

The Reputation Trap of NGO Accountability*

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Abstract

The management of nongovernmental organizations (NGOs) has emerged as an important problem in recent years. Much of the discussion about NGO management has centered around the need for accountability. We demonstrate that the tools typically used by donors to improve NGO accountability, namely reporting and shorter funding cycles, can trigger unintended consequences. Our analysis shows that demonstrating attribution within the constraints of a short funding cycle can become so important to the survival of the NGO that it interferes with the long-term policy goals of the organization. The resulting short-term NGO behavior is often misconstrued as incompetence, but it is actually motivated by the structural constraints of the relationship with donors. Whenever an NGO has to choose between actions that generate attributable outcomes versus actions that will not lead to attribution, the NGO is likely to choose the former, even when the latter choice would have a more durable policy impact. We illustrate this strategic dynamic with a focus on two types of NGO activity: water improvement and international crisis mediation.

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Nongovernmental organizations (NGOs) play an ever increasing role in addressing contemporary global political issues. NGOs have influenced peace processes, helped to ameliorate water crises, poverty, and improved the welfare of millions. As these accomplishments accrue, the ambitions and hopes of what can be accomplished have increased accordingly. Despite this impact, however, NGOs do not always produce durable policy outcomes. We often observe NGOs producing what appear to be small, temporary, and perhaps even counterproductive accomplishments. Environmental NGOs, for example, may organize multi-party talks that produce non-binding agreements with much fanfare, only to see the agreements unravel almost as quickly as they are produced. Similarly, water NGOs may find themselves counting on temporary solutions as they struggle to gather enough resources to tackle their long-term goals of sanitation, water quality, and access. Short-term outcomes such as these can often appear to be at odds with the long-term normative aspirations typically attributed to NGOs. Why do we observe these competent, altruistic organizations settle for non-durable outcomes?

Three types of explanations for this phenomena are plausible. First, conventional wisdom often rests on the idea that NGOs and the people who run them are more concerned with ideals than competence.¹ These explanations typically lack evidence, however, and are unsatisfying because they do not account for why an idealistic organization would divert its attention away from achieving long-term accomplishments. A second class of explanations involves structural constraints imposed by host governments. That is, NGOs can only accomplish what is allowed by the states within which they work. While this is an important line of reasoning, we proceed here with the assumption that such constraints are endogenized within the goals of the NGO.² Thus, one still must account for the incongruence between goals and outcomes. A third type of explanation, which we pursue here, focuses on the strategic behavior of NGOs and their donors. One might be tempted to dismiss strategic behavior when studying NGOs due to their altruistic nature, but the two qualities are not incompatible. NGOs are motivated by normative concerns, but these organizations are also driven by strategic interests,³ and these strategic interests can have a significant influence on the

¹The argument boils down to some variant of “this is a mission, not a business.” The same argument often applies to the management of universities. We would argue that the model we develop here is relevant to managing academia as well.

²In future research, we hope to relax this assumption to study the problem of private information and uncertainty in the host state. We suspect that this can be a problem primarily for NGOs who are new to a host, or new to their business.

³Cooley and Ron 2002; Finnemore and Sikkink 1998.

behavior of NGOs.⁴ In this research, we examine how one such strategic motivation—the pursuit and maintenance of a reputation visible to donors—can help to explain the seemingly myopic behavior of the NGOs we describe above.

Our argument in a nutshell is as follows. NGOs need donors to survive, and donors need NGOs to implement shared policy goals. Donors want to enable NGO success, of course, but they are also concerned with the quality of their investments. Since donors are often uncertain about the quality of individual NGOs, donors would like guarantees that their scarce resources are being distributed to competent and effective organizations. In search of investment confidence, donors target their funding to NGOs with a demonstrated ability to achieve tangible policy successes. Thus, to attract funding, NGOs have an incentive to focus their efforts on achieving immediate policy accomplishments that are easily attributable to the NGO. Herein lies the reputation trap.

While rewarding NGOs that achieve policy successes can help donors make sure that they are funding competent organizations, this strategy potentially creates a new problem. While in some policy arenas, the type of accomplishments that NGOs can achieve in the short term are consistent with their long-term goals, oftentimes they are not. In the latter cases, a myopic focus on small goals that are quickly and visibly accomplished can potentially divert an NGO’s attention away from its central mission. What appears from the outside as incompetence is actually the opposite. Acting rationally, high-quality NGOs find themselves in what we term a “reputation trap.” To survive financially, NGOs become frustratingly hobbled by their continuous need to produce tangible results in order to maintain their reputations. By requiring NGOs to provide such signals of their quality, donors do not aim to impede durable policy successes. Rather, they simply wish to maximize the potency of their resources by only funding competent and effective organizations. Calls for transparency and accountability, long the hallmark of reform calls for NGOs, will not address these problems. Only by changing the structure of the NGO-donor relationship will these actors be able to escape the reputation trap and focus a greater proportion of their efforts to durable policy success.

We illustrate this strategic dynamic with a focus on two types of NGO activities: water improvement and international crisis mediation. Clean water access improvement remains one of the most important and difficult tasks for development, and the goal has received tremendous atten-

⁴See e.g. Bob 2005; Gugerty 2009; Kelley 2009; Reinhardt 2009; Sell and Prakash 2004.

tion and funding over the last three decades. Many NGOs focused on water improvement, however, have found themselves in a reputation trap. Given their need for reporting quantifiable results to donors, water NGOs tend to pursue strategies that are conducive to reporting attributable successes that are observable within one funding cycle. In many cases, the need for attributable outcomes generates a focus on activities that do not lead to durable improvement to water access. Similarly, conflict mediation has emerged as a key priority in the post-Cold War era. The mediation efforts of the Centre for Humanitarian Dialogue (HDC) in Aceh, Indonesia, illustrate the importance of reputation early in the existence of an NGO and the structural pressure on the NGO to identify and report tangible accomplishments. HDC's progress in mediating the conflict in Aceh was highly publicized, and remains today a part of HDC's pitch as a high-quality organization, but the agreements reached with HDC's help did not produce durable policy outcomes. This focus on attribution makes sense when viewed in the context of financial survival, but it can undermine efforts to achieve the long-term goals of improved water access or conflict resolution. Together, these cases illustrate that the need for immediate, attributable successes leads NGOs to get caught choosing between a reputation for high quality and the pursuit of their long-term objectives.

In the next section, we review research that examines the well known problems of accountability and market forces within a principal-agent framework, as well as the side effects of implementing solutions to these problems. Building off of the platform established by Cooley and Ron⁵, we then model the repeated interaction between donors and NGOs to focus on the strategic interaction that emerges from the uncertainty problems motivating accountability efforts. Our theoretical analysis suggests that because the private information problems surrounding the capabilities of NGOs, these organizations follow a strategy of reputation development in an attempt to convince donors that they are a worthy investment. NGOs focus on providing attributable evidence of success within the reporting cycle tied to funding decisions. When that focus on producing attribution becomes incongruent with the long-term goals of the NGO, it results in a reputation trap.

⁵Cooley and Ron 2002.

Accountability and Attribution: Sources of Strategic Constraint

We begin our discussion with the assertion that NGOs have, and pursue, strategic interests. Some scholars have discussed the normative values, goals, and agendas pursued by NGOs.⁶ Cooley and Ron summarize this scholarship as “largely optimistic, suggesting they [NGOs] herald an emerging global civil society,” one that rests upon “shared liberal norms and values that motivate INGO action and explain their supposedly benign influence on international relations.”⁷ While we agree that NGOs do indeed follow certain normative agendas and uphold certain “moral character,” the organizations are not immune from strategic behavior.⁸ In particular, the continual need for funding sources forces NGOs to make decisions based upon donor expectations and demands.⁹ This dependency allows donors to constrain NGO actions. For example, Kelley¹⁰ finds that donors place political constraints on NGO election monitors, encouraging the NGOs to be more lenient on countries that receive greater foreign aid. Bütthe, Major, and Souza¹¹ find, however, that NGOs are sometimes able to overcome strategic constraints and respond to the humanitarian needs of their constituencies. The question then is when, and why, are NGOs constrained? In what follows, we review the works that focus on the strategic incentives of NGOs and place specific focus on the effects strategic incentives have on the behavior of NGOs.

While most NGOs are not profit-driven, they do face financial constraints that force NGOs to behave like their for-profit counterparts; they must continuously secure funding to remain able to pursue their normative objectives. For this reason, many scholars argue that the way instrumental concerns shape the emergence, objectives, and strategies of NGOs renders NGOs very similar to businesses or firms.¹² Like businesses, NGOs desire to survive and grow while pursuing their goals, whether the goals are to reduce poverty, end conflict, or provide access to potable water. Sell and Prakash go so far as to assert “that the similarities between business and NGO ‘campaigns’ far outweigh their differences.”¹³ Bush¹⁴ refers to the “survival instinct” of NGOs, arguing that

⁶For work that focuses on normative perspectives of NGOs, see for example (Keck and Sikkink 1998).

⁷Cooley and Ron 2002, 5.

⁸Ibid., 6.

⁹Bob 2010; Mihr and Schmitz 2007; Murdie and Bhasin 2011; Ron, Ramos, and Rodgers 2005.

¹⁰Kelley 2009.

¹¹Bütthe, Major, and Souza 2012.

¹²Cooley and Ron 2002; Johnson and Prakash 2007; Sell and Prakash 2004.

¹³Sell and Prakash 2004, 144.

¹⁴Bush 2011.

these instincts influence the actions of NGOs. Among other influences, these instincts encourage NGOs to adapt in order to continuously secure funding, resulting in NGOs operating like “normal” organizations, “despite the field’s ideological origins and grand rhetoric.”¹⁵ Thus, while NGOs maintain ideological goals, their need to secure funding from donors compels NGOs to operate strategically. Moreover, the reliance of NGOs on donors influences the behavior of the NGOs and shapes how the NGOs pursue their objectives.

Accountability in the NGO-donor Relationship

The NGO-donor dynamic is as a classic principal-agent relationship.¹⁶ NGOs face constant pressure to please donors in order to maintain funding and continue to pursue their policy goals. Donors, on the other hand, must decide in which NGOs to invest. Donors are concerned about their investments being used wisely by the NGOs in a way that maximizes the return on those investments. In simpler terms, donors do not want to waste their money on ineffective or low-quality NGOs.¹⁷ Critics of this approach argue that the principal-agent framework is inappropriate because the donor and the organization have the same preferences¹⁸ or that NGOs exhibit behavior that is more consistent with sincere preferences than strategic behavior.¹⁹ We contend that even when the donor and NGO do have the same ideological preferences, the assertion that their preferences are identical is incomplete and problematic. While donors and NGOs might have the same long-term goal of, for example, alleviating poverty, they may have divergent preferences over how to pursue this goal. More importantly, donors are unable to determine if the organization they are supporting is capable of pursuing these goals effectively. This uncertainty is critical to understanding the motivations of donors and their push for accountability.

Grant and Keohane claim that “reputational effects are involved in all issues of accountability.”²⁰ Actors strive to build a reputation in order to separate or distinguish themselves from the crowd by establishing an identity or brand. Boulding²¹ reaffirms that donors desire to select high-quality

¹⁵Bush 2011, 20.

¹⁶Cooley and Ron 2002.

¹⁷Boulding 2009; Bush 2011; Ebrahim 2002 and 2003 and 2005; Gugerty 2009; Jordan 2005; Reinhardt 2009; Rubenstein 2007; Wenar 2006.

¹⁸Barnett and Finnemore 1999.

¹⁹Büthe, Major, and Souza 2012.

²⁰Grant and Keohane 2005, 36.

²¹Boulding 2009.

NGOs and stresses the role that information asymmetries play in creating uncertainty for the donors. While an NGO has the necessary information about its abilities and objectives, the NGO faces the challenge of credibly revealing information about its capabilities to donors. NGOs have an incentive, then, to signal high capability through actions and outcomes rather than through (cheap) talk. Gugerty²² claims that the information asymmetry between donors and NGOs creates distrust. Because donors cannot separate the low-quality NGOs from the high-quality NGOs, they distrust all NGOs. To resolve the information asymmetry and ensure selection of high-quality NGOs, donors look for measurable signs of performance success by the NGO. Therefore, not only are the objectives of the NGO important to the donor, but also, the donor cares about the ability to observe and quantify the extent to which the NGO has achieved its goals.

Underlying the logic of improving accountability and the overall efficiency and competitiveness of NGOs is the notion that there is an emerging marketplace of NGOs that will naturally improve their outputs. Cooley and Ron²³, however, challenge the notion that a competitive supply of NGOs will unequivocally improve transparency. Instead, they argue that such competition can lead to increased problems of uncertainty and NGO insecurity. This insecurity is driven fundamentally by market pressures. As Cooley and Ron write, “The more that nonprofit groups attempt to secure and maintain contracts under market-generated pressures, the more they will copy the structures, interests, and procedures of their for-profit counterparts.”²⁴ Wenar, focusing on development aid organizations, asserts that for these NGOs the focus on accountability can influence their behavior by shifting focus to “satisfying certain bureaucratic requirements instead of pursuing its underlying mission.”²⁵ This discourages NGOs from taking on more difficult projects and hinders NGO effectiveness.²⁶ While accountability measures are used to ensure that NGOs are using donors’ contributions wisely, they often generate negative externalities as well, decreasing the effectiveness of the organizations.

NGOs face great difficulty in generating effective accountability procedures that satisfy donors. Gutner and Thompson²⁷ cite the challenge that donors have in judging the performance of NGOs;

²²Gugerty 2009.

²³Cooley and Ron 2002.

²⁴Ibid., 13-14.

²⁵Wenar 2006, 7.

²⁶Ibid., 16-17.

²⁷Gutner and Thompson 2010.

donors, thus, look at outcome-based metrics and an organization's ability to achieve certain objectives to assess whether or not the NGO meets expectations. Gutner and Thompson point to "definable and measurable" outcomes that are used by donors to assess NGO performance. Bush²⁸ argues that measurable programs are preferable to donors, particularly when donors are not able to directly observe the programs, or are not equipped to evaluate the program's effect on the long-term policy objectives of the organization. Ebrahim²⁹ also notes the importance of positivist and easily quantifiable measures of success and failure; in order to keep NGOs accountable, donors conduct reviews that highlight short-term, measurable results while ignoring the NGOs' contributions to more durable goals. While these reviews help assuage donor concerns, the emphasis on quantifiable measures generates tension between donors and NGOs. Elaborating on these tensions, Ebrahim states, "First, there are conflicts among NGOs and funders over whether they should be assessing processes such as 'participation' and 'empowerment' or whether they should measure more tangible products such as numbers of schools built, trees planted, and land area irrigated. For the most part, donor appraisals tend to focus on products."³⁰ Therefore, the push for accountability tends to focus on immediate, tangible successes, not concerns about the durability of program impact.

Not only does the push for accountability lead to a focus on immediately measurable successes, but the need for immediate successes also directly shapes NGOs behavior. Donor evaluation of immediate outputs discourages NGOs from focusing on longer-term objectives, running the risk of losing sight of these long-term goals altogether.³¹ Bush³² considers a particular type of NGO: democracy promoting NGOs. She finds that the pressure for measurable outcomes is greatest when it is most difficult for state donors to observe programs and that this also creates pressures for the NGOs to pursue more regime-compatible programs than they would otherwise.³³ Thus, for democracy NGOs, the focus on measurability creates tension between the NGOs' desire to advance democracy and the specific ways in which the NGOs pursue these goals. Importantly, Bush asserts that some programs essential for democracy success are also programs that are not easily measurable, forcing the NGOs to choose between the programs that signal outcomes to donors and their

²⁸Bush 2011.

²⁹Ebrahim 2002.

³⁰Ebrahim 2003, 817.

³¹Ebrahim 2005.

³²Bush 2011.

³³Bush focuses on state donors and their relationships with democracy-promoting NGOs. The model we develop below can be applied to a variety of institutional donors and issue areas.

ultimate goal of improving democratic processes and institutions. In this way, Bush’s hypotheses are very similar to the one we articulate in this paper. We diverge, however, in our explanation regarding the source of these inefficiencies. Bush focuses on the role of professionalization in the “democracy establishment” on shaping the behavior of NGOs. We see our focus on attribution as a complementary explanation for these inefficiencies. Moreover, there are dynamics in the NGO-donor relationship that are generalizable across policy-sectors. Considering the NGO-donor relationship more broadly can help explain which fields are most susceptible to principal-agent problems.

The argument by Cooley and Ron is foundational to this literature; here we make two observations that motivate our research. First, we agree that this principal-agent structure applies inescapable pressure to NGOs and donors as they navigate the logistics of their policy pursuits. Just as not all for-profit firms are undermined by short-term horizons and shareholders focused on immediate profit, one can also find evidence that not all NGO goals are undone by these strategic constraints.³⁴ In other words, the question remains as to *when* NGOs are overwhelmed by the strategic constraints of the principal-agent nature of their relationship with donors. Second, the theoretical argument in Cooley and Ron³⁵ is broadly tied to the logic of market pressures and principal-agent dynamics. In this paper, we seek to identify a specific causal mechanism by which NGOs become strategically stuck, so to speak. In doing so, we seek to further understand the specific constraints faced by NGOs and how they influence NGO behavior. In our efforts to address this second observation with a more focused, formal model of the NGO-donor relationship, we ultimately hope to gain purchase on resolving the question of when the reputation trap is sprung. Our next task, therefore, is to develop a model that identifies when and why NGOs are impacted by their need to be accountable to donors.

Modeling the Donor–NGO Relationship

The question remains: why do NGOs sometimes produce work that is immediate and public but appears to be incompatible with long-term success? As noted above, we suspect that the relationship between NGOs and donors³⁶ can be a fruitful source of answers. In order to fix our attention

³⁴Büthe, Major, and Souza 2012.

³⁵Cooley and Ron 2002.

³⁶Our argument is limited to the study of institutional donors, to the exclusion of individual private donors such as those identified in Büthe, Major, and Souza 2012.

on the interaction between NGOs and the donors that enable their survival, here we develop a specific model that builds off of the principal-agent framework set forth by Cooley and Ron.³⁷ By doing so, we hope to identify the specific causal mechanism that hobbles NGO behavior, and in the process gain some purchase on our ability to predict when such problems are likely to arise.

The premise of the model is that the NGO has requested funds and the donor chooses whether to fund the NGO to pursue a particular policy. If the NGO receives funding, it then allocates these resources. In particular, it must determine how much effort to put into achieving immediate policy successes versus pursuing other activities. By immediate policy successes, we refer to tangible positive outcomes achieved in the current funding cycle that can be attributed to the efforts of the NGO. Such policy successes may or may not lead to the achievement of macro-level long-term policy goals, which are not commonly attributable to the actions of an individual organization.

Donors want to maximize the achievement of their policy goals through their investment in an NGO. Whereas the typical discussion of investment centers around returns and profit, here the returns gained are in policy outcomes. We assume that, all else equal, the donor prefers to invest in NGOs that are more likely to succeed in obtaining these outcomes. Since the donor cannot fully observe the NGO's ability to succeed before the donor provides funding, this preference for a good investment means that donors must be concerned with the reputation of the NGO. We also assume that the NGO is first and foremost interested in survival. Thus, the NGO focuses its efforts on actions that will bolster its reputation and maximize its ability to attract funding from donors. It is important to emphasize that this assumption does not imply that NGOs are money-driven enterprises. NGOs clearly have a strong desire to reach policy goals. Without funding, however, they would not survive and thus would not have a chance to pursue their policy goals.³⁸

A key problem in the donor-NGO relationship is the donor's uncertainty surrounding the NGO's abilities. In particular, donors often do not know if an organization has the capacity to achieve positive policy outcomes, which we refer to as a high quality NGO. This uncertainty is exacerbated by

³⁷Cooley and Ron 2002.

³⁸Survival is not meant literally, but rather in the standard use referring to the existence of the organization. The assumption that NGOs care about funding is similar to the common assumption that politicians care primarily about staying in office. This assumption allows us to theoretically isolate the effects of reputation from other potential motivating factors for NGO behavior. One can indirectly incorporate the role of policy salience into the model below through the cost term. In particular, one would expect that NGOs that care more about the relevant issue would have lower marginal costs of effort than those that do not. Thus, as long as one does not assume that altruism or salience leads NGOs to always pursue high effort, our model can take into account both the monetary and policy interests that influence NGO decision making.

the fact that an organization's quality may change over time. For example, the director of an NGO may exit the organization, handing over the organization to new leadership who may be more or less skilled than her predecessor. On the opposite end of the NGO hierarchy, large turnover among staff could decrease the quality of the organization until new staff is properly trained. Additionally, new technology could be discovered or acquired by the organization, improving productivity and efficiency. Such shake-ups are always possible in an NGO, and these internal changes are often unobservable to donors. Even if the actual changes are observed, the consequences of these changes with respect to the organization's quality are difficult to credibly convey to the donor.

Moreover, while the donor can observe the immediate policy outcomes of the NGO's activities, given that it is not on the ground at all times, it often cannot observe the level of effort the NGO puts into various activities. NGOs, like any other type of organization, must make decisions about resources allocated to administration, infrastructure and marketing. While third parties have emerged to mitigate this particular information problem, they are not able to completely and immediately eliminate the privacy of this information.

These sources of uncertainty create problems that potentially inhibit the ability of the donor to maximize the policy returns from its investment in an NGO. Most importantly, if the donor is uncertain about the quality of NGOs, it cannot easily direct its resources to the highest quality organizations. Thus, a donor may end up funding an NGO that does not have the ability to produce successful policy outcomes. Known as adverse selection, this problem emerges when a principal is not able to select the type of agent that it would choose if it had complete information. Additionally, since the donor cannot always observe the behavior of the NGO, the donor is not able to condition its funding on the NGO's actions. Thus, there is the potential that the NGO will put less effort into achieving the donor's goals than the donor would ideally prefer. This problem, which is known as moral hazard, results from the inability of a principal to perfectly monitor its agent. These classic principal-agent problems are the underlying motivation for the push for greater accountability from NGOs.

The mechanism that naturally emerges to address the principal-agent problems between donors and NGOs is reputation. We conceptualize reputation as the donor's belief that an NGO is high quality. The donor prefers to fund organizations with good reputations. In the model developed below, an NGO's reputation is largely a function of its record of policy success. Since high quality

NGOs are better able to achieve successful policy outcomes, such achievements provide signals that bolster the reputation of the NGO in the eyes of the donor. Given this, donors steer funding to organizations that have demonstrated the ability to produce positive outcomes. This provides NGOs with an incentive to put effort into activities that will lead to observable, attributable policy successes in the immediate term. While such an incentive structure can help donors overcome problems of adverse selection and moral hazard, it can potentially create a new problem. As we explain below, when the types of accomplishments achievable by an NGO in the short term are not durable, NGOs and donors can find themselves in what we call a reputation trap.

Theoretical Model

Our theoretical model includes two players, a donor (the principal) and an NGO (the agent).³⁹ The NGO can be one of two types (τ): high quality (H) or low quality (L). High quality NGOs have the ability to pursue successful policies, while low quality NGOs do not. At the beginning of the game, Nature chooses the type of the NGO. The NGO is high quality with probability $\theta \in (0, 1)$ and low quality with probability $1 - \theta$. Similar to many game-theoretic models of the reputation, we assume that the principal is uncertain about the type and actions of the agent.⁴⁰ Thus, while the NGO learns its type, the donor does not.

In each period, the donor decides whether to fund the NGO. If the donor chooses not to fund, the NGO ceases to exist and the game ends. If the donor funds, it transfers a lump sum, f , to the organization. A high quality NGO then decides the level of effort to put into achieving a successful policy outcome in that period. In particular, it can expend a high level of effort (h) at a cost $e > 0$ or a low (l) level of effort at no cost.⁴¹ To allow for the possibility that the NGO would be willing to exert high effort, we assume that the cost of high effort does not exceed the per-period funding available from the donor (i.e., $e \leq f$). Formally, we assume that a low quality NGO can only expend a low level of effort, which is equivalent to assuming that the probability of policy success for a low quality NGO is equal to the probability of success for a high quality NGO exerting a low

³⁹The information structure of this model is similar to principal-agent models of firm reputation developed by Mailath and Samuelson 1998, 2001.

⁴⁰Fudenberg and Levine 1992; Mailath and Samuelson 2001.

⁴¹Throughout the discussion, whenever we refer to “high” or “low” effort, we are only referring to the level of effort the NGO puts into achieving policy successes in the current funding cycle, not its overall level of effort in all of its activities.

level of effort. The donor does not observe the amount of effort expended by the NGO.

After the NGO chooses the level of effort, Nature then determines the policy outcome for the period, which can be either successful or unsuccessful. If the NGO chooses a high level of effort, there is a successful outcome in the current period with probability π and an unsuccessful outcome with probability $1 - \pi$. For simplicity, we assume that low effort always results in an unsuccessful outcome.⁴² The policy outcome is observed by all players. We assume that donors receive a payoff of 1 for a successful outcome and 0 for an unsuccessful outcome. NGOs do not receive any direct payoff for the policy outcome.

Play continues until the donor decides not to fund the NGO. In all subsequent periods after the first period, we assume that there is the possibility of an exogenous shake-up in the NGO after the donor's funding decision with probability λ . For example, there could be a change in personnel of the NGO or a technological change. In the event of a shake-up, Nature redetermines the NGO's type. In particular, after a shakeup, the NGO is high quality with probability θ and low quality with probability $1 - \theta$. We assume that the donor knows the probability that a shake up will occur in a given period but that the donor does not observe the shake-up. Finally, we assume that the donor is myopic, so it only cares about its payoff in the current period (i.e., it has a discount factor of 0). We expect that donors will be interested in getting a return on their investment in a given period before they consider whether to renew an NGO's funding. On the other hand, since the NGO is concerned with survival, it discounts future payoffs with a discount factor $\delta \in (0, 1)$.

Given that we assume that the donor is myopic, we limit our analysis to Markov strategies, which only depend upon payoff-relevant histories. Let μ be the donor's belief that the NGO is high quality, and let $\sigma(\mu)$ be the probability that a high quality NGO will exert high effort given that belief. Then the donor expects to receive a successful policy outcome in a given period with probability $p(\mu) = \mu\sigma\pi$. Since the donor is myopic and the utility of a successful outcome is 1, it will choose to fund if $p(\mu) \geq f$.

Consider a situation in which high quality NGOs always exert high effort into achieving immediate policy successes. In this case, policy outcomes can provide information about the NGO's quality. The donor's posterior belief that the NGO is high quality in a given period is a function of

⁴²Though the analysis would be more complex, we expect that one would obtain similar substantive results in a model in which success is possible after low effort, as long as the probability of success is higher after high effort than after low effort.

its prior belief, the policy outcome in the previous period, and the probability of a shake-up. After a successful policy outcome, the posterior belief is:

$$\mu_s = 1 - \lambda(1 - \theta). \quad (1)$$

Since only high quality NGOs can be successful, a successful outcome in the previous period indicates that the NGO was high quality in the previous period. However, there is some probability, $\lambda(1 - \theta)$, that a shake-up in the current period will result in the the NGO being low quality. Thus, if $\lambda > 0$, the donor can never know with certainty whether the NGO is high quality in the current period. On the other hand, the donor's posterior belief that the NGO is high quality after an unsuccessful outcome is:

$$\begin{aligned} \mu_u &= (1 - \lambda) \left[\frac{(1 - \pi)\mu}{(1 - \pi)\mu + 1 - \mu} \right] + \lambda\theta \\ &= (1 - \lambda) \left[\frac{(1 - \pi)\mu}{1 - \pi\mu} \right] + \lambda\theta. \end{aligned} \quad (2)$$

If $0 < \mu < 1$, $\mu_s > \mu_u$. Thus, as long as there is uncertainty about the NGO's quality, the donor's belief that the NGO is high quality is higher after a successful policy outcome than after an unsuccessful outcome. In addition, it can be shown that the donor's belief that the NGO is high quality decreases after an unsuccessful outcome. If we let $\hat{\mu}$ be the fixed point at which $\mu_u = \mu$ (such that $0 < \hat{\mu} < 1$), it follows that the $\hat{\mu}$ is the lowest possible belief about the NGO's quality that the donor can have.

If there is no possibility of a shake-up (i.e., $\lambda = 0$), a high quality NGO will never choose to exert high effort into immediate policy successes. To see why this is the case, consider the situation in which the donor believes the NGO to be high quality ($\mu = 1$). In this case, $\mu_s = \mu_u = 1$. Because the donor assumes that any unsuccessful outcome is due to bad luck, rather than low effort, it will believe the NGO to be high quality regardless of the policy outcome. Thus, the NGO has no incentive to put effort into short-term policy successes since it would be funded in any case. In addition, there cannot be an equilibrium in which the high quality NGO chooses low effort when $\mu = 1$ but chooses high effort at other values of μ . In such an equilibrium, the donor would not fund if $\mu = 1$. Since $\mu_s = 1$, the NGO knows that it will not be funded in the next period if there is

a successful outcome. Given this, the NGO would have no incentive to pay the cost of high effort because it would cease to exist after a successful policy outcome. Thus, similar to the findings of Mailath and Samuelson in a model of firm reputation, separation between “competent” and “inept” firms can only occur if there is perpetual uncertainty about the firm’s type.⁴³ In our model, this implies that high effort by high quality NGOs can only occur in equilibrium if $\lambda > 0$. The next proposition identifies the conditions under which there will be high effort.

Proposition 1. *If the cost of effort is sufficiently small, $\lambda > 0$, and $f > \hat{\mu}\pi$, there exists a Markov perfect equilibrium in which a high quality NGO always chooses to put high effort into achieving immediate policy successes in the current period.*

The formal proof of the proposition can be found in the appendix. The intuition is as follows. If high quality NGOs will exert high effort, the donor will be more willing to fund high quality NGOs than low quality NGOs. Thus, the donor’s equilibrium strategy will depend upon its belief that the NGO is high quality. In particular, there will be a cutpoint, μ^* , such that the donor will fund if $\mu \geq \mu^*$ and not fund otherwise. Due to the possibility of a shake-up in each period, the donor can never know the NGO’s type with certainty. Since successful outcomes are only possible with high quality NGOs, the donor’s belief that the NGO is high quality is higher after a successful outcome than after an unsuccessful outcome. Because the NGO would prefer to maintain its funding, it has an incentive to prevent the donor’s belief from falling below μ^* . Since, in expectation, higher effort will produce a higher belief than lower effort, the NGO will pursue a high level of effort if the cost is sufficiently low.

The theoretical model provides insight into the potential role that reputation can play in the relationship between donors and NGOs. One can consider the parameter μ , the donor’s belief that the NGO is high quality, to be the NGO’s reputation. Because donors cannot directly observe the quality of an NGO, they must make their funding decisions based upon an NGO’s reputation. In particular, donors are only willing to fund NGOs with good reputations ($\mu \geq \mu^*$). If an NGO’s reputation falls too low, a donor will cut off its funding.

In the model, an NGO’s reputation is based upon its record of policy successes. Because donors cannot directly observe all of the actions of an NGO, they do not know the precise effort level that

⁴³Mailath and Samuelson 1998 and 2001.

the NGO puts into particular activities. However, they can observe whether the NGO's efforts lead to successful policy outcomes. For example, a donor might not know how much effort an NGO put into mediating a civil war, but it can observe whether the mediation led to a peace agreement. Thus, a donor updates its belief about the quality of an NGO after each policy success or failure. If success is only possible when a high quality NGO exerts a high level of effort, an NGO can quickly develop an excellent reputation after a policy success. On the other hand, a series of policy failures would gradually erode the NGO's reputation. After a sufficient number of failures in a row, the donor will begin to believe that the NGO is low quality and will cut off the NGO's funding.

These reputation dynamics thus influence the behavior of NGOs. To maintain its funding from donors, a high quality NGO will attempt to build and maintain a good reputation by putting more effort into activities aimed at achieving immediate policy successes. For such reputational concerns to influence the behavior of NGOs, there must always be some uncertainty on the part of the donor. If the donor knows with certainty that an NGO is high quality, there is nothing for the NGO to prove, as there is no outcome that would decrease the donor's belief that the NGO is high quality. If there is always a possibility for a shake-up in the organization—due to staff turnover or new challenges in the international policy arena—the donor can never know with certainty the quality of the NGO. This gives the NGO an incentive to put effort into achieving attributable policy successes to maintain a good reputation.

Model Implications: The Reputation Trap

This reputation process can provide a useful accountability mechanism for donors. Given the information asymmetries inherent in donor-NGO relations, donors aim to avoid problems of adverse selection, in which they fund low quality NGOs, and moral hazard, in which NGOs fail to put sufficient effort into the donor's policy goals. From the perspective of the donors, attributing the source of many policy successes can be very difficult. The overall objectives of international NGOs are often ambitious, and achievement of these long-term goals is not arrived at quickly. Moreover, it is often difficult to attribute macro-level social, economic, and political outcomes—such as life expectancy, infant mortality, economic development, and democratization—to the activities of an individual NGO. Thus, when NGOs put effort into activities that primarily contribute to the achievement of non-attributable outcomes, donors are not able to connect policy successes to the

Table 1: The Reputation Trap

	Less Durable Policy Impact	More Durable Policy Impact
Attributable Outcome	Reputation Trap	Reputation Mechanism (No Trap)
Non-Attributable Outcome	Donor Uncertainty	Donor Uncertainty

actions of the NGO. In this case, as indicated in Table 1, such policy outcomes cannot reduce a donor’s uncertainty about an NGO’s quality.

On the other hand, attributable policy outcomes can provide signals of an NGO’s quality. Such signals can ensure donors their money is not being wasted and that additional financial support would be put to good use. The reputation mechanism identified in our theoretical model allows donors to take advantage of the informational properties of these types of policy outcomes. By rewarding attributable policy successes with future funding, donors create an incentive structure that encourages NGOs to concentrate their efforts on activities that will likely produce such policy outcomes. Thus, the reputation mechanism will generally result in policy outcomes in the top row of Table 1. This shift in focus to attributable outcomes allows donors to learn more about an NGO’s quality and make more informed funding decisions.

A donor’s desire to fund quality NGOs is driven primarily by the fact that such organizations are best equipped to achieve its policy goals. However, actually reaching these policy goals also requires that any policy achievements reached by an NGO have a lasting positive impact. Short-lived policy successes generally do little to accomplish long-term goals. Therefore, donors (and NGOs) care about the durability of policy outcomes. However, while the reputation mechanism can help resolve donor uncertainty and address problems such as adverse selection and moral hazard, it does not guarantee that policy successes will be durable. In fact, at times the reputation mechanism may actually promote the production of outcomes with less durable policy impacts.

Ideally the reputation mechanism would lead to durable and attributable policy outcomes, corresponding to the upper right hand cell of Table 1. In this case, high quality NGOs would be

able to signal their abilities to donors and contribute to lasting policy achievements at the same time. However, in many cases, the attributable outcomes that NGOs are able to achieve in the immediate term may not have a durable policy impact. NGOs that focus on achieving these types of outcomes, which correspond to the upper left hand cell of Table 1, are able to signal their quality to donors but are less effective at reaching long-term policy goals.

To see how NGOs could find themselves pursuing these less durable outcomes, consider a hypothetical NGO focused on health care in a developing country. The NGO may promote the number of medical procedures that it has performed in a country as a signal of its quality, as these outcomes can be directly attributed to the actions of the NGO. However, this provides no information on the organization's impact on the overall level of health in the country. Moreover, given that there are many factors that influence health outcomes in a country, it would be difficult to attribute improvements in aggregate measures of national health outcomes to the activities of this particular NGO. Thus, potential projects that might greatly benefit general levels of health but that do not produce immediate attributable outcomes would not provide any insight into an NGO's quality. To signal this information to its donors, a high quality organization would have an incentive to focus its attention on maximizing the number of medical procedures performed, regardless of whether these activities are the most effective means of achieving the group's long-term goals.

We call the situation where NGOs opt to pursue activities aimed producing less durable attributable policy outcomes in lieu of more durable non-attributable policy outcomes a "reputation trap." To address information asymmetries about donor abilities and avoid funding low quality NGOs, donors reward organizations that can produce attributable policy outcomes. When faced with a choice between focusing its efforts on achieving attributable outcomes that may have a less durable policy impact and contributing to the production of more durable but nonattributable policy outcomes, NGOs opt for the former. This suboptimal outcome is not the result of incompetence (or naiveté) on the part of the donors or the NGOs. Instead, these parties are acting perfectly rationally given the circumstances. If NGOs were to shift their focus to generating durable but non-attributable policy outcomes, they would risk their funding and thus their survival. If donors were to stop rewarding the attributable policy successes, they would limit their ability to identify high quality NGOs and avoid problems of adverse selection. While this would give NGOs the opportunity to potentially pursue more durable outcomes, donors would not be able to determine if

any durable policy successes are the result of an NGO's actions.

Of course, not all donor-NGO relationships will lead to a reputation trap. Here we focus on two important variables for discussion: the role of shakeups and the intrinsic durability of attributable outcomes. In situations where NGOs have the ability to produce durable attributable outcomes quickly, the reputation mechanism will not lead to such negative consequences. Moreover, the reputations of NGOs are perishable only when there exists private information about the occurrence of some change (the shakeup) in the ability of the organization to succeed. When there is little uncertainty on the part of the donor about the quality or actions of an NGO, there is less need for a reputation mechanism. In those cases, donors may be able to create alternative incentive structures that are primarily aimed at producing durable outcomes. These dynamics suggest that the reputation trap may be particularly influential for young NGOs, or when donors and NGOs establish new partnerships.

The intrinsic durability of attributable policy outcomes is a second important factor in understanding when reputation maintenance dominates NGO behavior. Sometimes attributable policy outcomes tend to be less durable than those that are not attributable to the actions of an NGO. It is reasonable to question the extent to which NGOs and donors have control over this overlap between attribution and durability. The reputation trap is most pernicious when there is little or no overlap, and NGOs find themselves compelled to pick attribution at the expense of lasting policy success. When there is considerable overlap, however, organizations may be able to tailor their policy outputs to be recognizable without abandoning durability.

In the next section, we provide two empirical illustrations of the reputation mechanism focusing on this tradeoff between attribution and durability. In one case, the need to produce attributable outcomes has led a reputation trap in which short-term achievements do not have a durable policy impact. In the other case, such incentives have not prevented an NGO from achieving more durable policy outcomes.

Illustrating the Reputation Trap

To investigate the implications of our theoretical model, we compare two policy arenas in which we observe NGOs pursuing reputations in order to secure donor funding. We first examine the

practice of drilling boreholes, an important but troubled technique that is often used to improve water access. Our second case focuses on the practice of conflict mediation, where we highlight NGOs' ability to generate mediation outcomes that are in line with longer term goals of conflict resolution. In the former case, we demonstrate that the pressure to convey credible signals of quality to the donor influences the decisions NGOs make with respect to the pursuit of attributable but fragile policy outcomes. The water case thus illustrates the reputation trap. In the latter case, we show that while reputation is a driving force for NGO behavior, the reputation trap is not inevitable. The mediation case thus illustrates how NGOs can and do avoid the reputation trap when their drive for attributable actions aligns with durable policy outcomes.

Water NGOs and Boreholes

There are 884 million people who face a struggle to find safe drinking water each day, while close to 2.6 billion people do not have adequate access to proper sanitation.⁴⁴ Without access to clean water and proper sanitation, populations become susceptible to diarrhea and intestinal infections and, more broadly, malnutrition. Given the challenges and risks posed by unsafe water and inadequate sanitation, a number of NGOs have arisen to combat the problems and increase access to safe and clean water. In what follows, we illustrate how water-focused NGOs have suffered from a constant reliance on short-term solutions to water shortages.

Boreholes, the most widely used solution to water access, are an essential component to solving water access problems. They also have the advantage of being tangible and attributable contributions. Despite these advantages, however, boreholes also have known and documented failures that hinder long-term policy impacts and the development of sustainable clean water access. More durable solutions, such as research and extensive local training, require longer-term funding and implementation. More importantly, such solutions are less attributable to the NGOs. While effective at combatting unsafe water in the long-term, durable solutions require the active engagement of many actors. These durable but lengthy and complex projects send noisy signals about NGOs' effectiveness and quality. These noisy signals do little to alleviate donor concerns about their funding being used effectively by water NGOs, and thus do not provide sufficient accountability mechanisms. This drives high quality water NGOs to continue to dig new boreholes at the expense

⁴⁴UNICEF 2010.

of devoting scarce resources to maintenance, infrastructure and training, in order to signal their effort on the ground and their ability to achieve policy successes.

Access to clean water each day is a challenge, but many areas have groundwater reserves that, if accessed, could fulfill communities' needs. According to Foster, Tuinhof, and Garduño⁴⁵, groundwater resources could reduce poverty and improve people's lives if used more effectively. The question, then, for NGOs such as WaterAid, World Vision International, and Water for People, is how to facilitate access to this water in a safe way. NGOs have relied upon boreholes as an inexpensive way to access clean, uncontaminated groundwater.⁴⁶ Boreholes—small-diameter wells—provide a quick, low-cost means to increase the number of water access points in a region by taking advantage of pre-existing groundwater reserves. New boreholes have several immediate advantages. They create more proximate access to water for populations, which in turn decreases the burden of attaining water by reducing the number of hours spent walking to an access point. Proximity to water can improve both access and individual security. Furthermore, by making water more accessible, boreholes help improve health outcomes, especially for children.⁴⁷ World Vision International, for example, cites the success of building boreholes in the Afram Plains region of Ghana; close to eighty-seven percent of their wells built in the region since 1995 were still providing an “an adequate supply of safe water” as of 2012.⁴⁸

While boreholes bring some benefits to the populations they serve, a large literature cites their weaknesses. World Vision's success in Ghana, then, seems to be an exception to the rule. According to one study of Ghana, “many of the boreholes drilled were dry whilst other nominally successful boreholes showed a progressive decline in yield to fail after two to three years of use”.⁴⁹ Cobbing and Davies list a forty percent failure rate for boreholes built by various NGOs in the Afram Plains region. A study of Mali offers similar pessimism of the effectiveness of boreholes, finding a forty-one percent success rate when success was defined as the boreholes being in use by the community, and a ten percent success rate if success was defined as reaching World Health Organization minimum acceptable flow rates.⁵⁰ Gleitsmann, Kroma, and Steenhuis conclude that boreholes are not a

⁴⁵Foster, Tuinhof, and Garduño 2008.

⁴⁶MacDonald et al. 2009.

⁴⁷Carter, Tyrrel, and Howsam 1999.

⁴⁸WVI 2012.

⁴⁹Cobbing and Davies 2004, 111.

⁵⁰Gleitsmann, Kroma, and Steenhuis 2007.

sustainable way to improve rural water supply management.

More specifically, several problems have been identified about boreholes that destabilize their capacity to increase access to safe water. According to Malians with access to boreholes, the boreholes pumps are unreliable and frequently break down, the flow from the pumps is prohibitively slow, access fees to pumps are too high, the boreholes are generally difficult to use, and/or the pumps are located too far from home.⁵¹ Additionally, as boreholes break down, locals often do not have the knowledge or resources for repairs.⁵² The boreholes, then, often fall into disrepair.

Other studies cite groundwater drought as a reason for borehole failure. Periods of low rainfall, overuse, or other causes of inadequate groundwater replenishment result in boreholes running dry because there is simply not enough water to pump. Importantly, locations that are at greatest risk of groundwater drought are predictable and additional research before borehole drilling could help prevent drilling in locations where groundwater drought is likely. While the hazard for groundwater drought is predictable, NGOs rarely take the steps necessary to investigate the best locations or structure for boreholes for reasons we will discuss later in this section.⁵³

Boreholes as a means to increase water access points are an essential step, but they can also be a non-durable solution. NGOs, while still proponents of boreholes, realize their shortcomings. As such, NGOs have begun to think about new or more durable solutions to unsafe drinking water. For example, NGOs have signaled that for water supplies to be sustainable, local populations must be included, local decisions should reflect community choices, and extensive local training should accompany the creation of water access points.⁵⁴ Moreover, WaterAid and Water for People advocate research and long-term maintenance plans to improve their water access points. Water for People has data available on their global water-related activities on their website.⁵⁵ This data includes the location of Water for Aid water projects, as well as the current status of the site (is it operational) and how many people are utilizing the site. While such data is a positive step toward accountability and longer-term sustainability, Water for People, like many other organizations, remains caught in a trap where they focus on immediate policy solutions above all else.

⁵¹Gleitsmann, Kroma, and Steenhuis 2007.

⁵²Easterly 2014.

⁵³Calow et al. 1997.

⁵⁴Carter, Tyrrel, and Howsam 1999; Gleitsmann, Kroma, and Steenhuis 2007.

⁵⁵The Water for People data is available at <http://watermapmonitordev.appspot.com/> last accessed on January 14, 2014.

If boreholes are not durable and NGOs know this, why do NGOs continue to use them as a way to increase access to clean water? In other words, why have water NGOs not learned from boreholes failures? As mentioned above, NGOs have recognized the shortcomings of boreholes, but they have not translated that learning into practice. Boreholes are as common now, according to the most recent reports from water NGOs, as they were twenty-five years ago.⁵⁶ NGOs' continued fixation on boreholes is not caused by ignorance; rather, the focus on boreholes is a result of the reputation trap. Water NGOs, as our model suggests, feel pressure to employ strategies that are attributable to the organization. While research and training, for example, may contribute to more durable solutions to water access problems, the externalities of such strategies are not directly attributable to NGOs. Instead, credit for durable impacts would be shared among NGOs, governments, community leaders, and local groups. This means such programs focusing on durability are less able to send signals to donors that the NGOs are using the donor's money as effectively as possible. Research and training are less easily quantified projects that are also less directly connected to the goal of providing clean water access. Water NGOs, knowing that donors are concerned with the quality of the NGOs they fund, are aware of the need to pursue attributable policies that they can report to their donors; for water NGOs, this discourages NGOs to invest in durable options, opting instead to construct boreholes that immediately improve water access and signal that they are able to produce outcomes desirable to the donors. In sum, water NGOs construct boreholes in spite of their shortcomings because boreholes are immediate and attributable steps that allow NGOs to signal their quality to donors.

WaterAid, a leading water NGO, has acknowledged the difficulty in designing sustainable water and sanitation projects.⁵⁷ While it has dedicated time and resources to evaluating the efficacy of its programs, WaterAid has found that “documented experience from the wider WASH [water supply, sanitation, and hygiene] sector was difficult to assimilate into improved programme design and management”.⁵⁸ Calow et al.⁵⁹ write that NGOs place little emphasis on borehole alternatives because they encounter difficulties in quantifying the benefits or pinpointing verifiable (attributable)

⁵⁶See, for example, a discussion in Calow et al. (1997) of borehole use and shortcomings in the late 1980s and early 1990s. For a more specific case, WaterAid - an organization founded in 1981 - has showcased its use of boreholes as recently as its 2013 Annual Report (http://www.wateraid.org/us//media/Files/WaterAid_America_Annual_Report_2013.pdf).

⁵⁷Cotton, Adams, and Shaw 2012.

⁵⁸Ibid., 2.

⁵⁹Calow et al. 1997.

indicators of success with other activities. Donors have been pushing shorter funding periods and have shown “a preference for dealing with immediately tangible problems which produce short-term results (e.g. borehole drilling programmes and the installation of handpumps)”.⁶⁰ Donors, themselves, write that “Defining and aligning on investment outcomes and the data needed to measure them is the basis of our grant making approach. We call this outcome investing.”⁶¹ Feeling this pressure, NGOs focus on producing attributable results that are immediate and easily quantifiable.

In another example, as World Vision International sought to increase water access, “borehole drilling ‘success rates’ were emphasized. A borehole was judged a success if ‘wet’ at the completion of drilling”.⁶² This very immediate definition of success signals to donors that World Vision is producing measurable outcomes on the ground. It fails, however, to address the concerns about durability. World Vision has signaled its quality by advertising that it constructed 809 new wells in 2011.⁶³ Success is measured in terms of new boreholes dug, despite the known limitations of these boreholes in generating sustainable benefits for the populations they are intended to serve. NGOs, then, have focused on boreholes because they are attributable and produce immediate results. By the time a borehole fails, an NGO has already signaled its high quality to donors. Water NGOs find themselves in the reputation trap; they desire to sustainably improve clean water access throughout the world, but the need of donors to see attributable results from NGOs pushes water NGOs to pursue non-durable, but attributable, outcomes.

Avoiding the Reputation Trap in Crisis Mediation: Evidence from HDC

The Centre for Humanitarian Dialogue (HDC) is a humanitarian-focused NGO that began its operations in August of 1999. Headquartered in Geneva, Switzerland, HDC works across the globe to achieve the following goals: “to develop and strengthen a universal, intercultural and multidisciplinary dialogue in which all players concerned by humanitarian issues can exchange their experiences; and to devise and promote sustainable solutions to humanitarian problems”.⁶⁴

⁶⁰Calow et al. 1997, 255.

⁶¹<http://www.gatesfoundation.org/How-We-Work/General-Information/Our-Approach-to-Measurement-and-Evaluation>

⁶²Cobbing and Davies 2004, 117.

⁶³<http://www.wvi.org/water-sanitation-hygiene/water-facts>

⁶⁴Barakat, Connolly, and Large 2002, 6.

Under the broad goal of finding solutions to humanitarian problems, HDC is highly involved in international crisis mediation. HDC constantly strives to advance and achieve its goals, and in so doing, the organization has proven susceptible to the reputational dynamics created by the donor-NGO relationship. In particular, HDC intentionally selects the crises in which it gets involved with an eye to maximizing its impact and, importantly, its attributability. However, HDC demonstrates that not all NGOs fall victim to the reputation trap; while HDC's selection of Aceh was driven by a need to establish and strengthen its reputation, the organization's facilitation of two agreements in Aceh proved to be in line with its longer term goals of conflict resolution.

From its inception, HDC found itself conscious of reputation pressures. Put frankly, HDC needed to establish a reputation that proved its quality to donors in order to secure funding so that it could pursue its humanitarian goals. In 1999, then, HDC found itself selecting its first conflict to intervene in as a mediator. In line with our model, reputation drove HDC's decision to mediate the Aceh conflict in Indonesia. Originally, HDC planned to focus its efforts on the conflict in East Timor, however, "the density of aid agencies already present in East Timor following its independence led the HDC to seek a different venue".⁶⁵ If HDC mediated in East Timor, any successes would not have been attributable to HDC specifically, given the crowd of mediators already present. HDC, in order to establish its reputation as a quality (and thus funding-worthy) NGO, needed to focus on outcomes that would be attributable to the organization and that would capture the attention of donors. Aceh served as a perfect opportunity to build this reputation. HDC was the only mediator present in the Aceh conflict; all mediation successes would thus be attributable to the efforts of the organization.

The Indonesian region of Aceh had experienced continuous conflict since the middle of the twentieth century. Social cleavages led to a major rebellion between 1953 and 1962 known as Darul Islam; the rebellion sought Acehese regional autonomy over education, religion, and traditional laws. Although the central government granted autonomous status to the region in 1959, autonomy did not become a reality in practice. Thus, in 1976, the Free Aceh Movement (GAM) rose to prominence and declared Acehese independence.⁶⁶ The ideology of GAM is one of national liberation; specifically, GAM aimed to free Aceh from the political control of the foreign regime in

⁶⁵Leary 2004, 315.

⁶⁶Huber 2004.

Jakarta.⁶⁷ After being brutally repressed by the Indonesian military, GAM fled abroad to train and regain strength, returning to Indonesia in the late-1980s to re-launch their insurrection. Violence continued throughout the region and then intensified following the resignation of the authoritarian Indonesian President Suharto in 1998. By 2000, the Aceh conflict had attracted the attention of HDC, an external mediator who hoped to finally bring peace to the region.⁶⁸

Because of the complexities of the conflict in Aceh, HDC faced a challenging first-stab at mediation. As aforementioned, however, HDC hoped its solo efforts in Aceh would bring attribution to the organization, establish and strengthen its reputation as a quality NGO, and therefore garner support from donors. Upon entering Aceh in early 2000, HDC was able to achieve two immediate and attributable successes. First, HDC negotiated a “humanitarian pause” in May of 2000 that held sporadically until January of 2001. Then, in December of 2002, HDC facilitated what was considered a major breakthrough for the Aceh conflict, the Cessation of Hostilities Agreement, or COHA.⁶⁹ Both of these outcomes served as immediate signals of success that were attributable to HDC; the humanitarian pause and COHA strengthened the reputation of HDC as a quality NGO able to produce positive policy impacts.

Not only were the two agreements attributable to HDC and thus a signal of their ability to achieve successful outcomes, but they also proved to be compatible with the longer-term goals of conflict resolution in Aceh. The humanitarian pause endured “fitfully” from May 10, 2000 through early 2001.⁷⁰ The humanitarian pause, however fitful, contributed to a drop in violence immediately following the agreement. Moreover, while the humanitarian pause came to an end in January of 2001 after the government and GAM refused to extend the agreement, the humanitarian pause served as a stepping stone toward a more comprehensive agreement. COHA, a much more promising ceasefire, was signed on December 9, 2002 and was hailed as a major breakthrough. This second agreement was a more comprehensive in nature than the humanitarian pause. COHA included provisions for demilitarization, all-inclusive dialogues regarding autonomy, and provincial elections in Aceh.⁷¹ COHA endured until May of 2003; although the agreement ultimately failed, it again made progress toward conflict resolution. Thus, both the humanitarian pause and COHA

⁶⁷Schulze 2004, 6.

⁶⁸Huber 2004.

⁶⁹Ibid.

⁷⁰Ibid., 23.

⁷¹Ibid., vii.

were relatively durable and they served as indispensable steps in the search for lasting peace in Aceh.

Evidence from donor behavior in the HDC case also supports the claim that donors are motivated in large part by the reputation of an NGO. HDC, aware of its need to establish a reputation, chose a case where its actions would be attributable. Additionally, HDC advertised its immediate successes in Aceh to signal to donors that it was indeed a high-quality NGO capable of brokering ceasefires and agreements, even in the very challenging cases. While HDC's experience in Aceh did not put a permanent end to the fighting, the organization was able to generate positive signals and steps that ultimately set the framework for a durable peace. HDC's progress was perceived as a success by the international community and donors. The humanitarian pause, for example, was an initial success because it signaled that HDC had been able to organize face-to-face dialogue between belligerent groups and generate cooperation, however fleeting. Donors, viewing the ceasefire as a tangible form of success, credited HDC as a competent mediator that was worthy of continued funding.⁷² COHA also represented a positive and attributable result that bolstered HDC's reputation as a high-quality mediator. HDC's funding from donors has risen every year with few exceptions, showing recognition of the NGO's high-quality.

More specifically, Norway was an important supporter of HDC's efforts in Aceh; a brief examination of Norway as HDC's principal donor provides insights into the dynamics of donors' decision-making and their response to attributable outcomes from NGOs. As HDC was a nascent organization when it first started mediating the Acehnese conflict, the organization had to establish a reputation in order to garner continued funding. Norway offered limited funding to HDC beginning in 1999, primarily because of a personal rapport between HDC's director and Norway's deputy foreign minister. Following the humanitarian pause in 2000, the first success attributable to HDC, Norway began to provide additional funding for the NGO. By 2002, as HDC was on the cusp of their major breakthrough with COHA, Norway became the preeminent donor for HDC.⁷³ When Norway was uncertain about the quality of HDC, the country gave only limited funding because it was cautious to dedicate too much to an organization lacking attributable successes. As HDC established its reputation as a capable and high quality NGO through its immediate success

⁷²HDC's Annual Report from 2001 indicates that donors reacted positively to the "successful" signal created by the humanitarian pause. Funding jumped from CHF 4,624,300 in 2000 to CHF 5,756,000 in 2001.

⁷³Huber 2004, 21.

in Aceh, Norway's hesitance disappeared.

The case of HDC's mediation efforts in Aceh illustrates the pressures created by the donor-NGO relationship. Donors require attributability from NGOs in order to gain knowledge of the NGOs' type. When uncertain about the quality of the NGO, donors are hesitant and unwilling to fund NGOs. NGOs, knowing this dynamic, choose to pursue actions that will be both immediate and attributable to signal their type to donors. Along these lines, HDC was strongly influenced by the need to develop a reputation for being a high-quality organization. HDC selected into the Aceh case specifically because of reputational dynamics, as it knew it had to choose a location in which its actions would be attributable. HDC's actions in Aceh, however, did not leave it in the reputation trap. In the realm of conflict resolution, a humanitarian pause and a ceasefire are positive steps that support the long-term goals of conflict resolution. When juxtaposed to boreholes which actually have detrimental effects for long-term water access, ceasefires (regardless of their durability) sow the seeds of peace and are thus compatible with long-term goals shared by both donors and NGOs. HDC, in taking steps toward a lasting peace, established its reputation as a high quality NGO through its attributable actions in Aceh. The organization used its reputation to gain continued support from donors and to pursue subsequent mediation efforts in additional crises, such as Nepal and Burma.⁷⁴

Conclusion

Our central conclusion is connected to the fundamental principal-agent relationship between donors and NGOs, but goes beyond the foundation set forth by Cooley and Ron to elaborate the mechanisms that trigger constraints. The inability of donors to accurately and consistently observe high quality in the NGOs they support creates a political hurdle for NGOs as they seek to maintain funding in order to pursue their policy goals. Because an NGO's quality is both private information and dynamic over time, NGOs are forced to divert energy and resources to developing and maintaining a reputation. This incentive can cause NGOs to invest higher levels of effort in policy activities that will consistently deliver tangible evidence of progress in order to credibly signal high quality to their donors. When those high levels of effort have to be diverted away from durable

⁷⁴HDC 2011.

policy outcomes, NGOs can find themselves trapped by the need to produce and report attributable output.

One interesting implication of the model is the rational explanation of what may appear to be wasteful or short-sighted behavior on the part of NGOs. These organizations are routinely criticized for working on what appear to be small, temporary, and perhaps even counterproductive accomplishments. However, these behaviors may simply be an effort by NGOs to communicate meaningful signals of high quality to their donors. Ironically, even when these activities detract from the overall mission of the NGO, it will feel compelled to divert resources to consistent and public demonstrations of tangible progress in order to preserve funding.

We should emphasize that we do not claim that the reputation mechanism identified in the model above will define *all* donor-NGO relationships. Our argument merely indicates that the creation of such an incentive structure is possible in situations where donors are uncertain about the quality and behavior of NGOs. In situations where donors do not face such information asymmetries, or attribution and durability overlap, the trap can be avoided or mitigated. For example, in some mature NGOs, there may be a negligible chance that shake-up will lead to a change in its quality. Also, some donors and NGOs may be able to develop different institutional structures to resolve informational asymmetries that do not rely upon a reputation mechanism. Alternatively, some NGOs may be able to reduce their dependence on donor support, allowing them to focus on downward accountability to beneficiaries rather than upward accountability to donors.

Finally, the emergence of a reputation trap largely depends upon the type of policy outcomes that an NGO can achieve within the funding cycle and attribute to its own efforts. As noted above, when such policy accomplishments are not durable, the donor and the NGO can find themselves in a reputation trap. On the other hand, in issue areas where immediate attributable policy successes contribute to durable outcomes, the consequences of the reputation mechanism are less detrimental. Nevertheless, we expect that reputation dynamics will play a key role in many donor-NGO relationships.

By stepping away from the traditional focus between an NGO and its clients and shifting our perspective to the role of reputation in the relationship between the NGO and its donor, we offer a perspective that sheds new light on NGO behavior. Without making heroic or cynical assumptions about the intentions of NGOs, we demonstrate that these organizations balance their normative

goals with the strategic survival imperatives that emerge from the NGO-donor relationship. This balancing act has important implications for policy behavior.

Overcoming this tradeoff cannot be accomplished strictly through improvements in transparency and accountability (the two most common calls for NGO reform), but it would be a mistake to conclude that this structural problem cannot be solved. One possible solution could be to try to convince donors that the NGO's quality is established and invulnerable to change. Reputation stability, if possible, would relieve the NGO's need to re-demonstrate its quality to donors. This condition may be most likely to be achieved by changing the duration of funding agreements. Longer funding cycles give NGOs more time to accomplish their goals without focusing on survival. Just as a U.S. senator has more freedom to take political risks and focus on long term problems than her counterparts in the House of Representatives, NGOs with a multi-year funding guarantee have more leeway than those who face yearly renewals. Such a solution of course introduces potential accountability problems, of course, but this tradeoff needs to become a part of the policy discussion. Lastly, it is worth noting that a myopic focus is not always incompatible with the long-term policy goals of the NGOs and donors. To the extent that donors can tailor reporting requests such that within cycle behavior is consistent with long-term goals, both donors and NGOs can work together to mitigate the constraints of the reputation trap.

Appendix: Proof of Proposition 1

Proof. Assume that $\lambda > 0$ and $f/\pi > \hat{\mu}$. Consider the case where the high quality NGO always chooses high effort. In a Markov perfect equilibrium, strategies are only dependent upon payoff relevant histories, so they will be a function of the donor's belief about the NGO's quality (μ). The donor will prefer to fund if $p(\mu) = \mu\pi \geq f$. Thus, the donor will fund in a given period if $\mu \geq f/\pi \equiv \mu^*$ and not fund otherwise. In any period in which the donor's belief is less than μ^* , the NGO will not be funded and will cease to exist. Since $f/\pi > \hat{\mu}$, there exist potential beliefs at which the donor would fund after a successful outcome and not fund after an unsuccessful outcome. Let k_j be a state in which after j consecutive unsuccessful outcomes, the donor will not fund the NGO, and let K_j be the set of all k_j for a given j . (For example, if the current state is k_1 , then $\mu \geq \mu^*$ and $\mu_u < \mu^*$.) Let k_s be a state in which there was a successful outcome in the previous period. Then, $\{K_0, K_1, K_2, \dots, K_s\}$ is a partition of the true state space, the interval of possible values of μ : $[\hat{\mu}, 1 - \lambda(1 - \theta)]$. Given the donor's strategy, a Markov strategy for the NGO can be defined as a function $\sigma : \{k_0, k_1, k_2, \dots, k_s\} \rightarrow [0, 1]$.

Consider k_0 . Given the high quality NGO's strategy, the continuation values are:

$$V_H(k_1) = -e + \delta[1 - \lambda(1 - \theta)]\pi V_H(k_s) + \delta\lambda(1 - \theta)\pi V_L(k_s), \quad (3)$$

$$V_L(k_1) = 0. \quad (4)$$

For k_1 , the continuation values are:

$$V_H(k_1) = f - e + \delta[1 - \lambda(1 - \theta)]\pi V_H(k_s) + \delta\lambda(1 - \theta)\pi V_L(k_s), \quad (5)$$

$$V_L(k_1) = f. \quad (6)$$

For $j > 1$, the continuation values are:

$$\begin{aligned} V_H(k_j) = f - e + \delta[1 - \lambda(1 - \theta)] & [\pi V_H(k_s) + (1 - \pi)V_H(k_{j-1})] \\ & + \delta\lambda(1 - \theta)[\pi V_L(k_s) + (1 - \pi)V_L(k_{j-1})], \end{aligned} \quad (7)$$

$$V_L(k_j) = f + \delta(1 - \lambda\theta)V_L(k_{j-1}) + \delta\lambda\theta V_H(k_{j-1}). \quad (8)$$

For $j > 1$, given k_j , NGOs will receive funding with certainty in the next period regardless of the policy outcome. Thus, $V_\tau(k_j) > V_\tau(k_1)$ for $j > 1$ and $\tau \in \{H.L\}$. Since $V_\tau(k_2) > V_\tau(k_1)$, it follows that $V_\tau(k_3) > V_\tau(k_2)$. By this same logic, one can show that $V_\tau(k_j) > V_\tau(k_{j-1})$ for $j \leq s$.

Now consider the high quality NGO's strategy. For k_0 and k_1 , its value for deviating in a given period and choosing low effort is $V_H(k_0|L) = 0$ and $V_H(k_1|L) = f$, respectively. Thus, in both cases, the high quality NGO will choose high effort if $V_H(k_j) \geq V_H(k_j|L)$, or

$$e \leq \delta[1 - \lambda(1 - \theta)]\pi V_H(k_s) + \delta\lambda(1 - \theta)\pi V_L(k_s). \quad (9)$$

For $j > 1$,

$$V_H(k_j) = f + \delta[1 - \lambda(1 - \theta)]V_H(k_{j-1}) + \delta\lambda(1 - \theta)V_L(k_{j-1}). \quad (10)$$

Thus, the high quality NGO will choose high effort if

$$e \leq \delta[1 - \lambda(1 - \theta)]\pi[V_H(k_s) - V_H(k_{j-1})] + \delta\lambda(1 - \theta)\pi[V_L(k_s) - V_L(k_{j-1})]. \quad (11)$$

Since $V_\tau(k_j) > V_\tau(k_{j-1})$ for $j \leq s$ and $\tau \in \{H.L\}$, the right hand side of (11) is always positive and decreasing in j . Thus, if the high quality NGO will prefer to choose high effort in k_s , it will choose high effort in all other states. Thus, the high quality NGO will choose high effort if $e \leq e^*$, where

$$e^* = \delta[1 - \lambda(1 - \theta)]\pi[V_H(k_s) - V_H(k_{s-1})] + \delta\lambda(1 - \theta)\pi[V_L(k_s) - V_L(k_{s-1})] > 0. \quad (12)$$

□

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