurred in each project cycle<sup>10</sup>. It appears that most transaction costs are most frequently seen in the following stages of projects, design, appraisal & approval at pre-implementation, procurement of consultants & equipment, financial management, and monitoring & reporting at the implementation stage.

Some of these transaction costs can be attributed to the Vietnamese side, especially appraisal and approval costs, but others stem from donor practices. To concretely observe these transaction costs, we will look at a variety of cases in the following chapter.

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<sup>9</sup> According to Article 4- the process of ODA attraction, management and utilization of Government Decree 17/2001/ND-CP dated 4<sup>th</sup> of May, 2001 a project cycle includes the following main stages:

Strategy planning (strategy formulation)

1. Developing the national list of priority project/program proposals for ODA mobilization and utilization;
2. Mobilizing ODA resources
3. Negotiating and concluding international framework treaties on ODA;
4. Notifying international framework treaties on ODA;

Project formulation (identification)

5. Preparing ODA project/program documents (including pre-feasibility and feasibility study report)
6. Appraising and approving ODA project/program documents
7. Negotiating, concluding and ratifying or approving international specific treaties on ODA

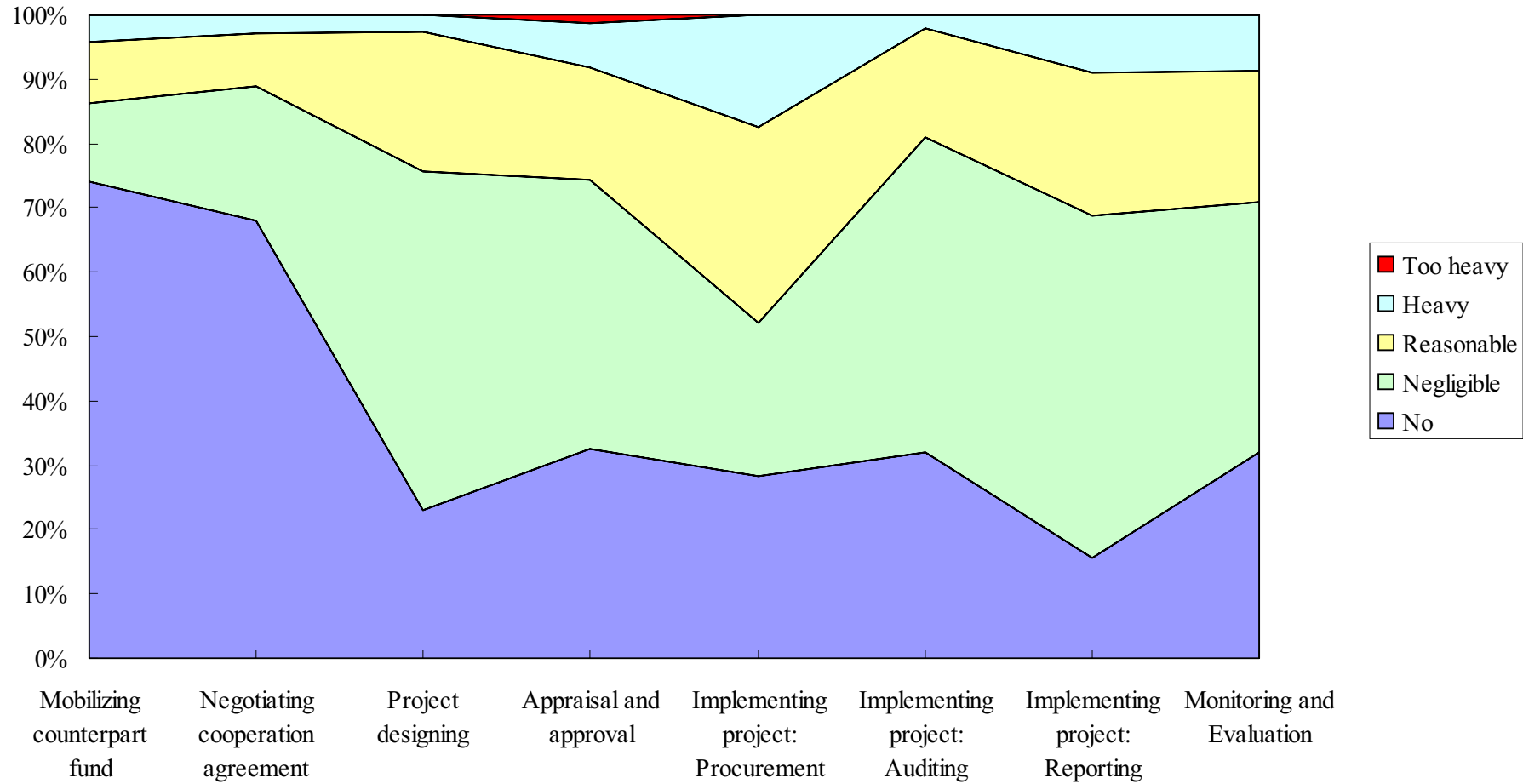
Implementing ODA projects/programs

8. Implementing ODA project/programs:
  - Procurement
  - Auditing
  - Reporting

Monitoring and evaluation

9. Monitoring and evaluation

**Transaction Costs Incurred by Each Stage of Project Cycles**



## Chapter 5 Voice of the Recipients

### 1. Project cycle

This chapter describes the views or voices in ODA and details the situation that recipients are facing in receiving grant aid from donors. Typical case studies will be reviewed to shed light on how and why transaction costs are incurred at each cycle of a project. These views can be summarized as follows

#### 1. **Pre-implementation**

- ✓ Donor-driven project preparation (Donor)
- ✓ Quality of international consultants (Donor)
- ✓ Long process to start projects on the donor side (Donor)
- ✓ Insufficient project design (Donor)
- ✓ Lack of project preparation capacity (GOVN)
- ✓ Complicated internal procedures: appraisal and approval (GOVN)
- ✓ Complicated internal procedures: securing counterpart funds (GOVN)

#### 2. **Implementation**

- ✓ Over-presence of donors (Donor)
- ✓ Quality of international consultants (Donor)
- ✓ High proportion of budgets for international consultants from the total project budget: what is its right ratio to total budget? (Donor/GOVN)
- ✓ How should the recipient be involved in the project management? Is it rationale for the donor side to request the Vietnamese side to assign high-ranking officials as counterpart personnel and to arrange project offices? (Donor/GOVN)
- ✓ Little financial incentive for counterpart personnel to join the project (Donor/GOVN)
- ✓ Procurement; price rather than quality? Moreover, a too greater centralized system of procurement from the donor headquarters (Donor)
- ✓ Complicated procedures on the donor side: budget approval, for example, delay of disbursement and budget cuts (Donor)
- ✓ Changes in aid delivery mechanisms (Donor)
- ✓ Lack of project management capacity (GOVN)
- ✓ Insufficient decentralization from donor headquarters/regional offices to the field office (Donor)

## **1.1 Pre-implementation Stage**

### **Donor-driven project preparation**

It is necessary to go back to pre-implementation stages when we examine transaction costs. The first case we will look at highlights the problems of linking transaction costs with the question of how to ensure national ownership. To ensure a national ownership is reached by the beneficiaries of a project directly, donors have introduced a participatory approach for project formulation and design, in this way they have made efforts to reflect the requests of the recipient side in project formulation. For example, a donor may take the following steps along with the ODA recipient: (1) participatory analysis>> (2) problem analysis>> (3) objectives analysis>> (4) examining alternatives>> (5) developing its project design matrix (PDM). This JICA study reflects the fact that such practices are not practiced sufficiently, especially as most project preparation is donor-driven. Most ODA recipients surveyed feel their requests are not fully listened to or reflected by donors.

#### **Case 1**

*In the case of one project, prioritized targets were not felt to have been selected rationally. Targets did not reflect the demands of the Vietnamese side but were the donor's priorities. This led to a reduced enthusiasm on the Vietnamese partner side, a certain level of time wasting for the project manager and project implementers and finally caused the ineffectiveness of resource allocation in the use of consultants and in the purchasing of unnecessary equipment.*

It is often the case, seen also above, that donors and their international consultants ignore the views of the recipient in project formulation even where these views have been clearly stated. Occasionally, project design can take more time than necessary, as detailed below, placing a further or greater burden on the recipient.

#### **Case 2**

*A donor had planned to start technical assistance in one sector. The donor later discovered that another donor already provided similar assistance. As a result, the donor tried to launch another project in a different province. The provincial people's committee did not know the project concept sufficiently. The donor then had to re-design the project for this province. This caused a five year delay in implementing the actual project. The Government officials in charge of this project felt that their previous comments had been ignored and many of them no longer wanted to support the project. As a result it took more time than would normally be necessary, and an excessive level of effort was spent in getting a consensus amongst the government departments concerned.*

#### **Case 3**

*Another project suffered substantially from the over-centralization and over-dominance*

*of the donor in its decision-making. Over-centralization and over-dominance of the donor in decision-making can be seen throughout a project cycle, from beginning to end. For example, there was a gap between the budget approval and the actual committed budget, meaning further project funds had to be mobilized to fill the gap between approval and commitment. This task was carried out by the donor. However, the donor rarely discussed with the line ministry and the Vietnam project manager the source of the mobilized funds that the donor intended to ask for nor were the different priorities of source funds discussed with the ministries. This may then lead to a low level of efficiency since the recipients demands were not considered properly, causing a low disbursement rate (around 30% of funds were disbursed by the end of the year). In concluding a projects agreement, especially in disbursement, appraisal and approval of a project plan and design, the donor stipulates and designs all requirements without any participation from the Vietnamese side.*

The reasons for this disregard of recipients views and opinions may be due to the working styles of donor consultants, who often just collect the necessary information on relevant sectors, visit and have discussions for only a short time in Vietnam itself and then design the actual project in the donor home country. On completion the donor consultant simply informs the recipient agency of the project design and does not consult in the final design of the project.

#### **Case 4**

*Often in the project design phase, the, voices, views and opinions of beneficiaries are usually ignored or not adequately taken into account. This leads to deficiencies in the project design, and results in difficulties and burdens during the implementation phase. Why does this happen? There are several explanations from Vietnamese counterpart personnel. Firstly, consulting firms usually conduct project design in their home country after conducting a survey in the host country. The time spent in Vietnam and in the project areas is usually short, thus they can not grasp the specific conditions of Vietnam or in the project areas.*

Language is also another large problem in project design. Vietnam is not an English-speaking country and recipients have often had difficulties in discussing project design with donor consultants, especially at the project level, due to these language problems. This sometimes leads to a donor-driven situation. A lack of experience can also force the recipient be more passive in dealing with donor consultants on some occasions. It can be said that the personal characteristics of most of foreigners maybe be too strong or dominant for many Vietnamese people.

#### **Case 5**

*At the preparation stages of the project, the Vietnamese side drew up a list of project activity requests and provided them to a donor. On further examination of the Vietnamese sides priorities, they found they were responsible for only providing information to the donor, and were involved in the project process very passively. This is partly because of a lack of expertise in many areas on the Vietnamese side and partly because of a lack of foreign language proficiency, especially in English. The Vietnamese*

*staff did not have the necessary experience and could not communicate in English. To re-train the Vietnamese side would have taken a substantial amount of time. Even during a project, these Vietnamese staff may not be competent or possess enough of the right skills to work with the foreign partner.*

What is the main reason of the above mentioned problems? How do donors find, formulate, and design new projects in general? In the case of a donor, at first, a donor agrees to the basic direction of the project, for example, target issues, target regions, project periods and project budget. Based on this framework, a donor puts its preparation work out to tender. Then, a number of consulting firms develop proposals for the project and bid for it. A donor selects the consulting firm which meets the donors' criteria (effectiveness and relevance of the proposal etc.). Following these processes, the consulting firm who has won the bidding process will visit Vietnam for a field study, and has meetings with the Ministry of Planning and Investment (MPI) and the ministries concerned. Ideally, the proposal prepared by the consultant firm is revised in accordance with the results of the meetings and field trips. However, in reality, the firm confines itself to fine-tuning the project in many cases. In the case of one donor, they assist the Vietnamese side in developing a project document. In the case of another donor, they basically wait for the Vietnamese side to submit a project proposal to them. Every donor has a mechanism to reflect the requests & opinions of the recipients. Despite of this, these cases tell us that these mechanisms do not always function well and in practice project preparation tends to be driven by the donor side in many cases.

What is the main cause of this situation? We may be able to explain why as follows: *Firstly*, one of the key factors is who works on first draft of the project? *Secondly*, how long can international consultants spend in intensive discussions on project design with the Vietnamese side? If intensive discussions are assured, donor consultants can design the project with the full consideration of the recipient's requests. *Thirdly*, to what extent are donor consultants actually engaged in project design work in Vietnam versus design work in their home country? This may also be closely related to the extent of the decentralization on the donor side, and the ability of its international consultants to operate within a country. Some consultants are not based in Vietnam, and therefore have to do the majority of project design work in their home country. *Fourthly*, how much can the donor side (or its consultants) make its working schedule more flexible? Most donors are dependent on consultants in project design stages. Donors stipulate the length of their consultancy contracts. Consultants tend to place a higher priority on their efficiency in completing their work on schedule, at their convenience, often at the expense of the recipient's convenience, and do not always spend enough time with the partner. In addition to this, the budget cycles of donors are also subject to time pressures placing pressure on consultants to complete to contract deadlines. This often creates burdens for recipients. In this case, it is important for the donor side to listen to the needs of the recipient. In this process, close communication with the recipient and the flexibility of donors are important elements.

From the viewpoint of the Vietnamese recipient, *Firstly*, many recipients have complained about the bidding process in order to select the consulting firms on the donor's side. Donors restrict this process by organizing tenders within donor home

countries. *Secondly*, donors and consultants often consider the project design process as their own affair, with the Vietnamese participating only through the provision of information or some comments and not active in the design process. If the Vietnamese participate more thoroughly in the project design process, technical assistance elements become much more of a process of knowledge transfer.

English-language problems on the Vietnamese side and the lack of experience in negotiating with foreign consultants and donors are also likely to be very important. This is a very elementary factor, but it often seems to result in a donor-driven project formulation and designing. With this in mind, the solution is for the Vietnamese side to upgrade its English proficiency and get greater familiarity of negotiating with foreign donors.

### **Quality of international consultants**

When donor consultants are the main element in project formulation and design, the quality of consultants is of the key concern. We found a great number of views and opinions on this matter from recipients.

#### **Case 6**

*Many donors depend on international experts at the project design stage. However, a recipient agency claimed that the capacity of these international experts was doubtful. Many of the recruited international experts did not have enough knowledge about the situation in Vietnam. Some experts lacked practical hands-on experience as they were students of the University (graduate program), to which the consultant firm was attached. This situation led to a series of problems arising during the project design. International experts usually do not understand what Vietnam needs to develop its economy. In addition, many experts ignored the recommendations of Vietnamese experts and their suggestions for priority projects and failed to include these in project recommendations to donors*

The Vietnamese side is concerned about the knowledge levels, relevant sector experience and also the understanding and experience of working in Vietnam of many donor consultants. Recipient agencies are not only dissatisfied with donor experts performance due to their lack of knowledge of Vietnam and but also because of their lack of expertise in the relevant topic. Moreover, the recipient side feels their voices and opinions are sometimes ignored by donor consultants.

#### **Case 7**

*Under the Agreement of a technical cooperation project, a number of fact-finding missions came to Vietnam from a donor's home country. A counterpart agency in a province was one of the locations of these visits. Through information collected from the fact-finding missions and recommendations by various departments of sectoral ministries, the project team quietly started the preparation of the project proposal and submitted it to the authorities concerned on the Vietnamese side. After a series of discussions on procedures and agreements on the target programs, the Vietnamese and*



*a donor sides agreed to conduct a review. The donor sent consultants to the project to help with the drafting of the project proposal for submission to the donor side. The preparation of the proposal was long and painstaking work. The main cause was that the donor consultants did not understand the Vietnamese situation, and this resulted in a number of discussions to explain the situation to the consultants by the project staff. Many heated discussions occurred between the international experts and the Vietnamese experts. The time span from preparation to the approval of this project was three years.*

In the above case, donor consultants assisted the recipient side in formulating and designing a new project. However, the recipient side felt there were a number of problems due to the lack of understanding of the donor consultants of the Vietnamese situation. As a result the recipient side had to explain the present situation in Vietnam to them again and again. This resulted in delays and a longer time period for this phase. Of course, it's basically necessary for the recipient agencies to explain and discuss the present situation in the relevant field because this is consultation process between the recipients and donor consultants at the beginning stage of the activities. Therefore, the recipient side has made efforts to do so. The critical here is if its extent is acceptable or not.

Why did the above case example take place? There are two approaches for donors in formulating and designing new projects: the first approach is through consultants, which are recruited through international competitive bidding within the donors home country, who then visit Vietnam and are engaged in the work. The second approach is for donors to send a project formulation mission, which consists of the donor agency and experts from the line ministries concerned of the donor government. Regardless of the approach, the quality of tender documents (terms of reference, TOR, of consultants) is very crucial.

In the cases we have reviewed above, we can say the following: *Firstly*, the donor side needs to develop its TORs more carefully, through close consultation with the Vietnamese side, and then select qualified consultants. To this end, the field office of donor agencies plays a vital role in analyzing the real situation of the relevant sector or area, and in conveying it to those developing the TORs. *Secondly*, in the case where there are a number of consultants familiar with the Vietnamese situation, donors should seriously consider the recruitment of those who have a strong expertise in the relevant fields. Though this would appear a logical approach it is often not being put into practice at present. The critical point here is that some consultants do not have a strong expertise and understanding in the relevant sectors. *Thirdly*, why don't donors assign their field offices to select relevant consulting firms? This could produce a number of advantages: (1) the recruitment of consulting firms located in Vietnam, ensuring an understanding of Vietnam (2) local authorities could be invited to examine the level of understanding of the local situation of the consulting firms. In order to secure the quality of the bidding, donors can send some of their experts to Vietnam.

**The long process in starting projects on the donor side**

One transaction cost identified by survey respondents was the long process and time needed to start projects by donors.

### Case 8

*The process of project approval consisted of the following procedures: (1) submission of the document to a sectoral ministry, (2) submission to the Government, (3) Permission for project proposal development, (4) negotiation with the donor, and (5) re-submission until the Project was approved. It took 2 years from the date of Project proposal preparation to the date of its implementation, resulting in changes in the Project timeline, and changes in the project content and duration as a result. The initial title of the project also had to be changed when it was approved. However, after two years a great number of beneficiaries had already been engaged in other posts. According to surveys conducted at that time, the number of beneficiaries turned out to be inconsiderable, so the Project had to be renamed with the present title.*

How long does it usually take donors to decide if they start the project or not after they receive a project proposal? This duration varies. In one case, it took around one year, and in other cases, it has taken four to ten years, however, this time period does appear to have shortened recently. There are a number of reasons for these decisions taking such a long time. *Firstly*, it depends on the completeness of the project proposal the Vietnamese side has developed and submitted. After the counterpart agency on the Vietnamese side submits the project proposal to a donor through the MPI, a donor sometimes makes comments and then the counterpart agency revises it based on these comments. This process can repeat several times. Consequently, this process often takes a long time to finalize a project document. This can result due to the poor quality of the project proposal, which is often rooted in the low ability of the recipient agency to develop a proposal which meets the expected standards of the donor. If the project proposal is not well developed initially and if its approach to solve the problems are not appropriate, it is inevitable that the recipient agency is forced to make numerous alterations until the quality of documents meets their expected standards. In the case above, the donor side may have needed to assist the recipient agency draft the documents. In some cases, consultants themselves become a factor in prolonging the process. Despite a lack of understanding of the situation in Vietnam, consultants try to develop a document without respect for suggestions given by the Vietnamese side. As a result the Vietnamese side fails to agree to the document produced. It also brings about a delay at the project preparation stage. *Secondly*, the complicated procedures of appraisal and approval at the donor side underlie this kind of transaction cost. *Thirdly*, the delays are rooted in the financial and human resource constraints of the donor. Even if a donor receives a project proposal that fulfills a donor's aid strategy, priorities and criteria for Vietnam, a donor cannot always start it due to resource constraints. In this case, it is likely to be an unavoidable reason.

The recipient regards these as transaction costs despite their unavoidable nature for several reasons. *Firstly*, even if the donor's requests to the Vietnamese side to revise the document are reasonable, these reasons may not have been fully shared with the Vietnamese side. As a result the recipient views this as a transaction costs. *Secondly*, it

introduces a level of uncertainty for the Vietnamese side because they cannot ensure the predictability of a donor's assistance. If country A cannot start a project soon, the Vietnamese side has to look for alternatives instead of this country. Despite the urgent need, as long as country A is suspended in the making of a decision, the recipient cannot approach other donors.

In situations such as these we may be able to summarize the following. *Firstly*, the Vietnamese side needs to develop realistic project proposals. *Secondly*, where donors send international consultants to assist the recipient develop a proposal, consultants should aim to develop an understanding of the Vietnamese situation and the sector being dealt with in order to ensure the greatest level of understanding and expertise in a specific issue. This would assist in shortening the duration of drawing up a final project proposal, and reduce transaction costs. It will also be necessary to explain why the proposal needs to be revised by the Vietnamese side. *Thirdly*, donors should ensure transparency and accountability during the project formulation process and fully inform the recipient side of progress, this will make it easier for the recipient to forecast and plan for the future

### **Insufficient project designing**

As we saw in an earlier example, one of the main transaction costs felt by the recipient are the costs at the preparation stage, as it takes a substantial amount of time for the recipient to receive answers to their queries from the donor side after they have submitted a project proposal. As a result, they cannot develop a time frame or future implementation plans. Though it is recognized that a shorter project design period is not always optimal when we consider possible later transaction costs, especially at the implementation stage, it may be.

### **Case 9**

*Transaction costs can result due to efforts to minimize burdens during preparation phases. All the parties involved in a project funded by a donor must make every effort to fulfill all required procedures in the shortest possible time period in comparison with similar projects. However, this can result in the irrationality of a project design in terms of content and progress for some components which may only be recognized during the implementation phase. This could be due to either an unclear project plan, ignorance of the beneficiaries' needs, unsuitability of the project to the actual conditions in the field, and failure to anticipate possible risks. In addition, components maybe designed illogically and too widely. All these situations have imposed large problems for this particular project.*

In another case, due to the haste in preparing a project the design was not carefully carried out. The establishment of the projects goals was, occasionally, not well developed and lacked a professional rationale. In this case, insufficient project design also lead to the creation of transaction costs during the implementation stages.

### Case 10

*At the project designing stage, the project plan was not developed carefully and thoroughly. Many objectives failed to be appropriate. The donor and the project set extremely ambitious targets for the project. Those targets were set up without a firm scientific or realistic foundation, which was only recognized during the implementation phase of the project. As a result changes to the project targets were required at the implementation phase. The coordinating agency retained the general targets and dropped all the specific ones.*

How should project preparations be carried out? In general, a donor may take the following steps (1) conducting an analysis of the real situation in the relevant sector in Vietnam (including studies in the donors home country as well as in Vietnam)>> (2) holding discussions with the Vietnamese side and recipients>> (3) designing the project>> (4) developing a project proposal. Actual project design may take the following steps: (1) conducting an analysis of the present situation (including the collection of necessary information on national strategies, policy measures to be taken, relevant projects and programs, and classifying development issues and challenges)>> (2) developing the basic plan of the project (including overall goals, project purposes, outputs, activities, input plans, monitoring & evaluation frameworks, and implementation frameworks)>> (3) conducting a general assessment of the project (the relevance, effectiveness, efficiency, impact, and sustainability). However, not every project follows these steps. This is partly due to the fact that these steps are not always needed depending on the features of the project, such as its scale and budget and its background for implementation (such as diplomatic reasons).

From the Vietnamese side transaction costs should be considered as follows: *Firstly*, insufficient project design often brings about problems especially at later, implementation stages. *Secondly*, it is often felt by the recipient that the donors fail to listen to their views and opinions carefully. As a result, recipients are frustrated with the donors' attitude. *Thirdly*, it is sometimes felt that donor consultants often try to design projects without sufficient understanding of the actual situation in Vietnam. When the latter two factors occur recipients feel the designed project does not meet their requirements.

In such situations, the followings might offer a solution to problems felt. *Firstly*, the donor should not be hasty in designing a new project. Of course, this may depend on the budget scale of a project. However the donor should, at a minimum ensure qualified consultants with a sufficient knowledge of Vietnam and a strong expertise in effective project design are employed in the project. *Secondly*, donors need to send qualified consultants and ensure a participatory process is ensured and the opinions and views of recipients are considered.

## Lack of project preparation capacity

### Case 11

*The lack of experience in preparing future project budget estimates, particularly the lack of a capability of foreseeing future problems that may arise has resulted in consequent project adjustments, amendments and reassessments that became extremely costly in terms of time and money.*

On the other hand, even where a project is not well designed, it appears that recipients almost always fail to criticize the donor for their failures in project design and insufficient efforts in listening and incorporating recipient's views. Recipients seem to recognize their weakness in expertise in relevant fields and their poor ability in project formulation and design. Due to these gaps in knowledge and experience recipients often fail to put forward their views and ideas for projects in areas such as target-setting, input plans and monitoring and evaluation mechanisms for projects during discussions with the donors. They fail to pursue their opinions and push their project ideas. Moreover, the counterpart agency may feel it does not possess the capacity to predict future problems at the implementation stage.

In summary we may be able to say: *Firstly*, training courses under the framework of “the Comprehensive Capacity Building for ODA Management” which will be initiated by MPI and introduced at the mid-term CG meeting in Sapa with the support of the World Bank and the Like-minded Donor Group, should not only cover general knowledge on project management, but also introduce various experiences and lessons from the past or on-going cases. It should also be practical and pragmatic, not excessively theoretical and dogmatic. *Secondly*, the donor side should make efforts to upgrade the risk management ability of recipients, by explaining the potential risks the Vietnamese side are exposed to, and holding close consultations with them. In this regard, the donor side does not have to implement something new, rather it should be expected at each stage of the project. This is an important element to overcome problems.

## Complicated internal procedures: appraisal and approval

Next, we observed the transaction costs created by the internal characteristics of the Vietnamese recipient. According to the results of several interviews, this type of transaction cost is considerably heavy.

### Case 12

*In this technical assistance project funded by a donor the lessons learnt from other projects led to a series of project documents being prepared carefully. However, a number of problems occurred in getting approval from the Vietnamese side which created a number of burdens for the recipient agency and its sectoral ministry. Although the Government has developed clear procedures and timetables for issuing ODA project approval, these procedures were not strictly followed. Submission of the project documents to the Ministry of Planning and Investment and other line Ministries was asked for twice after a series of delays and problems with the sectoral ministry in*

*charge. As a result it took 20 months to get approval for the operation of the project. In addition, a range of unclear rules also added to the costs that the project had to bear, such as the importation of a car for the project. It was ruled that a car could not be imported, forcing the project to purchase a domestically produced car, which did not have tariff exempt status.*

Even when the negotiation process with the donor is over, other types of transaction costs often remain for the recipient agency. This is due to the complex internal procedures of appraisal and approval of new projects within the Vietnamese government. After completing the long process of appraisal and approval inside the sectoral ministries concerned, projects are then brought to MPI. In some cases, it takes a greater time for approval than is acceptable because the government's priorities on ODA projects and the criteria of appraisal are not always clear, leading to delays. According to one interview, it can take around twenty months for a project to be approved.

### **Case 13**

*One particular project funded by a donor that was well aware of the needs and situation in Vietnam felt strong support from the ODA recipient. Both sides quickly built a mutual understanding and came to a quick agreement over the project. The project itself mainly funded by the donor, with no counterpart funds from the Vietnamese side being required. No transaction costs occurred during the disbursement and implementation stages. However, transaction costs did arise in the preparatory approval stages. These costs were mainly caused by complicated, time and effort consuming procedures in project proposal preparation and approval which both sides were forced to follow. The Vietnamese staff involved found themselves waiting for a substantial amount of time for approval, unable to carry out any work on the project. These staff bore the opportunity costs as they could have been employed on other projects or in training activities in the recipient agency.*

### **Case 14**

*One Sector Program Support project funded by one donor has proved a huge program, covering several sub sectors. One sub-component of the project is the development of capacity building for an Information Center under a sectoral ministry. This sub-project is considered as only a small subproject of the whole program. However, the National Management Unit of the Program still required the approval of this sub-project as an independent project, forcing the Center to submit the proposal to related ministries and departments within the sectoral ministry in charge and also MPI. This procedure was viewed costly and complicated.*

Transaction costs are also observed in the case where various sub-components belong to a single project as the following shows.

### **Case 15**

*One example is a project, where there were a number of problems with the Vietnamese authorities in approving the project due to the fact that they lacked any real professional understanding of the research topic. In particular, the project approval procedures were*

*complicated and redundant. This resulted in project staff and proponents spending substantial time and effort to explain and convince the authorities of every minor detail of the project. Accounting methods proved as equally problematic. Convincing the ministries concerned and localities selected for project implementation proved even more difficult. Finally, substantial problems were experienced in one part of the project, convincing teachers and parents of normal children to allow hearing-impaired children to sit in the same classroom and follow the same curricula, due to the lack of any similar experiences.*

### **Case 16**

*In order to match the demand in Vietnam for establishing a sectoral policy to support a national target program in a new development area, a donor provided non-refundable support to the sectoral ministry in charge of this area. However, approval in this ministry took a long time due to a lack of agreement amongst ministries. This caused a considerably prolonged approval process.*

Most interviewees expressed the view that internal procedures for project appraisal and approval of new projects were complicated and substantial. The Decree No. 17 issued in 2001 stipulates these procedures in its Article 18 (Appraisal of ODA Projects/Programmes), Article 19 (Appraisal of ODA Technical Assistance Projects/Programmes), and Article 20 (Approving Authority for the Contents of ODA Projects/Programmes) which are found in Chapter III (Preparation, Appraisal and Approval of ODA Projects/Programmes).

However, many recipient agencies recognize that Decree No. 17 is not put into practice properly. This may be due to the following: *Firstly*, it is due to an excessively centralized system within the Vietnamese government. It is necessary for ODA recipients to get approval, regardless of the extent of a projects importance or size (at the lower level of the Government Office), from the central Government level and the MPI (note: in the case of the project whose total budget is less than one million USD, its procedure is more simplified). The multiple mandatory approval of a number of ministries concerned to projects causes procedures to be more complicated internally and causes the procedures to take an extended amount of time. In addition, in the case where the project is designed with a new concept or methodology for Vietnam, it is sometimes difficult to persuade the government of its benefit, importance and necessity. *Secondly*, many recipient agencies are unclear of the criteria required for project appraisal. If the recipient agency knows the criteria before hand, they can try to cover all the required information in the project proposal. But in reality, it is not known clearly, resulting in an unclear project proposal which the agency is then forced to negotiate with the MPI and the other ministries concerned.

In these situations, we might need to take the following measures. *Firstly*, it is necessary to ensure transparency and accountability of aid management, in concrete dissemination of priority & criteria and thorough implementation of the Decree No. 17 on the Vietnamese side. *Secondly*, to this end, it is also necessary to conduct a diagnosis of the present situation of appraisal and approval within the government: identifying where

problems may be and where there may be room for improvement. If Decree No. 17 aims at enhancing transparency and accountability of its procedures, why doesn't it achieve the expected results? The Decree may not have been accompanied by any relevant internal reform, such as the simplification & harmonization of procedures, and authority delegation to lower levels. If this is so it may be necessary to make revisions to Decree No. 17 making it more realistic, or to further implement reforms to the system of the government in itself.

### **Complicated internal procedures: securing counterpart funds**

As for other transaction costs resulting from the Vietnamese side, many interviewees pointed to the complicated internal procedures required to get counterpart funding. Along with the complicated internal procedures of appraisal and approval, this is significant. In providing a donor project with office space, counterpart personnel, and equipment, the recipient side is taking necessary procedures to securing them.. In one case, these costs are calculated and are made clear as a percentage in the total project budget. In another case of in-kind costs such as office space, assigning counterpart personnel, the donor side sometimes does not clearly recognize the fact that the recipient has to undertake these necessary procedures to access counterpart funds.

#### **Case 17**

*The objective of one technical assistance project was to improve the training and research capacity within a sector. Under the project framework, a center was established. The donor required the Vietnamese side to provide counterpart funds of VND 2 billion, about 7 % of the foreign funds. In order for the recipient agency to get these funds, there are a number of agencies and ministries to be dealt with a number of complicated procedures involved. Despite the target programs being supported by the authorities and the sponsor, the project preparation team spent a great deal effort to explaining the reasons for and gaining the counter part funds from the Vietnamese authorities.*

In the above case, the recipient agency faced difficulties persuading the ministries concerned in understanding the necessity of the project and the counterpart funds.

#### **Case 18**

*Even in a Project whose size was small, the responsibility chart of those involved in granting counterpart funds can be outlined as follows: the Government is committed to ensure the counterpart funds and then request the organization benefiting from the project to arrange for that fund by itself. That organization must endeavor to arrange that proportion of counterpart funds and if it cannot do so it must explain why. With regards to this project, the recipient institute was supposed to be responsible for 10% of the total budget as the counterpart funds. The recipient could not afford the supply of these funds and as a result they simply ignored the appointment of a number of their personnel due to participate in the Project.*

In the case of small-scale projects, recipient agencies are requested by ministries



concerned to finance counterpart funds on their own from their own resources. However, they are often unable to do so.

### Case 19

*Based on project implementation plans, the State Treasury will release the counterpart funds according to its Quarterly Capital Payment Plans, which are prepared by a Project Management Unit and approved by the sectoral ministry in charge. Disbursements should follow a capital withdrawal plan approved by its ministry. However, according to one recipient, delays in disbursement of counterpart funds usually take place because of cash flow problems in the Treasury. This recipient also thought that the delays in disbursing counterpart funds created a range of problems such as postponements in carrying out work that the Vietnamese side had to complete, and adversely affects the Vietnamese staff in the project. Moreover, the situation is made worse where the counterpart funding is in the form of in-kind costs such as offices and staff.*

In this case, the problems are more fundamental and not easy to deal with as the ministries concerned are unable to provide the necessary counterpart funds due to the lack of a state budget. As a result, delays in disbursement of counterpart funds undermine the smooth implementation of the project.

When signing the project document for starting the project, the Vietnamese side often agrees to provide counterpart funds for projects, usually in the form of offices, human resources, etc. This requirement usually comes from the donor who would like to ensure a national ownership and a level of responsibility in the project. These counterpart funds are viewed as negligible or as virtual, and they are usually disbursed slowly. However, most Vietnamese partners are state agencies whose budgets are dependent on the state budget, while at this stage, no additional state budget allocations for projects are approved until after appraisal. Thus, partner departments and other agencies must fund project preparation funds from their limited recurrent budget allocations, which become much more difficult where field visits or specialist consultancy services are required. As a consequence, in this phase, it is very difficult for the Vietnamese partner agency to get the involvement of national experts. On top of this, Vietnamese staff working in a project is not paid a salary. Many of them have work within projects while still having the responsibility for their previous positions. This leads to their ineffectiveness in both positions. In addition, the slow disbursement of the Vietnamese sides funds can also hinder a projects progress.

Decree No. 17 stipulates the procedures in Article 11 (Internal Financial Mechanism for ODA Utilization), Article 12 (Funding for the Preparation of ODA Projects/Programmes) Chapter III (Preparation, Appraisal and Approval of ODA Projects/Programmes), Article 26 (Counterpart Funding for the Start-up and Implementation of ODA projects/Programmes), Article 27 (Advance of Funding for the Implementation of ODA Projects/Programs) as well as in the Chapter V (Management and Implementation of ODA Projects/Programmes). It seems further reforms may be needed to ensure improved functioning.

## **1.2 Implementation Stage**

### **Over-presence of donor**

We have observed various occasions where national ownership is not ensured due to the level of donor-driven project formation and project designing at the pre-implementation stage. We can see a similar situation and view at the implementation stage.

#### **Case 20**

*One project to be implemented was in a top priority aid area of a donor. It aimed to assist Vietnam in constructing a social infrastructure for a number of provinces that suffered from shortages in this area. The donor side was aware that the purpose and the content of the aid to Vietnam was to provide financial support for the construction of 12 infrastructure systems in 12 provinces where a solid infrastructure did not exist. Donor consultants took the initiative in proposing to Vietnam the program objectives of the project and the implementation approaches. The responsibilities of Vietnamese side, represented by a sectoral ministry in charge, were to recommend localities that had an infrastructure priority, to appoint a few counterpart personnel who would help the project management board to work more easily at these localities, to participate in surveys and to recommend workers for the construction of these projects. The Ministry was also responsible for commissioning a committee to evaluate the quality of the construction. All financial formalities of the project were settled by the donor consultants, including: financial management during the process of surveys, design, and execution, purchase of material, equipment, hiring workers, foreign and Vietnamese experts... The Vietnamese side only took charge of the signing of the agreement, being involved in the process of quality evaluation, checking and taking over the buildings and transferring the usage and management of the buildings to the local authorities. However, Vietnam has the capacity to use such funds to conduct surveys, design and construct infrastructures of the same quality and quantity. The donor side could have been involved to take charge of monitoring, evaluation and approval of the project. By doing the project in such a donor led way resources were wasted which could have been used more rationally.*

#### **Case 21**

*Due to a lack of counterpart personnel with the required experience and skill levels, international consultants dominated the implementation process. Their dominance was reflected by their actions and failure to enter into discussions with the Vietnamese partners. These actions ranged from changing the projects objectives during the implementation phase, changing their aid mechanisms, changing the human resources working for the projects, to imposing strict requirements on the Vietnamese partners. Some of these actions may make a project run more smoothly or help to achieve the projects objectives; however they still impose a burden on the Vietnamese side. Many actions simply created difficulties for the Vietnamese side.*

**Case 22**

*In 1999, a donor agreed to support a sectoral ministry to develop a development strategy for several future years. The Ministry assigned an institute as the counterpart agency, and when implementing the project the Institute coordinated with an international consulting firm. Like many consulting firms, this firm did not have a technical team working in Vietnam. As a result the majority of work was initially done in the donor's home country. This way of organizing the work of consulting firms has created high transaction costs, especially in such an important project like this. Owing to the scope of the work, international experts based in their countries usually had to travel to Vietnam to gather information. To save money, these visits were always short, from 2-3 weeks to 1 month. Thus, the information they grasped often did not reflect the specific situations and conditions of Vietnam, especially institutional issues. In many cases these consultants rushed to leave Vietnam and return to their home country after the completion of a survey. During the process of carrying out their work in their headquarters, where they recognized gaps in the information they had gathered, they would send a number of experts back to Vietnam to gather the missing information. Regular flights cost the project a large amount of money, which could of been used more efficiently. Another drawback of this kind of organization was that their reports did not fully reflect the needs of Vietnam because the information exchanged between the consulting firms of a donor and the recipient was limited given the fact that they initially had little knowledge of Vietnam's needs and conditions. In addition, donor consulting firms often sent their reports to the Vietnamese consulting firms for comment just few days before submission deadlines, thus any comments from the Vietnamese side were drawn up very quickly and could not be incorporated into the final report to the donor fully.*

**Case 23**

*As an unwritten rule in all technical assistance projects, consulting firms, usually selected subjectively by a donor, were assigned to manage and direct all the tasks in the project. In this project example, the consulting firm managed the finances and human resources. They were also deeply involved in all cycles of the project from design, implementation, checking and monitoring. The Vietnamese partner was viewed as passive in all the activities of the project. This has impeded the effectiveness of the Vietnamese staff involved in the project and may cause inefficiency.*

**Case 24**

*A donor assigned a foreign consulting firm to take charge of managing a project. The Vietnamese partner did not play any role in running the project. In terms of financial management, all the payments could only be reimbursed with the approval of the donor. This discouraged the active involvement of the Vietnamese staff. In terms of human resource management, the foreign consulting firm selected experts without consulting the Vietnamese side. The budget to pay the salary for those foreign experts took a large part of the total budget (the budget for experts accounted for 74% of the total budget, of which 84% was for foreign experts).*

**Case 25**

*In many projects, the sharing of information between the Vietnamese partners and the international experts are very limited due to a lack of mechanisms for sharing and exchanging information. As donor consulting firms are often given many rights, they often ignore recommendations from Vietnamese experts despite the fact that many experts of consulting firms lack knowledge of Vietnam's realities and conditions. In many cases, the consulting firm failed to inform their Vietnamese partner of their own steps in the project.*

#### **Case 26**

*One further example is a project funded by a donor, where the Vietnamese project manager was not informed of the annual budget and investment. This lack of information sharing mechanisms resulted in many problems and deficiencies arising during the implementation process. Vietnamese partners can often have an attitude of passiveness in making plans and implementing activities for projects, therefore reducing the effectiveness of the project. The transaction costs may arise due to a lack of information sharing mechanisms and cooperation between the donor o consultant and the Vietnamese parties.*

In what way can donors ensure a national ownership at the implementation stage is one of the key elements in relation to sustainability after the project completes. There are various ways of thinking to ensure a national ownership, and we have a variety of experiences and lessons from past activities. As a result we cannot make standardized conclusions. One way is to establish a consultation mechanism to reflect the requests of the partner agency. As we saw above, the reality of establishing communication between parties may be difficult. Donors try to manage project implementation without any close consultation with partners in terms of annual planning processes and the staffing of each project. Add to this the fact that information is not equally known between donors and recipients, and then recipient will be unable to participate in management discussions on an equal footing. As a consequence, mechanism to include the views and opinions of the recipient are undermined. Donor consultants, who often are not familiar with Vietnam, stay in Vietnam only for two to three weeks in order to collect necessary project information. Even where they work on a report later on, based on the results of a project field study, they usually do not assure enough time for the recipient side to examine the project document. This leads to the recipient side not having enough time to make their comments or make them with careful consideration. The project implementation stage is extremely driven by the donor as a result of these problems making the recipient agency passive. Occasionally, it reduces the motivation of the recipient to improve the effectiveness of the project.

As a result of these recipient experiences we can summarize that it may be necessary for donors to review and ensure there are mechanism to share relevant information between the recipient and the donor and also to reflect the voice, views and opinions of the recipients. These mechanisms should not only be stipulated in the agreement document drawn up between both sides as a matter of formality, but also be put into practice in substance. These mechanisms should also ensure a day-to-day consultation between the recipient and donor. In this way, long-term expert can play a vital role as long as the quality of consultants meets expected standards. There remain the problems of recipient

passivity and reduced efficiency, especially where the donor is negatively placed in the dissemination of the total budget of the project to the recipient. Though the reasons for this may not be clear, an appropriate feedback mechanism would assist a clearer review of recipient requests and raise their importance.

### **Quality of international consultants**

When the purpose and essence of grant aid is the transfer of knowledge and technology, or capacity building to counterpart agencies, the role and quality of an international consultant and their quality is extremely important. However, many people point out this could be improved.

#### **Case 27**

*Consultants hired by a donor spent only a small amount of time in Vietnam. In addition, their initial knowledge about the Vietnamese context was limited. This left many issues unsolved during the project designing phase.*

#### **Case 28**

*Consultants did not have a sufficient Vietnamese background and knowledge of conditions, leading to an underestimation of the workload involved and necessary for meeting project objectives and also an underestimation of the budget for transporting machinery to the project sites.*

#### **Case 29**

*Foreign consultants did not fully understand Vietnamese organizational and management systems and their time spent in Vietnam was insufficient to fill these gaps.*

#### **Case 30**

*A donor sometimes was too rigid and lacked an understanding and experience of working in Vietnam. The foreign personnel changed all the times and the newcomers could not comprehend the background of the project and the country. In addition, communications were usually made indirectly mostly through e-mails resulting in the parties failing to understand each other, sometimes due to very minor details.*

#### **Case 31**

*This situation was seen in other projects such as a donor funded project where 60% of the budget was allocated to pay for international experts who usually were selected not because of their expertise or their knowledge of Vietnam but due to their close relationship with the chief accountant. The benefits gained from their expertise seemed small. In addition, local experts were selected carelessly with many being too old and who suffered difficulties when traveling to project sites.*

#### **Case 32**

*In the case of one project, the consulting firm was given the right to select international experts. Except for a few experts who had an initial understanding of the Vietnamese context and a good knowledge in their field, many of the consultants were selected not*

*because of their expertise but because of their close relationship with the consulting firm. This may lead to inaccurate and worthless recommendations, resulting in a misallocation of resources lent by this donor in the future.*

### **Case 33**

*In another example, most of the project funds were used to hire international experts from the donor's home country. However, not all of them were of a good quality. Many of them did not have a good knowledge of the Vietnamese situation with some not considered strong in their professional areas. Some of the consultants were mobilized to Vietnam due to their good relationship with the consulting company. Some of them were too old while some others were too young. It was felt by the recipient that the older consultants had received the trip as some sort of pre-retirement field trip gift, with their contribution to the project viewed as negligible.*

### **Case 34**

*In the late 1990s, a donor had decided to support a sector ministry in a specific area. In addition, this project provided technical assistance which leaned towards training and technology transfer, building the skills of the project recipient side consisting of the sector ministry and provinces belonging to the project. A government research institute was entrusted as the consultant agency in coordination with an international Consultant (a consulting firm from the donor home country won the bid) to carry out the project. The project started implementation in 2000 and expected to be completed by 2005. However, after two years (after 2002) the project mainly does only training work. This project is one that suffered most heavily from an over supply in this sector. The inefficient arrangements of international consultants had created many problems, leading to a high level of transaction costs. In fact, from the beginning, there have been too many changes, particularly key positions in the projects. After a few months of being implementation the Deputy Team Leaders post was changed. After around a half year of being implemented the Team Leader was replaced by a new person. A long-term expert was dispatched to Vietnam but after working for nearly a year the expert was discharged. Though this expert received a relatively high salary paid his contribution was seen as small and insignificant.*

### **Case 35**

*A project funded by a donor rightly met with Vietnamese demand in a specific area at that time, and developed in favorable conditions. After the successful completion of the first phase, the newly appointed project coordinator showed little cooperative attitude. He wanted to take away the Vietnamese staff's responsibilities. The deterioration of the working relationship was very counter productive for the project. The Vietnamese side had to officially complain about this to a supervising institute at the donor side. This institute then had to recall the coordinator and assigned the previous coordinator back to Vietnam. The consequences of this were the prolonging of activities for one an extra year. The delay required readjustment of expenditures and extra expenses for the next year. The extra costs amounted to US\$20,000. This institute had to contribute US\$14,000, and the recipient agency at the Vietnamese side had to take care of the remaining US\$6,000. Moreover, the project extension for another year definitely linked*

*to other burdens like administrative costs, opportunity costs and other costs for the staff. On the other hand the change of a donor coordinator also involved extra costs to be borne by this institute. There were also many other burdens faced by the project due to these problems. The reasons behind this should be looked at in more detail.*

Typically, the Vietnamese side is not satisfied with the following points: *Firstly*, donor consultants stay in Vietnam for too short a period and fail to grasp the real situation in Vietnam. *Secondly*, close communications are not ensured, and consultants tend to rely on e-mail for communication with partners. *In consequence*, consultants remain distant from the realities in Vietnam. *Thirdly*, donors sometimes assign consultants who may have already retired as consultants. As a result they do not meet the requirements of the Vietnamese side in some cases. *Fourthly*, donors send consultants whose expertise is often not strong enough to meet the projects requirements, as it is often difficult to recruit those who have adequate knowledge of Vietnam. These problems occasionally cause a delay and burdens in a project. In some projects, project performance deteriorates after the chief technical advisor is replaced. In summary, this shows one of the key elements to implement projects effectively is the *human factor*. The poor performance of consultants is therefore an extremely serious problem and it is of no surprise that many recipient complaints are in relation to this.

In these situations, we can address the following. *Firstly*, before the donor side selects a consultant, they should discuss the TOR of consultants and the qualifications required with the partner agency in an interactive way and reflect the recipients' requests into the TOR as much as possible. Then, donors should ensure the selection of consultants based on these consultations. In this case, strong expertise should be a priority over a better understanding of Vietnam as it may be difficult to recruit consultants with a substantial knowledge of Vietnam. *Secondly*, donors need to ensure the sufficient duration of consultant's stay in Vietnam. The Vietnamese side often seeks the opportunity to discuss project implementation with consultants. To this end, as we said earlier, the location of the consultants' base is also important in the case of developing a master plan and feasibility study, as shown in this report. If consultants establish a base in Vietnam or the field, it makes it easier to work with the recipient. *Thirdly*, the donor should establish interactive mechanisms to reflect the voice, opinions and views of the recipient at each stage of project implementation.

### **Higher proportions of expenses for international consultants in the total project budget: what is its right ratio?**

#### **Case 36**

*A huge amount of the project budget, about 40%, was set aside for the hiring of international consultants. There are some excellent consultants but many do not reach expectations. The general assessment is that the international consultants only managed to solve some general problems and were unable to deal with more in-depth technical problems. These consultants may be better suited to other countries rather than Vietnam. Vietnam is at a certain developmental stage and requires higher-level consultants. This has forced the project to hire non-donor country and Vietnamese consultants.*

The comments and complaints related to donor consultants were not only with regards their quality, but also the proportion of the total budget used to hire them. According to one sectoral ministry, consultants account for around 20~30% in the total budget for donors such as the World Bank and several others. In one grant aid project funded by a donor, consultants accounted for 60~70%, causing the sectoral ministry responsible to spend a number of months negotiating with the donor to reduce the percentage of the budget due to go consultant costs. This time wasted can also be considered a transaction cost. But is this rational or not? Grant aid projects tend to be much smaller than loan projects, as a result even if the same amount is spent on international consultants, say US\$50, 000, it is natural that its proportion in a loan project of a large amount (say US\$50 million) is smaller than that in a lower value grant project (say valued at US\$1 million) In addition, assuming the main objective of a grant aid project is the transfer of technology and knowledge, it is normal that the share of personnel expenses is high.

Despite these notable differences and characteristics of grant aid projects in general, if the Vietnamese side comments or complains on the high proportion going for consultant costs the following steps may help. *Firstly*, does the Vietnamese side fully understand and recognize the differences between loan aid projects and grant aid projects? *Secondly*, the following fundamental questions should be addressed, such as understanding what the Vietnamese side really wants from a donor? Is it knowledge and technology in the form of human resources or something else? When considering the complaints of the Vietnamese side, we need to pay close attention to the context under which the respondents are complaining about the proportion of the budget allocated to international experts, namely, as noted early, the fact that some international consultants may not be qualified, resulting in a low or limited transfer of technology and knowledge and the inefficient allocation of the limited project budget. In other words, if the quality of consultants reached a certain level, then the Vietnamese side may not regard them as a transaction cost.

In these situations, the donor side should take the following minimum measures. *Firstly*, it may be necessary to discuss what the partner agency actually requires from the donor in a way returning to the grant aid project starting point. As a result of these discussions, if the Vietnamese side only really requires financing to fill a financial resource gap, it may be necessary for the donor to re-think the provision of assistance to the recipient. If a donor continues to provide assistance to a partner agency in such a situation, aid dependency could result. *Secondly*, it is necessary to make efforts to improve the quality of consultants. As we showed above, the reason why such emphasis is placed on problems with consultants could be due to the fact that the Vietnamese side is not fully satisfied with the performance of donor consultants.

### **How should the recipient side be involved in project management?**

One important aspect in ensuring a national ownership at the implementation stage of a project is how and to what extent the recipient side should be involved in the project management.



**Case 37**

*A donor funded this project in order to conduct a study on urban transportation management in Hanoi and Ho Chi Minh City. As this project was conducted in both cities, two corresponding project offices were set up. Each office included a team of foreign consultants and a team of 5 to 6 Vietnamese experts and other administrative officers. A large proportion of the total project funds were used to operate these two offices. In addition, as the project was implemented in two cities and as two corresponding offices were set up, there were regular visits of experts between the two offices.*

**Case 38**

*A donor assisted a ministry to prepare a master plan study of a certain issue and sector in the North of Vietnam. This was the first study of its kind in this sector in Vietnam by the donor. Time and effort was therefore spent by both the project line agency and the counterpart agency in understanding the procedures and regulations on implementation of a donor granted aid project. An institute was assigned as the counterpart agency in coordination with an international consulting firm from the donor home country. The donor regulations required the Government of Vietnam to provide: office space, counterpart staff and transport at its own cost. The project and the donors requirements required a large amount of counterpart funds which the recipient agency had difficulty satisfying. Getting the approval for a limited level of counterpart funds for the study were extremely time consuming and were only approved after the project itself had been in operation for some time and was in the completion stages. This influenced the project and obstructed its operation and work, caused extra time and resulted in a number of extra costs.*

**Case 39**

*The donor side in this project expected the participation of high-ranking officials in meetings. Due to the busy schedule of these officials, the need for more than a months notice of meetings in advance and the lack of knowledge of the Vietnamese staff as to the schedule of these officials, it took a substantial amount of time to arrange meetings. The donor side also wished to have only the best people working for these projects but failed to pay any extra salary and as a result lost a number of experts from the Vietnamese side.*

**Case 40**

*In a sub- project of one project, a coordinating organization was selected with some strict conditions. These conditions included (i) the coordinating organization must be a government agency; (ii) the project coordinator must be the director of a department of the Ministry. Few people and organizations satisfied these requirements. Finally, a Deputy General Director was allowed to take the position. Unfortunately, the coordinator was so busy with his official duties he was unable to participate in the preparation and negotiation of project documents during the preparation phase. He was only given approved documents as the implementation phase started. This created substantial confusion and obstacle for himself and his staff.*

**Case 41**

*As in many projects, this project aimed at conducting a study in both Hanoi and Ho Chi Minh City. A ministry assigned its Institute as the counterpart agency in coordination with one department concerned and other functional organizations in Hanoi and Ho Chi Minh City along with an international consultant company, commissioned by the donor, to implement the project. The Donor required the establishment of a National Steering Committee comprising of high-ranking officials in the Ministry of Transport and the Cities' People's Committees. In addition, a steering committee and a task force were set up in each city to serve the project. Members of these groups were from the office of the people's committees. These committees and task forces worked only part-time as most of the members of these groups still retained their other positions and appointments. These groups only met when a number of problems arose. This was due to the fact the officers of the People's Committees were very busy with their civil work. Participating in these groups was considered an extra responsibility. These two committees and task forces operated quite inefficiently and it took a long time in making decisions.*

Most recipient agencies appear to be largely dissatisfied when donors request them to assign high-ranking government officials as counterpart personnel to projects. This is reported as one of the largest transaction costs in this report.

The logic for this requirement on the donor side is as follows: *Firstly*, it is natural for the responsible person on the Vietnamese side to participate in the project actively in order to ensure a national ownership. Fundamentally, the project does belong to the Vietnamese side, not to the donors. Without the direct involvement of the Vietnamese side, donor projects would just be filling in a human and financial resource gap that the partner agencies may be facing. *Secondly*, it is also natural that the responsible person directly involved in the project wants to achieve an effective transfer of knowledge & technology in terms of sustainability after the project completes. It means a strong commitment is a key element in accomplishing the project as planned. The provision of office space etc is also thought of as an important element of the Vietnamese side's participation by the donor.

However, according to the above cases, the recipient side often feels these are a heavy burden. The reasons for this are as follows: *Firstly*, high-ranking government officials are too busy to be responsible for the project in addition to their present work. *Secondly*, for staff on the Vietnamese side, motivation may be low as salary levels regulated by the government are generally low and additional salaries may still be outstanding. To compensate for this, the Vietnamese government tries to take the counterpart fund; the recipient side is not always able to supply these funds in a timely manner due to the complicated internal procedures within the government. The situation where a number of donor projects tend to concentrate on specific sectors and sub-sectors leads to a further deterioration of the situation. Consequently, quite a few counterpart personnel are frequently occupied. This is also the case in a number of small-scale projects resulting in a burden (transaction costs) that are the same regardless of the size of the

project.

In these situations, we can take the following measures. To avoid the situation where too many small-scale and stand-alone type projects are implemented, simplification and harmonization might be instrumental in reducing transaction costs. This approach is now being introduced by a group of donors in Vietnam as well elsewhere in the world. But even in these cases, the individual situations of each donor and its diversity of aid should not be lost.

Regarding the issue of allowances for counterpart personnel, we found a variety of views and opinions on the matter, as follows.

#### **Little financial incentive for counterpart personnel to join the project**

There are many examples of transaction costs relating to financial incentives for counterpart personnel on the Vietnamese side. The phrase “they work in the western way, and being paid in the Vietnamese way”, is very symbolic for this situation.

#### **Case 42**

*The project management function is often assigned to government officers in addition to their normal duties without any additional allowances or salary subsidies. Therefore, their work quality cannot be assured as they have to combine their governmental work with the project work and suffer time pressures. It is very difficult to ensure project officers deal with day-to-day or even urgent work when they are busy doing other work elsewhere. However, they cannot be blamed for this as it is an additional duty which they are unpaid for. For this reason action related to the project may often be taken late and sometimes forgotten. Their working styles and attitude may also remain bureaucratic, and passive. The donor should develop a new approach to this problem.*

In one case, there was a difference in salary levels between those hired by the donor side and those hired by the Vietnamese side, with dissatisfaction felt on the recipient side.

#### **Case 43**

*Another common point for most foreign funded projects in Vietnam is the pay for Vietnamese project managerial staff. In principle it is often agreed between the Vietnamese and foreign partners that the managerial staffs are to be paid by the Vietnamese side with the project not having to set aside any budget for this. In reality however the Vietnamese side has no other way but to appoint their own staff to work on a part-time basis on the project, taking care of the project management without any special financial commitment. The critical issue here is that they work in the “western way” and are being paid in the “Vietnamese way”. This has been pointed out many times despite the fact that it has been agreed upon beforehand under the project. The consequences of this can be very serious and can cause many additional heavy burdens. In particular, the lack of a special pay for project managers can have the following consequences: poor work attitudes and motivation, the inability to recruit capable staff,*

*and excuses for inaccurate financial accounting. It is time for international and Vietnamese partners to sit together and look at this issue seriously. It should also be noted that according to the Vietnamese salary scheme a senior expert has a salary of about US\$50 per month, while in Thailand a similar expert may earn US\$400-500 a month. The donor should review this problem as Vietnam can not afford to spend an additional budget to supplement the pay of those working for projects without touching the salaries of nearly 1.5 million other public servants. Saving a small amount when paying project staff will create the high risk of a low effectiveness, even a project's failure, causing unforeseen heavy financial burdens.*

In another case, the counterpart personnel were dissatisfied as they were unable to get an additional allowance for the over-time work relating to the project.

#### **Case 44**

*A project implementing group worked a lot of overtime, therefore they sometimes suffered from time pressures due to the simultaneous fulfillment pressures of both tasks assigned to manage their organization and the project.*

#### **Case 45**

*In this project, the Vietnamese staffs were not paid by the project including the Center's director. A university paid the Center's staff while other project staffs were directly hired by the donor. The donors appointed staff were highly paid and were able to hire Vietnamese assistants who were paid up to US\$200/month. Due to this the Center has to find ways to generate extra incomes for its staff by opening evening classes to make use of equipment and facilities.*

It is not easy to resolve these issues. The reason why the salary level of the Vietnamese counterpart personnel is low is likely to be linked with the progress of the on-going Public Administration Reform (PAR). The Vietnamese side should make efforts to improve this situation. Originally, most projects were requested by the Vietnamese, despite the fact that the recipient may be unable to implement a project and to do what is required of it at to the expected standard without further financial incentives from the donor side. This is also the situation where the Vietnamese side cannot arrange working conditions including office space to long-term international consultants. If the donor side wants to increase the motivation of the Vietnamese side by means of additional financial incentives, the donor may be able to motivate the Vietnamese side and raise the projects performance temporarily. However, this may also undermine the sustainability of the project. After projects complete and additional incentives are removed, a projects outcome may disappear due to the lack of financial incentives.

If we take into consideration the above, what a donor can do may be very limited. Primarily, the Vietnamese government needs to accelerate PAR, especially, salary reform, and to solve the motivation problem. As for the donor side, the following may be of assistance; *firstly*, it is necessary for the donor side to explain their philosophy on financial allowances to the Vietnamese side as early as possible in order to avoid unnecessary friction between both sides. *Secondly*, this issue may become overly

stressed when other factors are included, such as the over-presence of the donor, the poor quality of donor consultants, the poor performance of the project, and a lack of communication between donor consultants and the recipient side. If both sides could ensure better communication with each other, this kind of problem and complaint could be largely mitigated. Donors should do their best to comply with all of these elements.

### **Procurement; price rather than quality, and too great a centralized system of procurement at the donor headquarters**

In this study, we could not observe any complaints or transaction costs relating to procurement conditions, particularly tied and untied conditions. But, the view of one recipient shows one example of a transaction cost problem: the equipment procured under untied conditions failed to meet the quality expected by the Vietnamese side. Consequently, bidding and procurement were done again. One of the reasons for this was the failure to develop fully the initial tender documents. Another reason for dissatisfaction on the Vietnamese side was that they felt their opinion was not reflected in the tender documents. In these situations, it is necessary for donors to thoroughly develop tender documents with their partner agency.

#### **Case 46**

*In this project the bidding process was often done outside the country. Large numbers of bad quality and old goods were purchased from a particular country. This problem has been reported by the department concerned to the donor, the Ministry of Planning and Investment, the Ministry of Finance and the Ministry of Foreign Affairs. It was concluded that more than 60 items didn't meet the requirements set by the Ministry concerned. The returning of poor quality goods wasted a lot of time (more than 6 month) and manpower. Fortunately, after this, good quality goods were purchased with expenditures paid by the donor.*

### **Complicated procedures on the donor side: budget approval**

In the case of discussions of aid effectiveness, the poor capacity on the Vietnamese side is generally considered as a transaction cost. On the other hand, the Vietnamese side considers there is some room for improvement on the donor side to improve their logistics.

Our first case describes a project budget which was not provided by the donor side as planned. Occasionally, the donor side reduces the budget scale without any advance notice. When this happens, the plan of action of a project and the overall operational plan in itself are forced to change.

#### **Case 47**

*A donor's funds were not disbursed as agreed upon. Specifically, total committed funds were US\$ 1.5 million, while the disbursed funds were only US\$1.2 million.*

**Case 48**

*30% of the committed budget had been cut due to problems within the donor agency. The reduction decision was made solely by the donor without any discussion with the recipient as to the possibility of finding funding solutions from elsewhere. Consequently, many activities were lifted out of the project. An international expert, who was appreciated as being competent and having realistic understanding about Vietnam and how to do business in Vietnam, was moved. This lowered the effectiveness of the project.*

In one case, the project reduced its budget mid-year.

**Case 49**

*A donor decided to cut 20% of committed funds in the middle of the year when the yearly plan had already been agreed amongst the involved parties. This action created a number of unnecessary costs. The coordinating organization had to make another yearly plan to suit this new situation. A range of activities were ended and removed, causing significant effects on the project and its output. Unusually this project went into a second phase on completion of the first phase. This second phase aimed to accomplish the ideas arising in the first phase. In principle the donor had agreed to fund the second phase. International experts were mobilized to cooperate with the Vietnamese partner to prepare a proposal for the next phase. After submitting the project proposal, the donor rejected funds for this phase. The efforts of the Vietnamese staff and international experts became meaningless with them bearing all the costs arising during the writing process.*

In another similar case, because of complicated budget approval procedures on the donor side, it took around one to two months for the recipient side to receive approval from donor side after they submitted the annual budget plan to the donor.

**Case 50**

*In the case of a project funded by a donor, the preparation was completed by the donor themselves rather than the Vietnamese side. The donor provided the necessary construction materials, however, due to the annual accounting system of the donor, the project had to repeat the same strange procedures for eight continuous years. In particular, the project had to submit its annual implementation plan to its donor for approval. Normally half of the fiscal year was spent in the approval process, resulting in only six months to complete all the work which they had planned for the whole year. This created a number of time pressures. Another problem is the complicated accounting procedures of the donor. There were also differences in the donor's and Vietnamese financial system's requirements. But the main difficulty was the rigid and outdated regulations on prices, which did not reflect the current price of related activities. The donor's price list was sometimes lower than that found in Vietnam. Accounting has become more complex and time-consuming due to the unclear guidance and approval given to Vietnamese staff. In other words the Vietnamese partners would run into problems if they did not know how to create "delicate relations" with appropriate people. The negative aspects of the project began here. This had the*

*consequence of forcing the donor to change its own aid management; some Vietnamese staff had to be removed from the donors' field office. But the burden that was felt to the project had already happened.*

### **Case 51**

*Due to the dominance of a donor in developing limitations regarding fund disbursements, the Vietnamese partner had many difficulties in carrying out activities. With regards the disbursement plan, the first difficulty for the Vietnamese partner was approval for the yearly budget. Once the line ministry approved the yearly plan, the project staff had to submit to the donor office a yearly financial estimation and an accompanied disbursement plan. The donor would then review these documents and should then give approval in no more than 1 or 2 months. This extended the inactive time of the project within the year. The second difficulty was that, in many sub-projects, only 80% of funds were provided in advance with the remainder paid in full under completion of the project. Activities in poor areas that had not received advance payment faced many difficulties, and got into debt and found it hard to pay debtors (such as stipends, allowances, supplements for trainees etc). A third difficulty was that the donor changed their disbursement amounts within the fiscal year of 2001-2002 without any consensus between the donor and the Vietnamese side. These difficulties attributed to the low disbursement rate of the project.*

In these cases, most transaction costs were created by the donor due to the complicated donor procedures in budget planning. In each case, the planned budget was not sent by the donor side as planned, resulting in a delay in payment by the donor. It should be remembered that the donors had detailed before the project started the possibility that the budget situation could fluctuate in each fiscal year of the project. However to the recipient side it was seen as a donor caused delay and budget changes without advance notice were not appreciated by any recipient. As a result this was seen as a lack of accountability, transparency and predictability by the donor.

In these situations, we can surmise the followings. *Firstly*, it is necessary for the donor side to inform the recipient of any possibility of any changes in the future when they conclude a project agreement. *Secondly*, it is necessary for the donor side to simplify its relevant procedures in order to disburse budgets on schedule, and to ensure accountability, transparency and predictability. If there is to be a delay the donor should inform the recipient why the forward of funds are delayed and when the budget can be expected from the donor.

### **Changes in aid delivery mechanisms**

We also found a number of further examples of transaction costs related to budget disbursement, as follows.

### **Case 52**

*In 2000, a donor agreed to start a technical assistance project. This project was the extension of a previous project which was also granted by the same donor. However, the*

*donor had changed the transfer mechanisms of aid budget previously used under the first project. While in the previous project its budget was transferred directly to provincial authorities, in the second project Vietnamese central agencies received the aid which they then disbursed to the local authorities. Due to the distance between Hanoi and the central agencies and the provinces and the recipient agencies difficulties arose. Administrative procedures caused delays in disbursement causing a longer period to disburse funds than the first project.*

We do not know the individual reasons behind donors changing their delivery mechanisms, each donor has a differing reason for these changes. In this case, we can say the following; *firstly*, the donor should have explained the changes in their delivery method mechanisms to the Vietnamese side sufficiently in advance. *Secondly*, this situation took place in an atmosphere where an increasing number of projects had local agencies as counterparts. The donor may have had to explore a more realistic and simple transfer mechanisms for the project budget.

### **The lack of project management capacity**

Recipient agencies also recognized the inadequacy in their project management ability which also leads to transaction costs. The Ministry of Planning and Investment also underlined this issue in their initiative: “the Comprehensive Capacity Building for ODA Management” which will be launched in June 2003.

### **Case 53**

*The poor capacity of the Vietnamese staff in managing and implementing this project was an important factor in causing an unnecessary burden and costs to the project. As a result of poor project management, the donor threatened to terminate the project, after the second stage, when they realized there were unaccomplished project objectives. This strong action by the donor forced the Vietnamese side to review the whole process of project management and implementation. Reforms such as consolidating the project office, changing personnel, refining management and financial mechanisms, redesigning the project objectives etc helped to put the project back on track and now the project has started its third phase with confidence. Though the project implementation has been extended, the burdens and costs were substantial and are worth considering.*

One of the weaknesses of Vietnamese partners is the weak capacity of staff engaged in projects. Vietnamese staff usually claims that they do not have adequate English to communicate with international experts, resulting in misunderstandings between the Vietnamese partners and the donor. These misunderstandings can lead to a lengthened implementation process. In a number of projects, international experts required interpreters to communicate with local partners, leading to a drain on resources, reducing the budget for project activities. However, it should be noted that the English levels and skills of Vietnamese staff has improved greatly over the last few years. In addition, many Vietnamese staff do not have enough experience in managing and coordinating ODA projects, causing a range of problems during the implementation



stage. Some projects also claim that Vietnamese staff lack experience in preparing estimates, particularly a lack of capability to foresee problems that may arise. This results in consequent adjustments, amendments and reassessments that became costly in terms of both time and money.

In these situations, we can say the following. *Firstly*, conducting training courses on project management is one possibility as the MPI proposes in “Comprehensive Capacity Building for ODA Management”. However, short-term training courses are very limited, though they may be able to provide a basic and general knowledge of management to the recipient side. Therefore, *secondly*, it is necessary for the donor concerned to transfer their knowledge and experiences through the daily work of the project and aim to gradually assist in the development of counterpart personnel in mid and long run.

### **Insufficient decentralization from donor headquarters/regional offices to the field office**

As pointed out at the OECD-DAC Task Force on Donor Practices and also the report from the Like-minded Donor Group in Vietnam, the extent of transaction costs is likely to depend on the extent of decentralization from a donor’s headquarters to its field offices.

#### **Case 54**

*In 1998, a donor started a project aiming to formulate a development strategy for implementation in 4 provinces in Central Vietnam. A counterpart agency on the Vietnamese side was assigned as the consultant agency (the sub-contractor) in coordination with the donor country-based consultant company, to implement the project. As a requirement of the donor, the consulting firm had to inform the Donor of the progress of the project. In addition, when problems emerged, the consultant had to ask for agreement from the donor regarding the solutions devised to deal with these problems. Although a donor had a representative in Hanoi, this office only monitored projects but did not have the authorization to make project decisions. All monitoring and evaluation were carried out by the donors’ regional office based in a neighboring country. As this office was not located in Vietnam, they lacked the necessary understanding of the Vietnamese situation. In addition, they were unable to keep up with the emergence of specific problems which developed daily. This resulted in delays in making proper, suitable and timely decisions, which in turn, lead to implementation delays.*

#### **Case 55**

*One donor had developed a rigid set of regulations concerning its own ODA projects. Firstly, there was a controlled distribution of power between a donor mission in Vietnam and the donors headquarters in the home country. The donor mission in Vietnam seems only to have the power to bring consultants into Vietnam and nothing more, though some problems required action immediately. For example, the regulations concerning the purchase of equipment for the project allowed only the purchasing of goods originating from the donor country. As a result they were often unavailable within*

*Vietnam and when they were very expensive, causing the project to purchase them from other countries. The donor mission in Vietnam could not make the final decision on this and it had to ask permission from headquarters. This took a lot of time and effort. Furthermore, there were also many proposals from this project that were never answered by the headquarters.*

Decision-making in (some) donor agencies is centralized. Transaction costs arise from the burden of communication between different parts of a centralized donor structure.

1. Delays occur simply by having to relay information between the government, the local donor office, the regional office and then headquarters.
2. Some prospective projects - and time spent on developing them - may come to nothing, as decisions favored by local donor offices may not be shared by headquarters.
3. More centralized donors have less expertise and/or capacity available locally. Usually consultants prepare the project and present it to the donor first, but the donor may not have the expertise or time to reflect on a consultants' proposal and develop its own position before negotiating with the government. Hence, in negotiations the government and donor in effect discuss a third party document.

Specific local conditions and constraints are harder to take into account when donor decisions are taken outside the country, where staff may have less of an understanding of the national context and concerns. In these cases, it is necessary for donors to further decentralize their decision making and operations from their headquarters and regional offices to the field.

## **2. Aid modality**

### **Case 56: In-kind**

*In one case of a project funded by a donor, its objectives were to modernize facilities and equipment. After entering into the implementation stage, an international consultant in charge of project management came to Vietnam and was engaged in most of the logistic affairs imposed by the donor, such as procurement, financial management, auditing, monitoring and reporting. This involved close communication with the recipient. In this case, a project management unit was not established. The recipient had few transaction costs imposed by its donor and its implementation and construction work went smoothly. With regard to monitoring and reporting on project performance, the international consultant was directly in charge of project management, and kept in daily communication with the recipient. A donor could follow and understand the progress of the project through this international consultant, and did not need to request the recipient to frequently submit reports which were too detailed. As a result, the transaction cost here was not large.*

*In the case of one project whose objective was the transfer of technology and experience, a donor sent a project coordinator to be directly in charge of logistical affairs, that is, procurement, financial management, monitoring and reporting. This project coordinator*

*managed the project budget provided by the donor, and thus the recipient did not touch this. As for monitoring and reporting, daily communication ensured that the donor could follow the progress of the project and be aware of any problems as they arose. Consequently, the donor did not need to request the recipient to work out a detailed reporting format and the transaction costs were negligible.*

### **Case 57: In-cash**

*In another case of a project funded by a donor, firstly, the donor sent international consultants to the recipient, and next established a project management unit (PMU). The donor assigned a Co-Director, international and national consultants in charge of specific expertise areas, and administrative staff to the PMU. The main function of the PMU was to be in charge of the administrative affairs imposed by the donor, such as procurement (consultants and equipments, etc), financial management, auditing, monitoring and reporting. A huge transaction cost was incurred at this stage. In financial management, the donor provided the project budget in-cash. Thus, the recipient agency opened a bank account to receive it. In Vietnam, opening a bank account in itself is sometimes troublesome. Problems were felt operating the bank account, to draw out required money from the bank account, the recipient had to write a report clearly showing how the budget was to be spent, and then had to submit this to the PMU. Then the PMU checked its relevance before giving approval. After approval the money is disbursed. These many stages needed numerous authorizations and signatures and resulted in delays in disbursement. The recipient and donor also had a lot of trouble with the procedures for the procurement of consultants and equipment. Which procedures should PMU follow, the recipient's or the donor's procedures? There was also a lot of trouble involved in how to implement each of the projects activities. As a result, the disbursement of one part of this project is again delayed. As for reporting and monitoring, donors requested the PMU to submit detailed information quarterly. Consequently, transaction costs were created again. This sectoral ministry department expects donors to harmonize multiple procedures such as procurement, financial management, reporting and monitoring.*

It is difficult to generalize transaction costs in Vietnam. However, the implications here are very interesting. First, we can discern that one of the most crucial questions in discussing transaction costs in Vietnam is what and to what extent do donors expect the recipient to take the responsibility of logistic matters under their ownership and enhance national capacity? In other words, how do donors ensure ownership? In-cash or in-kind issues are closely linked with this question. Today, national ownership is widely accepted in the international donor community, and it can be classified in detail as follows:

- Aid delivery in accordance with the recipient government's policy;
- Project formulation stage in line with a sectoral action plan and the requests of the government for projects;
- Active involvement in project design and planning; and
- Active involvement at the implementation stage including procurement, financial management, monitoring and reporting.

Capacity building can also be classified twofold: (1) capacity building in the expertise field, and (2) capacity building in the field of project management such as procurement, financial management and auditing, monitoring and reporting. As can be found in Japanese ODA, Ideally the recipient agency is expected to achieve both aspects simultaneously. However in reality it does not take place because of weak capacity building and a limited number of counterpart personnel. If we found only Japanese aid being delivered to recipient agencies, we might expect them to do so under the ownership principles and enhanced capacity. However there are a great number of donors and International NGOs in Vietnam and it is not realistic for Japan to do this. As a result, Japan tries to absorb excessive transaction costs temporarily in order to create circumstances where counterpart personnel can devote themselves to their own work. In this case, most of the transaction costs incurred at the implementation stage are borne by the donor side.

However, where ODA is given in the form of in-cash aid, donors expect recipients to be involved in project management in a different way, one which focuses on the enhancement of ownership and national capacity. To ensure the sustainability of a project after completion, it is necessary to enhance capacity building in expertise and project management, the areas mentioned in the paragraph above. To this end, counterpart personnel should be directly in charge of procurement, financial management and auditing, monitoring and reporting. If the donor side controls these areas then the recipient will never be able to build a project management capacity and graduate from aid dependency. In practice, for the same reason as Japan, there are a number of donors who set up project management units and support the recipient's project management. PMU creation is highly appreciated by ministries as it reduces transaction costs and the pressures on counterpart personnel who are all too often too busy with daily work, and unable to allocate time for project management logistics. Although in-cash aid tends to increase the role of the recipient logistically, especially in project management, at the same time it also creates other burdens and difficulties in reporting the expenditure of the project budget. In this case, the transaction costs are relatively large. Most donors, except Japan and GTZ, fall into this group.

When comparing these two aid types, In-kind and In-cash, we might be able to say that in-cash aid tends to increase transaction costs in Vietnam. This issue is closely linked to aid philosophy because both approaches share some of the same principles of enhancing ownership and building a national capacity. The difference is the tools used, in-cash or in-kind. On top of this when other factors are added, for example counterpart personnel in charge of sub-sectors popular among donors and the multiple procedures in several donors, transaction costs rise. The scale of the transaction costs might vary depending on the type of aid, but even in small-scale projects, transaction costs are inevitable. The higher the number of in-cash projects, the heavier the transaction costs created. As for monitoring and reporting, where communication is less personal and reliant upon formal reporting techniques between recipients and donors this may increase transaction costs, for example, where too detailed and frequent reporting is required.

If we look at in-cash aid, we may not be able to say its transaction costs are unnecessary despite the heavier levels of costs, this is partly due to donors adopting approaches based on aid philosophy and partly as it has many advantages in other aspects. In addition, there are many cases where recipients highly appreciate a project performance, regardless of the scale of transaction costs. Recently, according to one ministry, a number of departments operating in sub-sectors popular amongst a variety of donors, using in-cash aid, are becoming interested in ODA harmonization and simplification and this new ODA modality in order to reduce their costs and burden. Therefore, the recent efforts initiated by the Like-minded Donor Group might be sufficiently justified in some specific occasions. However we also need to analyze the risk of a loss of aid diversity as stated in the OECD-DAC risk analysis paper.

Going back to the starting point of transaction costs, most recipients do not recognize the clear correlation between the scales of transaction costs and aid effectiveness and efficiency. They also do not recognize the correlation between the scales of transaction costs and other elements such as the project approach vs. program approach, and tied vs. untied and they never regard the PMU as a cause of transaction costs. Rather, PMU is seen as an effective framework to reduce transaction costs on the recipient side. The implication here is very important. The discussion around donor harmonization tends to seem very simple at the international level but in reality it is not. The scales of transaction costs are different depending on in-cash or in-kind and this depends on the aid philosophy of each donor. The most important issue is to what extent donors can adjust to the Vietnamese context. Regardless of the different approaches, donor practices without any flexibility (in other words, an approach ignoring the advantages of each aid philosophy and tool) might create transaction costs. In this sense, we appreciate the following statement by the United Kingdom at the 2002 CG meeting in that they accept flexibility and diversity among donors.

*“Sectoral approaches are generally seen as synonymous with budget support. The reality is that sectoral approaches are more of a process than an actual clearly defined aid instrument. Sectoral approaches can be financed in a variety of different ways including project, pooled and budgetary financing. The core element is an agreed strategic framework for the sector that guides the overall development effort”. (Source: The presentation by the United Kingdom at the last CG meeting in Hanoi 2002)*

## Chapter 6 Conclusion

### 1. Implications

Through this report, we could summarize that it is necessary for the Vietnamese government, ODA recipients and donors to understand following findings on transaction costs, and avoid easily creating any special or complicated new procedures.

- *First*, it is extremely difficult to measure transaction costs quantitatively, although it is often the starting point for discussions on aid effectiveness and efficiency. There seems to be no shared definition of transaction costs at an international level. In this study, we have set the definition of transaction costs as simply as possible, as we saw at the beginning of this report. Even if amount of transaction cost is equivalent, recipients consider it differently; some consider it as excessive and unnecessary, and others not. According to our research, the share of those who recognize the cost as un-ignorable accounts only for 10%, while the remainder does not think so.
- *Second*, Transaction costs caused by the Vietnamese side are often more serious than we have expected, while the donor community has mainly focused on the costs caused by themselves. Measures to be taken to confront these costs must be diversified, depending on their causes. Harmonization (including common formats of reporting and financial management) and the introduction of new modalities, such as sector-wide approaches (SWAP) and budget support, might be instrumental in reducing costs, where transaction costs are mainly created by donors or, where a great number of stand-alone projects are concentrated on a specific department. However, even in these cases, views of each donor must be respected and aid diversity has to be secured because they are what the Vietnamese government expects.

Donors' over-presence in pre-implementation and implementation stages may happen due to the weak capacity of the Vietnamese side. With this in mind it is necessary to clarify the needs of the Vietnamese side, to encourage the development of their capacity, and also to review the donors practice. As for the costs caused by donors, we should address the following points:

When most decision-makings are done in a donors' home country and not in Vietnam, it makes difficult, if not impossible, for Vietnamese side to work jointly with the donors' consultants. An excessive consultant-driven style at each stage of a project/programme cycle loses a chance for the recipients to reflect their views and opinions. As a result the Vietnamese side is passive in the process and is simply informed of important information, such as the recruitment of consultants and the change of delivery mechanisms. Meanwhile, internal complicated procedures on project appraisal, approval and

counterpart funding, which are regulated within the government system, might be extremely burdensome, compared with the transaction costs created by donors. There is a lack of transparency, accountability, and predictability (and participation) on both sides. Both sides have to keep in mind these elements in order to reduce excessive and unnecessary transaction costs. It also implies both sides should do a number of ordinary and basic things in a steady and uncomplicated manner.

- *Third*, we could not observe any clear linkage between the size of excessive and unnecessary transaction costs, and other factors discussed in the donor community, such as aid effectiveness, procurement conditions (tied vs. untied), and project-type aid vs. program-type aid. In every project mentioned in this report, even where transaction costs are incurred, these are not seen as a negative factor by the recipient side in terms of aid effectiveness and efficiency. Rather, many recipients and counterparts have shown a great appreciation for projects, when they are managed appropriately, despite the high level of transaction costs. The partner agency may put up with any level of transaction costs as long as the project produces the expected outcomes. This is one of the reasons that transaction costs are so difficult to assess. There might be some correlation between recognition of burden on transaction costs and outcomes of activities.
- *Fourth*, it is necessary for both sides to review the framework of grant aid, clarifying what the Vietnamese side expects of donors and their consultants in conducting grant aid projects. Various cases in this report have described a problem on motivation on the Vietnamese side. This problem was also addressed by the Vietnamese side at the mid-term consultative donor meeting in June 2003.

Considering a high proportion of consultant expenses in the total budget, it has to be clearly confirmed what the Vietnamese side really want from this aid programme/project. Is it enhancement of capacity through the technical cooperation, or something else? In relation to this, we would also like to address the incentive issue and the burdens they feel. From the viewpoint of donors, assigning high-ranking officials as counterpart personnel is very desirable for ensuring effectiveness and sustainability of a project, as mentioned in Cases 39 and 43 above. Meanwhile, from a Vietnamese viewpoint, Vietnam is a country with limited human resources, and donors interests and expectations are heavily concentrated on those limited skillful local experts. Without those skillful counterparts, how can projects be sustained in an efficient manner? It is needed to provide adequate incentives, such as knowledge gains, financial measures, and career promotion, in order to maintain the sustainability of project/programme. Another question that we have to address is what is the desirable division of labor between the Vietnamese side and the donors in order to encourage a self-help principle?

- *Fifth*, as for the introduction of sector-wide approaches (SWAP) in Vietnam in future, we have following observation:
  - ✓ It is important for the donor and the Vietnamese sides to share sectoral strategies at least, and national strategies, if we could. Then both sides would implement projects and programs in line with these strategies. It will further enable both sides to collaborate in monitoring at a sectoral level.
  - ✓ Even in the SWAP, diversity of aid modality should be ensured. Otherwise, harmonization may bear additional transaction costs. Each modality has an advantage and disadvantage respectively. Thus, to avoid misguidance in the future of development assistance and to keep encourage donors' will to assist Vietnam, it is essential to recognize diversity and to make full use of each advantage.

## 2. Future direction

In conclusion, we synthesize our findings and its measures to reduce transaction costs in the following pages, and then would like to provide a basis for the future discussion in the donor community in Vietnam. But, first and foremost, this report simply describes the findings of our study, and we should be prudent when putting into practice the findings. At least, we feel this report provides a level of convenient information for the MPI and donors to go forward in “Capacity Building for Aid Management”.



### Transaction costs and the basic directions to reduce them

#### 1. Pre-implementation stage

Type of transaction costs	Agencies creating transaction costs	Basic direction to reduce this type of transaction cost
Donor-driven project preparation	Donor side	<ul style="list-style-type: none"> <li>• Who works on the first draft of the project proposal?</li> <li>• To what extent are sufficient discussions ensured between the Vietnamese and the donor sides?</li> <li>• To what extent is actual work on the project design done in Vietnam?</li> <li>• To what extent can donor consultants adjust their time schedules in order to the work in a flexible manner in accordance with the realities of Vietnam?</li> </ul>
Quality of international consultants	Donor side	<ul style="list-style-type: none"> <li>• When donors recruit international consultants, it is necessary to work on a correct terms of reference (TOR). Based on the TOR, donors need to select the correct people as international consultants.</li> <li>• In the case where donors face difficulties in recruiting international consultants who have a satisfactory knowledge of Vietnam, they should place a higher priority on recruiting those who have strong expertise in each field (sometimes, donor consultants do not have enough knowledge not only on Vietnam and but also a specific field) according to the view of the recipient.</li> <li>• Donors should consider assigning field offices to take responsibility in selecting consulting firms in Vietnam.</li> </ul>

Long process to start projects from the donor side	Donor side	<ul style="list-style-type: none"> <li>• First of all, the Vietnamese counterpart agencies should work on realistic project proposals for submission to the donor.</li> <li>• The donor should as much as possible hire international consultants who have an adequate knowledge of Vietnam or a strong expertise in a specific field in order to avoid the wasting of time.</li> <li>• Donors should make efforts to ensure the transparency and accountability of the Vietnamese side so that counterpart personnel can grasp and understand the status of their project proposals.</li> </ul>
Insufficient project design	Donor side	<ul style="list-style-type: none"> <li>• Donors should not be hasty in carrying out project design. The ideal timeframe and the steps to be taken for project design are dependent on the scale of each project. At a minimum donor should select qualified consultants.</li> <li>• Donors should establish mechanism to get the requests and opinions of the Vietnamese side within the design process.</li> </ul>
Lack of project management ability	Vietnamese side	<ul style="list-style-type: none"> <li>• Training courses to build the capacity of Vietnamese counterpart personnel. This is to be done under the framework of “Capacity Building for Aid Management”, and should aim to provide more than a basic short-term improvement in general understanding, but should also introduce various experiences and lessons to the recipient side to enhance their risk management abilities.</li> <li>• Donors should make efforts to ensure day-to-day advice for the upgrading of management skills and the risk management skills. The impact of short-term training courses is limited, and day-to-day advice and on-the-job training is more</li> </ul>

		effective.
Complicated internal procedures: appraisal and approval	Vietnamese side	<ul style="list-style-type: none"> <li>The Vietnamese side should steadily ensure greater transparency and accountability. It is necessary to follow Decree No. 17 more closely and exactly.</li> <li>It is necessary to diagnose the actual situation of the internal processes of project appraisal and approval, and to present the direction measures should go to improve the situation. Decree No. 17 is supposed to enhance transparency and accountability, but it should be put into practice more often. Why is the Decree not implemented as initially expected before? Partly, it might be because the Decree was just issued without any accompanying changes, such as the simplification of procedures, thereby a heavy burden still exists in the form of excessive transaction costs. In this situation, the Decree may have to be revised based on the actual situation in order to function better. Or to assist this, other relevant government systems should be revised.</li> </ul>
Complicated internal procedures: counterpart funds	Vietnamese side	<ul style="list-style-type: none"> <li>Ditto</li> </ul>

## 2. Implementation stage

Type of transaction costs	Agencies creating transaction costs	Basic direction to reduce this type of transaction cost
Over-presence of donor	Donor side	<ul style="list-style-type: none"> <li>It is necessary to review whether there is a mechanism to share information and to reflect the views and opinions of the recipient. These mechanisms should be ensured not only as a formality, such as setting up a joint steering committee in the</li> </ul>

		project agreement but also substantively. It is also closely related to the extent that daily communications with the recipient side can be ensured
Quality of international consultants	Donor side	<ul style="list-style-type: none"> <li>• It is essential that work on terms of reference (TOR) for the recruitment of qualified consultants is done in consultation with the Vietnamese side. It is also necessary to incorporate their requests into these TORs. One qualification should be that, consultants should have enough knowledge on Vietnam or strong expertise in a target field.</li> <li>• It is necessary to ensure a sufficient period for donor consultants to stay in Vietnam so that they can grasp the real situation in Vietnam and discuss various issues with the recipient agency. In such a situation, the place that consultants do their actual work is of great importance and should be taken into consideration.</li> <li>• Donors should consider assigning field offices to take the responsibility for selecting consulting firms in Vietnam.</li> </ul>
High proportion of the total budget for hiring international consultants	Vietnamese and donor side	<ul style="list-style-type: none"> <li>• It is necessary to discuss the following issues, going back to the starting point: what is the significance of grant aid? What does the Vietnamese side really want from the donor?</li> <li>• It is necessary to further improve the quality of international consultants to avoid a criticism of consultant costs from the recipient side</li> </ul>
How should the recipient side be involved in the project management?	Vietnamese and donor sides	<ul style="list-style-type: none"> <li>• It is necessary to discuss why and what way those responsible are expected to be involved in the implementation with donors.</li> <li>• In the situation where there are a great number of stand-alone</li> </ul>

		<p>projects in a specific sector, it might be instrumental for the donor side to introduce a harmonization of procedures in the financial management and reporting, and to implement technical assistance projects collectively through a number of donors. Although a group of donors have experimented with this approach elsewhere in the world, diversity of aid modality should not be impeded.</p>
<p>Little financial incentive for counterpart personnel to join the project</p>	<p>Vietnamese side</p>	<ul style="list-style-type: none"> <li>• Fundamentally, it is necessary to discuss the rationale of any allowances with the Vietnamese counterpart personnel, and to accelerate the Salary Reform of the Public Administration Reform (PAR).</li> <li>• It is necessary for the donor side to explain their policy towards this at the beginning of the project.</li> <li>• This transaction cost becomes obvious considering several factors such as over-presence of donors and the poor quality of donor consultants, poor performance of projects and poor communication between the donor side and the Vietnamese side. Thus, the donor side should make efforts to ensure these levels.</li> </ul>
<p>Procurement; (price rather than quality) and too greater centralized system of procurement at the donor headquarters</p>	<p>Donor side</p>	<ul style="list-style-type: none"> <li>• It is necessary to sufficiently work on the specifications for equipment jointly with the recipient side, and to develop tender documents. Then procurements should be carried out.</li> <li>• It is necessary to further decentralize the decision making of procurement from donor headquarters to the field. Some donors have to get approval from their headquarters or regional office each time. This should be dependent on the estimated budget of its procured equipments.</li> </ul>

Complicated procedures on the donor side: budget approval	Donor side	<ul style="list-style-type: none"> <li>• It is necessary to improve internal procedures (simplification etc) on the donor side.</li> <li>• Besides this, it is also necessary to ensure transparency, accountability, predictability of its procedure. In the case of a delay of disbursement, the donor should explain why there is a delay and when the budget will be disbursed.</li> </ul>
Changes in aid delivery mechanisms	Donor side	<ul style="list-style-type: none"> <li>• It is necessary to explain the possibility of this in advance.</li> <li>• If the donor side changes its transfer mechanisms in accordance with decentralization (as detailed in this report), it should be established more realistically, considering local capacity.</li> </ul>
Lack of project management capacity	Donor side	<ul style="list-style-type: none"> <li>• Conducting training courses on project management under the framework of “Capacity Building for Aid Management” is one of the approaches.</li> <li>• It is necessary for donors to take the responsibility to transfer knowledge and experiences of aid management through day-to-day consultation &amp; advice.</li> </ul>
Decentralization from donor headquarters/regional office to the field office	Donor side	<ul style="list-style-type: none"> <li>• It is necessary to promote decentralization from donor headquarters (or regional office) to the field office.</li> </ul>

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