



Unravelling Tied Aid

Why aid must never be tied to donor country companies at the expense of women and men living in poverty.

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Summary

Tied aid – aid that can only be used to buy goods or services from the country providing the aid – puts donors’ commercial priorities before the priorities of women and men living in poverty.

In general, tied aid costs more than untied aid. Tied aid is thought to increase costs by 15-30% for many goods and services - more still in the case of food aid. Not only are the costs of tied aid higher; the quality of goods and services can often be lower, because they are less well suited to local contexts and preferences (Section 2.1). So on average every dollar of tied aid goes less far than a dollar of untied aid, robbing people in poverty of essential goods and services that would have been perfectly affordable if the aid was spent a different way.

Tied aid also holds back the long-term development of communities in the South, depriving them of the chance to make their own purchasing decisions that fit their own priorities. Specifically, tying aid means foreclosing the possibility of procuring locally – even though local procurement has the potential to create a ‘double dividend’: not only delivering project results, but also building up a stronger local economy for the future (Section 2.2).

Yet despite donor agreements on untying, tied aid continues to make up a significant share of bilateral aid - a share that is likely to grow further unless current commercial and political pressures are resisted (Section 1).

Donors must:

- Commit to untie all aid to all countries
- Use local procurement systems as the default option

- Remove the barriers that prevent Southern firms winning contracts
- Presume in favour of local, pro-poor, procurement

Section 1: tied aid – significant, opaque, and set to increase

Tied aid – aid given on the condition that the recipient use it to buy goods or services from the donor countryⁱ – still accounts for a significant share of bilateral aid (Figure 1). This is despite the fact that development actors have been committing to untie aid for the last decade and a half, starting with a recommendation from the Organisation for Economic Cooperation and Development Development Assistance Committee (OECD DAC) in 2001, and reinforced by successive development effectiveness and UN financing for development agreements.¹

In 2015, 16.5% of aid within the scope of the DAC’s recommendation was still tied – almost 5 billion US dollars.ⁱⁱ But this headline masks the true level of tying, for two reasons.ⁱⁱⁱ First, the large majority of bilateral aid falls **outside** the scope of the DAC’s recommendation,^{iv} and – though harder to quantify

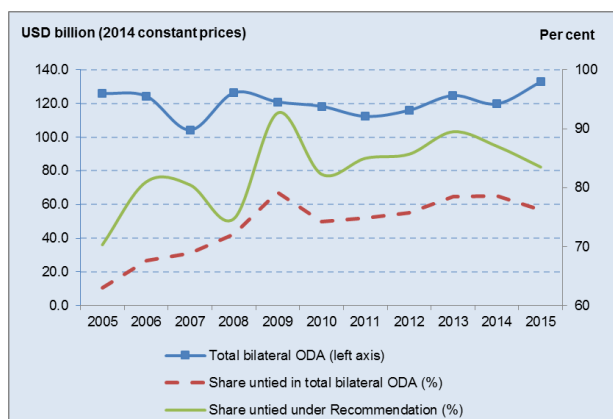
ⁱ For the avoidance of doubt, this note deals solely with tying in the sense of linking aid to the purchase of donor country goods or services.
ⁱⁱ The scale of tied aid varies substantially from donor to donor. Of the 50 largest tied aid projects recorded on the OECD DAC CRS system in 2015, 30 were United States projects, and 11 were Japanese.

ⁱⁱⁱ In addition to the factors outlined here, a further significant source of tied aid is South-South cooperation, but that would require a separate briefing.

^{iv} The recommendation excludes free-standing technical cooperation, and leaves it to Members’ discretion whether they will untie food aid. In addition, the recommendation only covers aid to Least Developed Countries and Heavily Indebted Poor Countries.

precisely – the levels of tying in this aid are thought to be higher (Figure 1).^v

Figure 1. Total bilateral ODA commitments and shares untied



Source: reproduced from the OECD DCD / DAC 2017 Report on the DAC Untying Recommendation

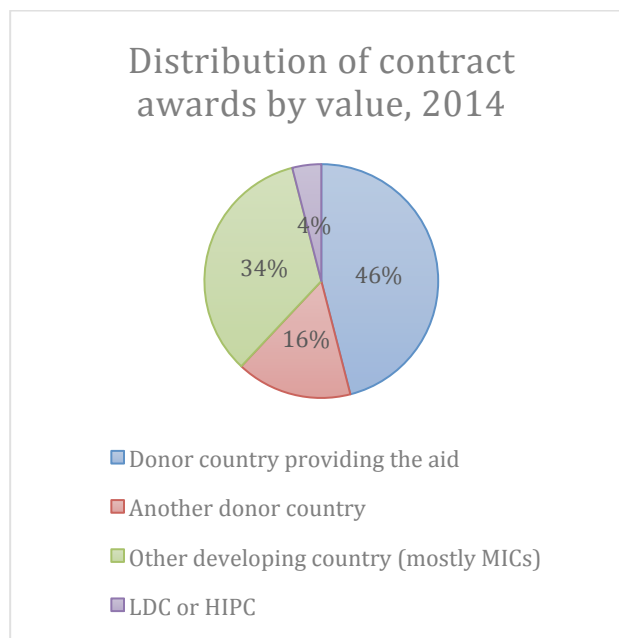
Second, and more importantly, **even if aid is reported as untied in principle, it may still be tied in practice**, through informal barriers that prevent firms outside the donor country from competing. Such barriers may include, for example, only advertising the tender in the donor country’s language, or setting very specific eligibility criteria that only a handful of firms can fulfill.

It is impossible to quantify exactly how much aid is tied in practice, but existing data confirm that domestic firms in donor countries are the biggest beneficiaries of donors’ aid contracts. In 2014, donors reported to the OECD on some 15 billion US dollars’ worth of individual aid contracts within the scope of the DAC recommendation on untying: 46% of this value was awarded to firms in the donor country (Figure 2).³ In certain donor countries the share of contract spending with domestic firms was higher still, even in countries reporting very low levels of tying in principle: Canada reported 100% of its aid as untied, yet 95% of aid contract spending by value went to Canadian firms.⁴

Finally, all DAC data and headline figures on tied aid exclude administrative costs and in-donor refugee costs, which are tied by nature and cannot be untied.

^v Indicative data is included in the OECD DCD / DAC 2017 Report on the DAC Untying Recommendation, but it is not certain how reliably donors report on tying status outside the Recommendation’s scope.

Figure 2. Distribution of contract awards by value, 2014



Source: Eurodad analysis of the OECD DCD / DAC 2017 Report on the DAC Untying Recommendation, Table 5

Notes:

1. This chart is based on data in the OECD DAC Contract Award database. However, not all donors report all relevant contracts in the database, even though this is stipulated by the Untying Recommendation
2. LDC = Least Developed Country; HIPC = Heavily Indebted Poor Country; MIC = Middle Income Country

Recent developments hint that an expansion in tied aid may be looming. Donors are currently elaborating new rules that would allow greater use of aid to finance private sector companies. In principle, there is no reason why such use of aid could not be fully untied – indeed, untying is essential to the stated objectives of the private sector agenda, which include supporting local private sector development and, ultimately, accelerating progress towards the Sustainable Development Goals. But in practice **the complexity of the new rules creates a risk that donors could conceal tied transactions**, and a coalition of civil society organisations has repeatedly raised concerns that the rules do not do enough to mitigate this risk.⁵ In addition, new nationalist governments in certain major donor countries are seeking new ways to make aid



work in their (narrowly defined) national interest: for example there has already been controversy in the United States over proposals to tie more food aid.⁶

These trends make it all the more urgent to revisit the arguments why tied aid works against the interests of people in poverty, and to set out the key steps that donors can take to end tying for good.

Section 2: why tied aid fails women and men living in poverty

Tied aid is a bad deal for women and men living in poverty - in the short and long term alike.

2.1: in the short term: restraining development results

In general, tied aid costs more than untied aid. A literature review commissioned by the OECD found that tied aid is likely to increase costs by 15-30% for many goods and services, and more still in the case of food aid.⁷ So **on average every dollar of tied aid goes less far than a dollar of untied aid**, jeopardising critical development outcomes. Among the largest tied aid projects in 2015 were a large number of HIV / AIDS interventions, as well as a major ebola control project – both of these are domains in which sub-optimal value for money would cost lives.⁸

Not only are the costs of tied aid higher; **the quality of goods and services can often be lower, because they are less well suited to local contexts and preferences.** For example, technology purchased through tied aid may be incompatible with local maintenance facilities, leading to rapid obsolescence.⁹ Similarly, tied food aid risks failing to allow for local nutritional and social requirements: there have even been cases where genetically modified food aid was imposed on countries that had strong policies against genetic modification.¹⁰

In the case of food aid, tying can also delay the arrival of aid, due to shipping times – making delivery some 13 weeks slower than local procurement, according to one study.¹¹ And – although this has so far received less attention in the literature – tied aid is sometimes likely to have a larger carbon footprint than many other procurement options.

2.2. In the long term: tying the hands of Southern actors

Tied aid is less effective in the long run, because it misses the opportunity to support Southern economies and Southern ownership of development priorities.

Impact for local economies

Only 4% of the 15 billion dollars' worth of aid contract awards reported to the DAC in 2014 went to suppliers in the poorest countries.^{vi}


This is a serious missed opportunity. **If aid is spent locally, each dollar can have a “double dividend”¹²** – not only delivering results for a project, but also creating income and jobs for local suppliers. Such income can in turn be spent with other local businesses, or paid in local taxes, potentially creating a virtuous circle of economic growth.^{vii} What is more, aid spent locally can, in the right circumstances, help more sustainable local value chains to develop, by providing a predictable source of income that encourages suppliers to build their capacities. In fields such as food security and pharmaceuticals, fostering sustainable local production can potentially have life-saving impacts.¹³ When combined with other interventions that tackle entry barriers, local procurement can also be used as a tool to enhance access to markets for marginalised producers, for example women smallholders¹⁴ who would otherwise face unequal opportunities due to gender discrimination in access to land, credit, and productive input.¹⁵

To be sure, the impact of local procurement depends on the context, and there are risks as well as opportunities.^{viii} But so long as aid is tied, either in principle or in practice, the option of supporting local

^{vi} I.e. in Least Developed Countries and Heavily Indebted Poor Countries – source, OECD DCD / DAC Report on the DAC Untying Recommendation, Table 5 (contract awards within the scope of the recommendation), analysis by value.

^{vii} This effect has been analysed in detail in Afghanistan by the Peace Dividend Trust ('Spending the development dollar twice: the local economic impact of procurement in Afghanistan', 2009)

^{viii} Including both social / environmental risks (e.g. if local companies do not meet basic environmental standards), and economic risks (e.g. inflation in some contexts – see Peace Dividend Trust, 'A methodology for assessing the impact of local hiring and local procurement by development partners', 2011)



suppliers is ruled out, before its potential benefits have even been properly considered.

Impact for local ownership

Tied aid undermines the development effectiveness principle that development priorities must be owned by Southern countries, as it takes purchasing decisions away from countries in the South, and puts them into the hands of donors. Procurement should be an opportunity to channel development funds through local systems, increasing accountability to citizens and ultimately making the system more robust and transparent.^{ix} But instead tied aid creates cumbersome parallel procedures that are beyond the scrutiny of local people.¹⁶

A knotty issue: trade-offs

In many cases, considerations of cost; quality; timeliness; long-term economic development and local ownership will all point in favour of procuring through local systems and local suppliers, rather than using parallel processes and selecting a supplier in the donor country. But trade-offs will inevitably arise. For example, donors may sometimes need to accept some extra costs in order to support local suppliers: the UN High Commission for Refugees has a guideline that purchases should be made locally provided that the extra cost does not exceed 15%¹⁷, and the World Bank allows a margin of 7.5 – 15% to favour local suppliers in competitive bidding¹⁸ (although this operates imperfectly in practice).¹⁹

The need for trade-offs, though, is no reason for aid to be tied. On the contrary, the delicate nature of these trade-offs is all the more reason why procurement decisions should be evidence-based and transparent, not pre-judged by loyalty to a handful of suppliers with large legal and lobbying budgets.

The tangled logic of 'national self-interest'

Section 1 of this paper observed that, in some countries, arguments for tying as a means to serve the 'national interest' were becoming increasingly prominent.

Those who make this argument are in effect saying that the interests - if not the lives - of people living in poverty should be subordinated to the interests of the Northern private sector, precisely when allocating the one scarce resource explicitly intended to put Southern interests first. This argument should need no rebuttal.

But it happens that this idea is not only unjust – it is also out of touch with the evidence. A literature review commissioned by the OECD in 2009 found that, based on the limited available evidence, “the macroeconomic impact [of tying for donors] is found to be fairly limited”.²⁰ A 2014 academic report went further, and concluded that “While some econometric studies have shown a positive correlation between aid flows and donor exports, ... the vast majority of scholars have concluded that tied aid does not generate significant trade benefits to donors, not least because it accounts only for a small percentage of their exports”²¹. In other words, even if, contrary to all the OECD DAC’s most fundamental principles, the ultimate goal of aid was the development of **donor** – not recipient – countries’ economies, tying would be an ineffective way to get there.

The Way Forward

The recommendations below set out key steps towards ending tied aid and ensuring that procurement delivers on the priorities of women and men living in poverty.^x

A note on the targets for these recommendations

Ensuring that procurement delivers on its potential to reduce poverty and realise human rights will ultimately depend on the actions of Southern actors – governments, parliaments, and civil society – in strengthening procurement systems and aligning them to their own development priorities. But the injustice of tied aid is precisely that it deprives Southern actors of

^{ix} This reasoning has much in common with the arguments advanced in favour of budget support as an aid modality (e.g. UK Aid Network, 'Budget Support', <http://www.ukan.org.uk/aid-quality/budget-support/> [accessed 7 September 2017])

^x The recommendations draw closely on those made in Ellmers, "How To Spend It"



the autonomy to do this without the interference of donor country interests. For that reason, and in line with Eurodad’s comparative advantage as a Northern-based network, the recommendations below are addressed to bilateral agencies, multilateral bodies, international civil society organisations and other key stakeholders in aid procurement from the global North.

1. Commit to untie all aid to all countries

The OECD DAC should revise the aid rules, to say that **tied aid cannot count fully as Official Development Assistance**, since by its very nature, its main objective is not to ‘promote the economic development and welfare of developing countries’.^{xi 22}

Pending action by the DAC, donors should **untie all their aid to all countries and all sectors**: whether through prime contracts, through sub contracts, or – if proposed changes to the aid rules are agreed – through imports and investments enabled by the new private sector aid instruments.

2. Use local procurement systems as the default option

Donors – both bilateral and multilateral – **should channel aid through the procurement systems of the recipient country**. They should only use alternative procurement methods where, in the assessment of citizens of the recipient country, there is a compelling – human rights, environmental, or development effectiveness^{xii} - reason to do so.

3. Remove the barriers that prevent Southern firms winning contracts

If donors are unable to use country systems, and retain direct responsibility for procurement themselves, they should **ensure that barriers for Southern bidders are**

removed, throughout the delivery chain.^{xiii} Known barriers include inaccessible information, unnecessary size and complexity, asymmetries in access to support networks such as embassies, and a tendency towards risk aversion among procurement officers.²³

The OECD DAC should require donors to **report on the geographic distribution of contract awards for all bilateral aid spending**, including prime contracts and sub-contracts, and to provide a written explanation whenever contracts are awarded to firms in the donor country.^{xiv}

The Global Partnership for Effective Development Cooperation should carry out **more research on how best to remove barriers for Southern firms**, including the extent to which different aid modalities are conducive to untying in theory and in practice.^{xv}

4. Support local, pro-poor, procurement

Procurement can be a powerful tool to support local industry, to create decent work (e.g. through labour intensive methods) and to reduce inequalities (e.g. through support to women-owned enterprises). The pros and cons of these approaches are best decided at national level. But where no clear national policy on pro-poor procurement exists, donors should **presume in favour of buying local, buying from suppliers that create decent work, and buying in ways that reduce inequalities.**^{xvi}

Donors should **complement pro-poor procurement with other locally led interventions to build local market capacity** – for example, training local employers in labour rights, or supporting economic empowerment programmes for women entrepreneurs.

^{xi} This argument was previously made by Ellmers in “How to Spend It”

^{xii} For example, if the procurement does not safeguard against infrastructure procurements that would cause damage to protected habitats, if it does not specify that procured goods and services must meet standards on accessibility for persons with disabilities, or if it does not basic thresholds for transparency and accountability

^{xiii} This includes procurements undertaken by private sector contractors, civil society organisations, or companies financed through the proposed new private sector aid instruments.

^{xiv} Similar transparency provisions will be required if the proposal to include private sector instruments within ODA is agreed.

^{xv} For example, pooled funds are less likely to be associated with tying (Geddes, Clay, and Natali, “Untying aid: is it working?”)

^{xvi} Without prejudice to the basic requirement that procurement should comply with human rights or environmental obligations.



End notes

¹ “The Paris Declaration on Aid Effectiveness”, “Busan Partnership for Effective Development Cooperation”, “Monterrey Consensus on Financing for Development”, “Addis Ababa Action Agenda of the Third International Conference on Financing for Development”

² Organisation for Economic Co-operation and Development Development Cooperation Directorate / Development Assistance Committee, “2017 Report on the DAC Untying Recommendation.” 2016 prices.

³ Ibid. Analysis by value.

⁴ Ibid. Percentages relate to aid within the scope of the DAC recommendation.

⁵ See for example our March 2017 position paper, “CSO Recommendations on the PSI Reform.”

⁶ Wroughton and Zengerle, “Exclusive: White House Weighs Tightening U.S Food Aid Shipping Rules - Sources.” Reuters, “Trump Drops Plan to Change How Food Aid Shipped.”

⁷ Clay, Geddes, and Natali, “Untying Aid: Is It Working?”

⁸ Source: analysis of the OECD DAC Creditor Reporting System database

⁹ Carbone, “Much Ado about Nothing? The European Union and the Global Politics of Untying Aid.”

¹⁰ La Chimia, *Tied Aid and Development Aid Procurement in the Framework of EU and WTO Law*. Page 70.

¹¹ Lentz, Barrett, and Gómez, “The Impacts of Local and Regional Procurement of US Food Aid: Learning Alliance Synthesis Report.”

¹² Ellmers, “How to Spend It: Smart Procurement for More Effective Aid.”

¹³ La Chimia, *Tied Aid and Development Aid Procurement in the Framework of EU and WTO Law*. Ellmers, “How to Spend it: Smart Procurement for More Effective Aid”. GIZ /East African Community / UNCTAD, “Policy Coherence for Local Production of Pharmaceutical Products”.

¹⁴ Ellmers, “How to Spend It: Smart Procurement for More Effective Aid.”

¹⁵ Gender and Development Network, Gender Action for Peace and Security, and UK SRHR Network, “Turning Promises into Progress: Gender Equality and Rights for Women and Girls - Lessons Learnt and Actions Needed.”

¹⁶ Ellmers, “How to Spend It: Smart Procurement for More Effective Aid.”

¹⁷ “Sourcing from Local Suppliers - UNHCR|Emergency Handbook.”

¹⁸ World Bank, “Procurement Regulations for IPF Borrowers.”

¹⁹ Ellmers, “How to Spend It: Smart Procurement for More Effective Aid.”

²⁰ Clay, Geddes, and Natali, “Untying Aid: Is It Working?”

²¹ Carbone, “Much Ado about Nothing? The European Union and the Global Politics of Untying Aid.”

²² Organisation for Economic Co-operation and Development Development Assistance Committee, “Is It ODA?”

²³ Ellmers, “How to Spend It: Smart Procurement for More Effective Aid.”



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