

CONSULTATION DRAFT

# **The Economics and Governance of Non Governmental Organizations (NGOs) in Bangladesh**

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## ABBREVIATIONS AND ACRONYMS

ABC	Assessment of Basic Competency	FIVDB	Friends in Village Development Bangladesh
ADAB	Association of Development Agencies in Bangladesh	FNB	Federation of NGOs in Bangladesh
ADB	Asian Development Bank	GDP	Gross Domestic Product
ADP	Annual Development Program	GK	Gonoshasthaya Kendra
AIDS	Acquired Immune Deficiency Syndrome	GOB	Government of Bangladesh
ASA	Association for Social Advancement	GSS	Gono Shahajjo Sangstha
ASK	Ain o Shalish Kendra	HEED	Health Education and Economic Development
BAAC	Bank of Agriculture and Agricultural Cooperatives	HIES	Household Income and Expenditure Survey
BAS	Bangladesh Accounting Standards	HSC	Higher Secondary Certificate
BEI	Bangladesh Enterprise Institute	IAS	International Accounting Standards
BLAST	Bangladesh Legal Aid and Services Trust	ICAB	Institute of Chartered Accountants of Bangladesh
BPHC	Bangladesh Population and Health Consortium	IDA	International Development Association
CAMPE	Campaign for Popular Education	IDCOL	Infrastructure Development Company Limited
CBO	Community-Based Organization	IDF	Integrated Development Foundation
CCC	Committee of Concerned Citizens	IGVGD	Income Generation for Vulnerable Group Development
CCDB	Christian Commission for Development in Bangladesh	INFEP	Integrated Non-Formal Education Project
CDF	Credit and Development Forum	IRDP	Integrated Rural Development Project
CGAP	Consultative Group to Assist the Poorest	MDG	Millennium Development Goals
CHT	Chittagong Hill Tracts	MFI	Micro Finance Institution
CIDA	Canadian International Development Agency	MIS	Management Information System
DAM	Dhaka Ahsania Mission	MOHFW	Ministry of Health and Family Welfare
DANIDA	Danish International Development Assistance	MOLGRD	Ministry of Local Government and Rural Development
DFID	Department for International Development	MoU	Memorandum of Understanding
DNFE	Department of Non Formal Education	MRRU	Micro-credit Research and Reference Center
DSW	Department of Social Welfare	NCB	Nationalized Commercial Bank
EC	European Commission	NFE	Non Formal Education
ERD	Economic Relations Division	NFPE	Non Formal Primary Education
ESP	Educational Support Program	NGO	Non-Governmental Organization
EU	European Union	NGOAB	NGO Affairs Bureau
FCR	Foreign Contributions (Regulation) Ordinance	NHA	National Health Accounts
FEMA	Fair Election Monitoring Alliance	NSDP	NGO Service Delivery Program
ODA	Official Development Assistance	SHS	Solar Energy Home Systems
ORT	Oral Rehydration Therapy	SIDA	Swedish International Development Agency
PBO	Public Benefit Organization	SRO	Self Regulatory Organization
PCP	Pakistan Centre for Philanthropy	SSC	Secondary School Certificate

PIL	Public Interest Litigation	TB	Tuberculosis
PKSF	Palli Karma-Sahayak Foundation	TIB	Transparency International Bangladesh
PO	Partner Organization	TMSS	Thengamara Mohila Sabuj Sangha
PRSP	Poverty Reduction Strategy Paper	UCEP	Underprivileged Children's Educational Program
RDRS	Rangpur Dinajpur Rural Service	UPHCP	Urban Primary Health Care Project
REB	Rural Electrification Board	USAID	US Agency for International Development
RJSC	Registrar of Joint Stock Companies	VGD	Vulnerable Group Development
ROSC	Reaching Out of School Children	VHSS	Voluntary Health Services Society
SDC	Swiss Development Corporation	WDR	World Development Report
SEC	Securities and Exchange Commission	WFP	World Food Program

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# Executive Summary

Progress on a range of social indicators in Bangladesh over the last fifteen years has been striking in certain areas, and widely credited to the country's pluralist service provision regime. The services of Non Governmental Organizations (NGOs) have grown significantly during this period and they have shown that it is possible to scale up innovative anti-poverty experiments into nationwide programs. Notable innovations that were expanded include delivering credit to the previously 'unbankable poor', developing a non-formal education program to cater to poor children, particularly girls, and the use of thousands of village based community health workers providing doorstep services, in partnership with Government. The fact that poor women constitute a large proportion of NGO beneficiaries, despite the persistence of strong patriarchal norms, also testifies to institutional innovation. The unique nature of Bangladesh's NGOs is not confined to the delivery of social services and pro-poor advocacy. NGOs have developed commercial ventures in order to link poor producers with input and output markets as well as to develop a source of internally generated revenue. As we look forward, the draft Poverty Reduction Strategy Paper (PRSP) views the role of NGOs as an integral part to achieving national poverty reduction targets, particularly through delivering and facilitating pro-poor services.

However, the rapid growth and diversification of the NGO sector have also given rise to questions and concerns. These include the viability of the regulatory framework developed when the size and scope of NGOs was far more limited; the appropriate political and commercial spaces for NGO activities; trade-offs between NGO sustainability and pro-poor orientation; the impact and quality of NGO services as they have scaled up; NGO corporate governance; and the implications of different Government-NGO partnerships. There has been little systematic review of the public policy implications of the changing character of NGOs in Bangladesh and the present report seeks to contribute to this effort.

The questions that we explore and the structure of the report are as follows. The first part of the report presents the Bangladesh context, the current debates surrounding NGOs and an analytical framework that can help analyze these issues. We then turn to the question of what NGOs do, who they cater to, how their programs and expenditures differ from other providers and what has been the impact of their programs on individual, household and community welfare. Given the diverse services that are provided we choose to limit our analysis to three key services – micro-credit, education and health – as well as to advocacy activities.

The report then takes a close look at issues relating to financing NGO activities through donor support, Government contracts, private donations, micro-finance income and commercial activities. The basic questions that are addressed relate to the relative importance of these various sources of income, the implications of changing trends in financing and what this implies for the nature of NGO activity in the medium term. We then assess the status of the legal and regulatory framework relating it to the scope of activities and financing trends discussed earlier. As part of this an assessment of the state of financial accountability and corporate governance in the NGO sector is presented. The main questions that are asked relate to the extent that current legislations need updating, whether the institutional structures overseeing this legislation require reform and the extent that NGOs are following best practice norms in internal governance and accountability. The

final chapter uses the analysis from the earlier work to focus on the question of whether NGOs should expand or diversify their programs, whether they have the capacity to do so and what is required from all stakeholders so that any change in direction maximizes the benefits to the poor.

### **A framework for analyzing NGO activity**

The NGO sector and individual organizations within it stand out by virtue of their scale. There are an estimated 2000 or so development NGOs in Bangladesh and a small group are among the largest such organizations in the world. These big NGOs – BRAC, ASA and Proshika – have nationwide programs, with tens of thousands of employees and multi-million dollar budgets. Most NGOs are small and have limited managerial and staff capacity. For instance in a sample of 720 NGOs, 90% had programs in less than five (out of 64) districts and only three NGOs had programs in more than 200 (out of 507) sub-districts.

An assessment of NGOs requires a framework for analyzing how NGOs can contribute to improving services to the poor. We use a framework that centers around: (i) the characteristics of services provided by NGOs (ii) the accountability relationship between policymakers, providers and service-users and (iii) the overall national context for both public and private pro-poor service delivery<sup>1</sup>. We assess the characteristics of services provided by NGOs using public economics tools. To the extent possible we assess the rationale for NGO provision on equity and effectiveness grounds, using information on expenditure patterns, success in targeting the poor and indicators of impact.

Relations of accountability between the main actors - poor service users, policymakers and service providers - ultimately determine the quality of services. In theory, service users may influence public service quality through their political power over policymakers, with NGOs helping by amplifying the voice of poor service-users through advocacy activities. However when donors fund NGOs to directly provide services this may weaken mechanisms of accountability between policymakers and providers. The merits and drawbacks of different donor financing methods are assessed in this light. The increasing prominence of NGO services reflects their comparative advantage in bringing services directly to poor users. However it also highlights the need for a closer look at the conditions for accountability by NGOs to beneficiaries - conditions which cannot be taken for granted, as we discuss later.

We find that the overall national context for pro-poor service provision is mixed. There are many successful examples of impressive service delivery outcomes in Bangladesh. As discussed earlier they have resulted from the pluralist service provision system comprising Government, NGOs and the private sector. At the same time there are certain clear areas for improvement in both the private and public sectors. The private sector in services such as education, health and banking have rudimentary corporate governance arrangements, are overseen by an over-stretched regulatory framework and in many cases are linked to the politics of the country. Increasingly progressive public spending allocations in Bangladesh have been diluted by weaknesses in public sector service delivery. The analysis of NGO activities, their corporate governance and financing arrangements need to be considered in light of this more general framework of service provision in Bangladesh as a relative benchmark of NGO activities. At the same time the importance of the space made for NGO activity by successive Governments of Bangladesh is often underplayed. In

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<sup>1</sup> These themes are adapted from the World Development Report 2004, *Making Services Work for the Poor*



comparative, and certainly regional, perspective, public policy towards NGOs in Bangladesh has been unusually successful in balancing the need for official oversight with the operational autonomy necessary for NGOs to operate and innovate. However, the recent souring of the relationship between Government and a few NGOs suggests that the political space for NGO service provision and advocacy activities cannot be taken for granted.

### **Key activities and their impact: an assessment of NGO performance**

NGOs provide a strikingly homogenous set of services, with credit dominating. A survey of three hundred NGO branches in 2003 show that while the total range of NGO interventions is wide<sup>2</sup> the typical NGO branch provides between three to four services. Around 90 per cent of all NGO branch offices<sup>3</sup> provide credit services, followed by health (56 per cent), sanitation (52 per cent) and education (45 per cent). A parallel community survey conducted as part of the 2003 NGO survey shows that the service delivery priorities identified by communities match closely with what is provided by NGOs. Advocacy and public awareness work are also common areas of NGO work: 93 per cent reported awareness-raising activities, usually relating to sanitation, health and social issues, while 42 per cent of NGO branches reported having lobbied local or national Government over the previous year. We now turn to the assessment of three key services; micro-credit, health and education, as well as advocacy activities.

#### *Micro-credit*

One of the main reasons for the growing presence of NGO programs is due to the expansion in micro-finance. Micro-credit now reaches as many as 37 per cent of all Bangladeshi households and around 60 per cent of poor households. The sector is dominated by the Grameen Bank<sup>4</sup>, BRAC, ASA and Proshika, who between them lend to 76 per cent of all borrowers.

Micro-credit generally succeeds in reaching the poor, though there are several geographical pockets of poverty where micro-credit coverage is relatively low. Contrary to popular perceptions there are significant numbers of the poorest who are micro-credit group members though the scaling up of successful experiments targeting financing services to the extreme poor will lead to even greater participation. The impact of micro-credit on smoothing incomes and reducing household vulnerability to seasonal and other shocks is of critical importance to the rural poor. Improvements in key social indicators of wellbeing are also associated with micro-credit borrowing most notably measures of female empowerment, children's schooling and health status. These social gains are also associated with the complementary social mobilization, training and awareness raising activities that typically go hand in hand with micro-credit. While micro-credit has brought benefits to borrowing households, these have not been large enough to have had a significant impact on community level employment creation and growth. The strong emphasis on financial sustainability, vital to the sector's success, has led to controversy about purportedly high interest rates. The

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<sup>2</sup> Aside from micro-credit, education and health, NGOs provide many other services. These include the provision of safety net programs, agricultural extension, social forestry, disaster management, skill training and so on, many in partnership with both central and local Government.

<sup>3</sup> This ratio is expressed as a percentage of NGO *branches* compiled by the World Bank in a nationally representative survey in 2003. Since the branches of the large organizations all provide micro-credit, over 92% of branches surveyed provide micro-credit.

<sup>4</sup> The Grameen Bank is registered as a specialized bank and is not a NGO. However its credit delivery model has been replicated largely by the NGO sector in Bangladesh and as such Grameen's experiences are often included in a discussion on NGOs.

comparative under-regulation of micro-finance also poses clear risks. We discuss both these issues in greater detail below.

##### *Health*

NGOs use village based community health workers to provide door to door health services, mainly focusing on preventative care and simple curative care targeted at women and children. While a nationwide network of these NGO para-professionals succeed in extending health care to large numbers of poor households, NGO facility based care is relatively sparse. Hence while expenditures by NGOs on health grew significantly since the mid-nineties they constitute about one-third of public sector expenditures and less than 10 percent of total health expenditures (that includes household spending on private care). NGOs also contribute to health outcomes by providing water and sanitation services, with notable successes in community-based programs involving behavioral change. Achievements in health include programs on child nutrition and tuberculosis treatment, in partnership with Government.

The impact of NGO interventions on a range of health and nutritional indicators is striking. Cure rates averaged 85% in the tuberculosis program, malnutrition rates dropped by around 20% among the poor due to the presence of NGOs in the community and neo-natal mortality among NGO clients has been found to be significantly lower when compared with a control group of households.

##### *Education*

About 1.5 million children - around eight per cent of primary enrolment - are in NGO schools, most in non-formal primary schools for which the sector is best known. The NGO education sector is highly skewed with one large NGO, BRAC, receiving around three-fourths of donor resources with a similar share of primary enrolment. BRAC also franchises its model by sub-contracting two hundred small NGOs to deliver non-formal education programs.

Incidence analysis comparing different providers of primary schooling show that NGO education programs are effectively targeted to the poor, and to poor girls, in particular. NGO schools impact positively on school enrolment and achievement, particularly of girls, and record higher attendance and completion rates than formal schools. Educational achievements tell a more mixed story: NGO school students perform considerably better than their formal school counterparts in terms of reading and writing skills, but only slightly better on basic competencies.

A key concern is that the coordination between Government and NGO education programs is weak. There is little official recognition of NGO education programs, which continue to depend largely on external grants. One obstacle in increasing NGO-Government collaboration in education is that contracting arrangements have had a long history of being problematic (see below for a more detailed discussion). The recent diversification into pre-primary and secondary education programs by the market-leader, BRAC, could lead to other NGOs following suit with prospects for improved collaboration with Government in future.

### *Advocacy*

The advocacy activities of NGOs have become somewhat controversial. Most NGO advocacy focuses on issues affecting the poor, and is seen as fully legitimate (e.g. violence against women, dowry, land rights, access to justice, housing, education). However, recently a few NGOs were accused of stretching their advocacy work into partisan political activity and electioneering, and funding for their service delivery programs was sequestered as a result. As Government funding for NGO services grows in importance, NGOs are less likely to want to antagonize Government. Hence the more prominent advocacy-oriented NGOs tend to be involved only slightly in direct service activities, and large, multi-activity NGOs tend to avoid issues that could seriously antagonize Government. Nevertheless even without taking on contentious issues such as human rights and electoral reform, there are plenty of low-key advocacy activities that multi-activity NGOs engage in that are of significant benefit to the poor (e.g. RDRS's campaigns on violence against women and promoting access to resources by the poor).

Advocacy fulfils an essential function in a democracy such as Bangladesh, and must be given space. Therefore, NGOs' scope to do advocacy should be entirely unconstrained, excepting what is partisan in nature. One option could be for NGOs to separate their advocacy and service provider activities by undertaking them through separate legal entities, which would allow financing strategies to be appropriately tailored for each activity. Returning to the analytical framework we find that the role of NGOs in strengthening relations of accountability between policymakers, and poor service-users has been mixed, as NGO advocacy efforts are to an extent constrained by their dependence on Government. NGOs have had more success bridging the gap between service-users and providers in Bangladesh through their own services and by facilitating Government, community and private sector provision.

### **Financing NGOs: trends and prospects**

The share of aid going to NGOs has risen sharply. We estimate that **total aid** to NGOs rose from an average of \$232 million (0.7% of GDP) between 1990-95 to \$326 million (0.7% of GDP) between 1996-2004 while total aid to Bangladesh fell from an annual average of \$1.62 billion (4.9% of GDP) to \$1.35 billion (2.9% of GDP) during this period. As a result the share of aid to NGOs as a portion of total aid to Bangladesh has risen from 14.4% in the first half of the nineties to 24.5% since then. These figures include our estimates of aid to NGOs from multilateral development agency loans, typically through Annual Development Programme (ADP) projects that contract NGOs. Our estimates suggest that on average 20% of aid, averaging around \$77 million a year, that is provided to NGOs comes through Government from lending agencies.

There are a number of ways through which donors provide direct financing to NGOs in Bangladesh. The most common is funding for specific projects. Where financing needs are large, donor funds may be pooled and a donor-liaison function introduced, to coordinate support and reduce transaction costs for the NGO. In a few cases donors have financed the whole range of NGO activities and there are examples where the institution develops into a different legal entity by the end of the funding period. However experience with this type of financing has been mixed and in recent years there appears to be a renewed preference for financing individual projects. Moreover the recognition that partnerships with smaller NGOs carry high transaction costs has increased reliance on wholesale vehicles, in which an agency manages a pool of money for which smaller NGOs compete.

**Financing of NGOs through the Government budget** improves the comprehensiveness of the fiscal framework and the quality of public policy choices. However the manner by which this service delivery partnership is managed matters a lot, as Government-NGO contracting has not escaped the governance problems associated with public procurement in general: absence of transparency, bribes associated with contract awards, delays and rent-seeking, and emergence of fake, and ‘fly by night’ NGOs in collusion with the contracting ministry. The successful contracting practices of the micro-credit apex body, PKSF, and IDCOL - agencies with substantial professional capacity and autonomy - should be mainstreamed throughout government. These include strict eligibility criteria, transparent guidelines for NGO selection, and monitoring mechanisms to assess performance. Successful contracting of NGOs typically also includes competitive bidding with transparent, time-bound application and approval processes. The newly-established NGO Foundation should adopt and adhere to such best practices. A system for certifying NGOs would help improve partnerships and contracting arrangements (see discussion on certification bodies below).

Around 70% of **private charitable contributions** in Bangladesh go to religious institutions, with educational establishments (15 percent) a distant second followed by recreational events. Development NGOs that are the focus of this report do not feature prominently among the list of local donations. The new provision for tax deductions for charitable contributions introduced in the 2005 Budget may increase resources going to development NGOs. The certification process for tax deductions could be devolved to an independent professional body. Lessons may be drawn from the Pakistan Centre for Philanthropy’s certification program and from the Philippine Council for NGO Certification. In both countries the Ministry of Finance has devolved certification for tax purposes to these bodies.

NGOs’ internally generated funds are mainly their net **income from micro-credit** operations; several NGOs also generate surpluses from commercial activities (see below). We find that by and large, micro-finance operations are cost-efficient relative to international comparators. Analysis of NGOs of varying sizes suggests that on the whole most micro-finance programs are financially sustainable. ASA stands out as the industry’s most profitable micro-credit operation, largely because of its cost-efficiency but also because of higher average loan sizes. Profits are used for further expansion of micro-credit and to subsidize access by the poorest.

Projections show that the micro-credit market is not saturated and that interest income is likely to grow. However careful attention will need to be paid to portfolio quality as competition for borrowers intensifies. Growing financial sustainability has meant declining dependence on donor funding, and the bulk of revolving loan funds are now from client savings and micro-credit surpluses. PKSF is an important source of finance but NGOs are increasingly exploring ways to reduce their dependence after PKSF directed that any NGO that it lends to should charge no more than 12.5 percent interest. NGOs’ access to commercial funds is limited at present, but should be a goal for those with successful micro-finance programs. Independent credit ratings of micro-finance institutions, disclosure and benchmarking of performance indicators and a regulatory framework that allows equity investments in micro-finance programs will pave the way.

Several NGOs have established **commercial enterprises** whose profit stream is earmarked to support their development programs. This “endowment model” is designed to reduce dependence on donor and other outside funding sources, and is an innovative solution characteristic

of foundations and charities elsewhere. A further innovation is the NGOs' role as 'social venture capitalists,' developing 'frontier' markets with commercial ventures such as Grameen Phone. As incorporated businesses, they should pay taxes to the extent that their profits are not ploughed back into developmental activities of the parent NGO. Our analysis indicates that the profitability of NGO enterprises varies, and larger NGOs tend to have the edge. The current market share of most NGO businesses is small, with some notable exceptions. Overall, NGO businesses that are separately incorporated from their social programs perform better, because separation allows for greater specialisation, more strategic business planning and improved governance. This will provide greater transparency and create a level playing field with the private sector.

Looking ahead the sources of financing for NGOs will vary according to the type of activity the NGO is engaged in. The increasingly mature micro-finance industry can sustain much of its activity from self-generated funds and market borrowing. Education and health services in the medium run are best financed by the Government budget to ensure greater cohesion with public services. However the benefits of greater financing of NGO social services through the Budget must be weighed against the risks. These include increasing dependence on Government and the potential for conflict to arise from advocacy work that challenges official policy. The second risk is that poor contracting procedures may lead to poor quality NGOs being selected and unsatisfactory development outcomes.

A common theme that emerges from the discussion on the various types of financing for NGOs is that there is a need for regulatory reform and financial accountability improvements. We find that fiduciary weaknesses within several NGOs and the lack of a certification system that distinguishes reliable NGOs from 'fly-by night' entities are key constraints to a proven service delivery model. The potential to access commercial sources of financing for micro-finance programs is also partly impeded by the lack of a modern regulatory framework overseeing this growing sector and the lack of a rating agency or certification body. Profits from commercial ventures cause resentment among the private sector and Government due to the lack of clarity with tax laws and the use of profits. As such there is a clear need to strengthen the regulations, the regulators and financial accountability requirements for the modern NGO sector – issues that we turn to next.

### **The regulatory framework and financial accountability**

The legal framework relating to NGOs is obsolete with an over-abundance of laws and official agencies with limited capacity. The NGO Affairs Bureau (NGOAB) is widely recognized as the primary regulator of development NGOs, administering the laws relating to foreign donations<sup>5</sup>. Staffing at NGOAB has barely changed since 1990 even though the number of NGOs it is meant to oversee has tripled – delays are common, financial reports are not scrutinized adequately and basic data relating to foreign-funded NGOs are not maintained systematically. Of the twelve laws for registering and regulating NGOs, most NGOs register under the Voluntary Social Welfare Agencies (Registration and Control) Ordinance, 1961, administered by the Ministry of Social Welfare. The Registrar of Joint Stock Companies registers Societies and Non-Profit Companies but capacity in this agency is also extremely weak - the absence of computerized systems makes it difficult to verify which organizations have submitted audited financial reports or even the number of not-for-profit companies. There are other weaknesses with the legislative framework. Tax exemptions are

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<sup>5</sup> The Foreign Donations Regulation Ordinance of 1977 and the Foreign Contributions Ordinance of 1982.

increasingly complicated by NGO commercial activity to fund development programs. Appropriate appeals procedures and mechanisms for merger or exit of NGOs are also absent.

Laws relating to internal governance and financial accountability of NGOs are inadequate. The reporting and accounting burdens placed on NGOs are contradictory, and weak capacity means regulators present a feeble deterrent against cases of poor internal governance. Capacity and computerized accounting systems vary and are related to the size of the NGO. PKSF introduced some standardized financial management practices for micro-finance programs, but accounting and auditing practices are also influenced by highly variable donor financial reporting requirements, that typically focus on the donor-financed project rather than on the whole institution. The quality of audit reports varies significantly and regulators rarely focus on the comprehensiveness and quality of these reports. There is little oversight over NGO audit standards within the profession. Moreover, audit reports are rarely posted in public spaces (such as on relevant websites). NGO Boards suffer from weaknesses common in the for-profit corporate sector and typically feature the founder-director, family members and a number of over-stretched individuals who rarely rotate their positions.

As the regulatory framework for NGOs is modernized, a first principle should be maintaining –or better, enhancing -- the space given to NGOs to innovate and scale up their activities. Regulations should be ‘facilitative’, and excessive or poorly designed regulation must be avoided at all costs. Further, regulatory focus should change from government micro-management of NGOs’ foreign funds to support for better corporate governance, strengthened accountability and transparency by NGOs. Relevant regulations need to be harmonized to incorporate standardized requirements relating to corporate governance, financial disclosure and accountability to regulatory agencies. Other necessary modifications include changes to reflect the contemporary scope of NGO activities, such as NGOs with commercial ventures, and simplify registration. New laws should define NGOs as ‘Public Benefit Organizations (PBOs), merging dated definitions of ‘social welfare agency’ and ‘organization involved in voluntary activity’ to focus on organizational purposes and activities. It is also necessary to modernize the laws governing micro-credit activities. A tiered regulatory structure that focussed mainly on large deposit-taking institutions appears appropriate.

The composition, tenure and functions of NGO Boards need to be strengthened and apex bodies can play a key role in fostering consensus on these issues. Uniform accounting standards are also necessary for the whole sector. The value of audit reports can be improved by setting up an oversight system to monitor the quality of audits through the proposed Financial Reporting Council. Public perceptions about the transparency of NGOs would be improved if financial disclosure was strengthened, by ensuring uniform public access to NGO audit reports, for example.

Improving NGO regulation also requires addressing institutional capacity weaknesses. One option that the Government could consider is setting up an independent NGO Commission that takes over the functions of the current regulatory bodies. The Commission could be empowered to deal with the establishment of NGOs and encourage standardized reporting and disclosure practices, similar to the role played by the Securities and Exchange Commission (SEC) for listed companies. The Commission could be supported by certification bodies, licensed to rate and certify medium and small NGOs, reducing the regulatory burden of the proposed Commission. Setting up a multi-stakeholder NGO Law Reform Committee mandated to modernize legislation governing NGOs is a recommended next step.

## Scaling up through a strategic compact

There are large development challenges that remain in Bangladesh in spite of impressive progress on a number of fronts. For instance while infant mortality has declined, neo-natal mortality is proving stubbornly hard to bring down. While strides in school enrolment and gender parity in primary has been achieved, drop-out rates among the poor at the early stages of secondary school remain high. Micro-credit has reached vast numbers of poor households nationwide and yet there remain significant pockets of the country with limited access to financial services. While female empowerment indicators have undoubtedly improved due to in part to NGO activity, there remain significant social challenges confronting women in both the domestic and public sphere.

These facts demonstrate the need to improve services to the poor and to promote access to existing services. We find that NGOs continue to play a significant role in delivering pro-poor services that have a positive impact on household outcomes. However at the same time the direct provision of NGO services could be weakening the accountability link between elected central and local Government representatives and clients. Moreover the weaknesses in the regulatory framework and in financial accountability raise questions as to the fiduciary risks of further expansion. We turn to the following questions: Is further NGO growth desirable from a public policy standpoint? Do NGOs have the capacity to expand and address the development challenges described above? And how should any such growth be financed and managed?

### *Does further NGO growth make sense?*

Is NGO provision at an optimal level, or is there a case for more, less or a different mix of NGO services? What does this imply for the role of Government and accountability to clients? Once again it is useful to assess this question from a sectoral perspective prior to drawing general conclusions.

In micro-finance, we argue that Government should strengthen regulation and supervision, leaving direct provision to NGOs. Strengthening oversight over NGOs that have mobilized large amounts of savings from poor people will strengthen the accountability link between policy-maker and client. The regulatory framework and government policy should facilitate and support micro-finance NGOs to: (i) meet the needs of under-served areas (such as the north-west); (ii) scale up successful MFI experiments targeting the poorest; and (iii) gradually expand into micro-enterprise lending, paying close attention to portfolio quality. Programs for the poorest and in under-served areas may require carefully designed subsidies.

Turning to education, we find that NGO schools successfully reach the poor with quality services and we argue that there is a case for further expansion of NGO primary schools, as well as tighter focus on geographically and socially marginal groups. Where Government and NGO primary schools co-exist, a voucher system could be piloted to provide consumer choice, strengthening the short route to accountability between provider and client. Other strategic growth areas for NGOs in education are at the pre-primary level as highlighted in the PRSP, and in disseminating best practices in relation to school management practices, such as community involvement, personnel management and teaching methods. Recent examples of NGOs handing over educational assets to communities, following a period of capacity building and co-financing, is an interesting model that if successful could bring about large scale benefits.

In health, the main strength of the NGO system is the army of community health workers who provide critical awareness-raising within households as well as operating as intermediaries between Government and private facilities and poor clients. Looking ahead, the focus needs to be on second generation challenges in the health sector that could be more complex to address. To help address neo-natal mortality, NGOs could be further involved in raising awareness of post-natal care, as well as equipping community health workers to better support home deliveries. Interventions to improve stubbornly high nutritional outcomes could also be scaled up through the network of community-based health workers. A clear public good and comparative advantage of scaling up NGO activity is in communicable disease, as community health workers can promote awareness of HIV/AIDs, malaria and tuberculosis detection and cure, as has been seen in the success of the Directly Observed Therapy program.

As part of a process of re-aligning priorities the report argues that NGOs need to develop exit strategies in areas where quality services are already being provided or where they lack a comparative advantage. Looking ahead the role of NGOs in building the capacity of community groups to access resources (the RDRS model), is one that could, in the long run, bring greater benefits to a larger number of people than directly providing services.

*Is further NGO growth possible?*

The report analyzes the organizational factors underlying success in the implementation of NGO programs to date, exploring whether these provide a basis for further growth. Strong, charismatic leadership contributed to the expansion of large NGOs by providing strategic direction, attracting donor support, instilling a sense of collective purpose, and strengthening staff incentives. The challenges of succession cannot be taken lightly as loyalty towards the founding head is an important part of the unity of many NGOs. However there are encouraging signs that new managerial structures and processes are being established to smooth the transition to a new generation of leadership.

Aside from leadership skills, effective human resource management was vital in scaling-up service delivery. We argue that the relative effectiveness of NGO staff is not linked to greater altruism - nor do NGO staff enjoy better salaries and perks than Government staff though incentive systems that remunerate staff according to performance certainly help. Close monitoring and supervision, supported by the 'campus'-style living arrangements in the field, along with the ability to dismiss employees for poor performance offer the most convincing explanation of good staff performance. There are other factors as well such as investments in staff training, participatory decision-making and the satisfaction of seeing results on the ground.

Rapid growth of the NGO sector was also enabled by a 'franchising effect'; NGOs reproduced organizational structure and program design in hundreds of branches nationwide. The impact was particularly marked among micro-finance programs: a standard range of financial products permitted rapid staff recruitment and training. This model remains dominant, and the focused expansion recommended for the future will also depend on a franchising model, although the proposed areas of expansion are more complex (e.g. programs for the poorest, addressing neo-natal mortality etc) requiring stronger staff capacity. This will require greater investments in developing a solid middle management layer to oversee these more complex products. The franchise model should also strive not to stifle innovation e.g. in micro-credit and education where the



Grameen and BRAC models are so dominant.

*The strategic compact*

As we look ahead to the proposed focused scaling up there is a demonstrable need for a strategic compact between Government, NGOs, donors and clients. These actions are a combination of short to medium run measures whose combined impact will improve services to the poor and accelerate Bangladesh's progress towards achieving the Millennium Development Goals. The compact can be viewed as follows:

The main role for **Government** is in modernizing the legal and regulatory framework and ensuring effective oversight over NGO activities. As part of this it is important that all parts of Government recognize NGOs as allies in development, and accept constructive criticism as supportive of a democratic polity. Government should withdraw where NGOs have the clear edge in the delivery of certain services. As the process of decentralization evolves, local Governments can play a more active role in delivering services in partnership with NGOs. Government ought to strengthen monitoring and contracting procedures to improve the effectiveness of aid that is channeled to NGOs.

**Donors** should continue to support NGO activities in Bangladesh, both to improve pro-poor service delivery and to promote a broad-based civil society, while ensuring that they do not undermine the accountability of NGOs to Bangladeshi stakeholders. Donors should also reduce the transaction costs of their financing, harmonizing reporting requirements, upgrading financial management skills of their own staff, and retaining 'institutional memory' within their organizations. While financing social sector activities donors also need to develop a clear strategy for sustainability, as has occurred in micro-finance. This strategy ought to be developed in tandem with Government and NGOs where in the medium run the Budget progressively absorbs the costs of financing of various social sector programs. In areas such as advocacy, where the conflicts of interest with Government financing are too great, donors could work with NGOs to tap the market for greater private charitable contributions.

**NGOs** also have a large agenda if they are to continue to be effective partners in development. Priorities include the need to (i) strengthen financial management and corporate governance; (ii) scale up efforts to provide public disclosure with respect to income sources, expenditure patterns and programme information along with a public information strategy to address misconceptions about NGOs (iii) make greater efforts to align programmes with national strategies, coordinate with local and national Government officials and act as facilitators of Government, private sector and community service provision (iv) revisit strategic directions periodically based on national development needs and internal capacity constraints (v) develop a middle management layer to oversee more complex development programs.

**Clients** may also support the strategic compact using mechanisms that improve their capacity to demand and monitor services, for example, through vouchers enabling choice between public, NGO and private providers.



# Chapter 1: Introduction

**B**angladesh's achievements in poverty reduction and human development over the past three decades<sup>6</sup> have been credited in substantial part to the mix of public and private service provision, including the pioneering approaches of its development NGOs. A plural approach to poverty reduction and social service delivery in Bangladesh remains necessary because of the scale of the problem, and because of its severe and intractable nature. Acting alone, the Government of Bangladesh cannot command the resources, personnel, administrative reach or expertise necessary to maintain progress on poverty reduction. Between them, Government and NGO programs have achieved wider total coverage in terms of services for the poor, and innovative, replicable approaches to tackling poverty have been developed. Government-NGO partnerships also permit the scope for both to exploit their comparative organizational advantages to enhance service provision outcomes.

**However the rapid growth and diversification of the NGO sector have also given rise to questions and concerns.** Government is concerned about alleged NGO involvement in proscribed political activity and financial irregularities, a concern that led to a freeze on foreign funds to a prominent NGO as well as moves to tighten the regulations overseeing NGOs. Observers within and beyond the sector also acknowledge the weakness in existing regulation overseeing NGOs. The commercial private sector resists the growth of NGO commercial activities as unfair competition, while questions are raised whether this evolution constitutes an unwarranted diversion away from the focus on poverty reduction, or a justifiable strategy for achieving programme sustainability. As the volume of resources managed by the NGO sector grows so do concerns about their internal and corporate governance, including their relations of accountability with government, donors and beneficiaries. Government, NGOs and donors increasingly focus on the modalities and implications of different contracting arrangements between Government and NGOs. Questions are often raised about the coverage, impact and quality of NGO services given the increasing share of aid resources that are channelled through NGOs. This study aims to contribute to these debates.

The report is organized as follows. The next section describes the unique characteristics of the sector, setting out current debates about the role of NGOs in Bangladesh and outlining the analytical framework used in the report. Chapter Two takes a closer look at three key services provided by NGOs – micro-finance, education and health – and their advocacy role as well as summarizing the evidence on the development impact of these activities. Chapter Three reviews changes in NGO financing and their implications, focusing on donor aid, Government financing, private donations and self-financing through micro-finance surpluses and commercial enterprises. Chapter Four uses the analysis of the state of the NGO sector to examine the legal, regulatory and fiduciary issues relating to NGOs in Bangladesh. Chapter Five discusses the case for further scaling

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<sup>6</sup> The number of people below the poverty line has gone down from over 70 percent in the early 1970s to around 50 percent in 2001. Infant and child mortality have declined from 140 and 95 respectively in 1972 to about 60 and 30 in 2000 and Bangladesh is on course to meeting the MDG targets on these indicators. Gross primary enrolment increased from 72 percent in 1980 to 98 percent in 2001; significantly the share of girls in primary enrolment has increased from 37 percent to 50 percent during this period. The fertility rate has fallen from 6.3 children in 1975 to 3.3 in the mid-nineties and annual population growth at 1.5 percent per year is lower than in India and Pakistan (World Bank 2003a)

up of NGO activity in certain areas, the internal capacity implications and the role of Government, donors and clients in this process.

### 1.1 Characteristics and evolution of the Bangladesh NGO sector

**Bangladesh is unusually well-endowed with a dense and sophisticated network of development-oriented NGOs.** While other countries may have comparably-sized nonprofit or 'third' sectors, few, if any, combine the qualities of scale with secular, innovative development-orientation and focus on the poor as is found in Bangladesh. Institutional and definitional variety makes direct data-based comparison with other developing countries difficult.<sup>7</sup> However, by 2000, more than 90 per cent of rural communities had some NGO presence<sup>8</sup>. Around 13 million mainly poor women are now reached through micro-finance programs, some 8 percent of primary enrolment is provided by NGO schools, and there are nationwide health and sanitation programs that involve NGOs. Approximately 45,000 NGOs are registered with the Ministry of Social Affairs, though the vast majority are not active development NGOs that are the focus of this report (see chapter 2 for more details). Around 1882 NGOs were registered with the NGO Affairs Bureau (NGOAB) in 2004 as potential recipients of foreign funds, and we estimate there are around 2000 development NGOs currently operating in Bangladesh.<sup>9</sup>

NGOs range from tiny local groups to a small number of vast organizations which achieved unprecedented expansion in the 1990s, and now employ thousands of employees and handle multi-million dollar budgets. This small group now includes some of the largest such organizations in the world and dominates the sector, approaching government departments in terms of budgets, reach and complexity. The range of activities undertaken is wide, with NGOs known to be active in: micro-finance; health and education services; social safety net programs; agricultural extension; social forestry and environmental protection; safe water and sanitation; disaster management and relief; and legal and human rights education<sup>10</sup>. However, as we discuss in chapter two the typical NGO branch focuses on providing three or four services. Poor rural women constitute the large proportion of NGO beneficiaries. This is all the more remarkable for having been made in the context of severe, interlocking constraints of extreme poverty and the persistence of strong patriarchal norms associated with both South Asian culture and Islam, as characteristic of Bangladeshi society. While some NGOs have consistently focussed their efforts on mobilizing the poor to press their own claims on local or national Government, the sector as a whole has gained prominence in advocacy activities since the 1990s<sup>11</sup>. NGO commercial enterprises are also growing in importance, including businesses which may contribute to rural economic growth and the employment of the rural poor by linking rural and urban markets.

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<sup>7</sup> The most rigorous source of comparative data, the Johns Hopkins Comparative Nonprofit Sector Project, unfortunately does not collect data for Bangladesh. However, to the extent that comparison is possible, the data for Bangladesh suggest it boasts an unusually large number of active domestic, development-oriented NGOs. So while India boasts around one million nonprofit organizations, these include professional and caste associations and only a small proportion of the total are likely to be involved in development activities. Of Thailand's 15,000 nonprofit organizations, up to half are cremation associations, some with associated welfare activities. Only 800 urban nonprofit organizations were identified in Ghana, and most of these were unregistered; however, this figure excludes rural credit, savings and self-help associations (Salamon and Anheier 1998).

<sup>8</sup> Fruttero and Gauri 2004

<sup>9</sup> Information from the NGO Affairs Bureau, October 2004.

<sup>10</sup> Zohir 2004

<sup>11</sup> Lewis forthcoming; Stiles 2002

**Bangladesh's NGO sector is remarkable for the speed with which it grew to its present size and prominence.** While community-level welfare activity has a long history in the region<sup>12</sup> the institutionalised nonprofit sector was insignificant at the time of Independence in 1971. The leading NGOs of the present cut their organizational teeth on postwar relief activities in the 1970s. Their initially radical edge was blunted early on, as most NGOs began to prioritise service provision over 'conscientization' and mobilisation work in the 1980s. The growing focus on service delivery reflected donor preferences for a less radical model of civil society and for more emphasis on service provision, and NGOs themselves began to recognize that efforts to mobilise the poor without also providing them with economic inputs were unlikely to succeed. This shift meant that NGOs were, with some justification, viewed as aid-dependent service delivery agents supportive of the military regime through the 1980s<sup>13</sup>. It was during the late 1980s that donors began to fund NGOs on a large scale, particularly a small group which now includes the largest organizations - BRAC, the Grameen Bank (registered as a specialized Bank but sharing many characteristics of NGO service delivery), RDRS, ASA and Proshika. A new phase in NGO advocacy work began with the emergence of multi-party electoral democracy in the 1990s. By the mid-1990s, development NGOs began to build new alliances and develop new strategies for influencing and challenging official policies and practices, in collaboration with other branches of civil society.

One decisive factor in the rapid growth of the sector has undoubtedly been the availability of foreign aid: grants to NGOs averaged \$160 million annually in the first half of the nineties and has grown to about \$238 million annually since then (see table 3.1). These figures do not include the share of credit funds disbursed by lending agencies that flow through NGOs, as this is not recorded by the NGO Affairs Bureau and is therefore harder to estimate. However, estimates for this study indicate that since 1995 around \$76 million was channelled annually to development NGOs from concessional loan sources. Adding these two sources we estimate that total aid to NGOs rose from around 14 percent of total aid to Bangladesh in the first half of the nineties to around 25% since 1995. The larger NGOs are now funding a rising proportion of their development activities out of fees for services (primarily micro-credit interest income) and from the proceeds of their commercial enterprises (see Chapter Three for more details).

Population density and the availability of a good transportation infrastructure network were also important contextual factors behind the expansion in NGO services. Other institutional features linked to NGO growth are the presence of strong leadership and management skills, the development of staff incentives and monitoring systems and the in-built capacity for experimentation (see chapter five).<sup>14</sup> The regulatory regime also contributed to NGO growth as we discuss below.

### 1.1.1 The role of Government in creating a supportive environment

The importance of the space made for NGO activity by successive Bangladesh governments is often underplayed, and deserves some attention. In comparative, and certainly regional, perspective, public policy towards NGOs in Bangladesh has been unusually successful in balancing the need for official oversight with the operational autonomy necessary for NGOs to operate and

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<sup>12</sup> Hashemi 1996; Davis 2001; Lewis forthcoming

<sup>13</sup> Lewis forthcoming

<sup>14</sup> For a detailed case study of the institutional development of ASA, now one of the largest NGOs in the country, see Rutherford 1995.

## 4 ECONOMICS AND GOVERNANCE OF NGOS IN BANGLADESH

innovate. The absence of heavy-handed constraints on the NGO sector by the Government of Bangladesh has been noted to explain its more rapid growth compared to other countries<sup>15</sup>. In part this reflects the comparative simplicity of the regulatory architecture in Bangladesh: a single layer of Government in effect regulates NGOs in Bangladesh, in contrast to the situation in India and Pakistan, where the federal systems create multiple layers of Government for NGOs to negotiate<sup>16</sup>.

In the case of NGO run micro-finance programs, it is generally acknowledged that the non-intrusive policies of successive Governments of Bangladesh were instrumental to the sector's growth. Essentially NGO micro-finance programs were permitted to expand as long as they mobilized savings only from members. Instead of direct Government regulation and oversight, the autonomous apex body, PKSF has played a de facto supervisory role since the 1990s, including monitoring standard performance indicators. To date, the regulatory framework does not cover or legally mandate supervision of micro-finance activity or MFIs specifically. Also vital to the space for micro-finance activity was the stability and economic opportunities ensured by impressive macroeconomic performance over an extended period<sup>17</sup>.

The Government's fiscal policy also signals the value placed upon NGO service delivery. The apex body for micro-finance, PKSF, has received sizeable budgetary transfers over the past few years. The recent creation of the NGO Foundation and the endowment received from the Government reflects the willingness of the Government to support NGOs and acknowledge their strength. Government has included a provision for tax deductions for charitable contributions in the 2005 Budget. This is line with tax laws in many countries and has the potential of providing a significant boost to private philanthropic contributions to NGOs.

That the official environment for NGO operations was generally supportive can be seen in the existence of long-standing partnerships between Government and NGOs, some dating back over twenty years. One well-known example is that of oral rehydration therapy, used highly effectively to tackle diarrhoeal diseases in a much-studied and emulated model of development management (see chapter two). Government actors from all levels were engaged in the program, from the Secretary of Health to thana officials and Union Council representatives; even the Post Office was brought on board, using postage stamps to disseminate messages about ORT. Such long-standing collaborative arrangements may also have helped legitimize the work of NGOs in wider society, contributing to the high levels of acceptability and trust these organizations have enjoyed in Bangladesh.

The draft Bangladesh Poverty Reduction Strategy Paper (PRSP) points to the significant space provided to NGOs, a role that is considerably greater than in most other developing country PRSPs. The Bangladesh document discusses the role of NGOs in areas as varied as strengthening of agriculture, education, health, micro-finance, safety nets, nutrition, local governance, anti-corruption and access to justice<sup>18</sup>.

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<sup>15</sup> Smillie and Hailey 2001: 40 and Salamon and Anheier 1998

<sup>16</sup> Smillie and Hailey op.cit.

<sup>17</sup> Zaman 2004

<sup>18</sup> The PRSP matrix includes NGOs along with other implementing agencies in the following areas: improving agriculture extension, promoting quality seed development, improving livestock productivity, disaster management, reaching the ultra-poor, access to pre-primary, primary education and technical education, improving child, mother and reproductive health, controlling communicable and non-communicable diseases, improving mother and child nutrition, promoting local Government, tackling corruption, improving accountability and access to justice.

Anecdotal evidence suggests that NGO and Government staff appear to have developed effective working relations<sup>19</sup>. This evidence is supported by a recent survey of NGOs, in which the staff of field-based NGOs overwhelmingly report viewing both national and local Government officials as helpful in their work (see Annex figure 1.1). At higher levels, it seems that Government-NGO relations have frequently been smoothed by the close personal relationships between senior officials and NGO leaders, facilitated by their mutual membership of the close-knit national elite.<sup>20</sup> Public policymakers in Bangladesh are well-informed of the vast and intractable nature of the development challenge, as well as realistic about the capacity of Government to tackle the problem alone.<sup>21</sup>

This overall context of the Government's facilitating role for NGOs needs to be borne in mind as we turn to the next section that describes recent tensions between the Government and specific NGOs.

## 1.2 Current debates

There are a number of issues that are currently at the forefront of the public policy debate on NGOs. These include (i) perceived weaknesses in the regulatory framework and in the financial accountability of NGOs; (ii) the scope, impact and cost-effectiveness of NGO activities including the trade-offs between service delivery and advocacy; (iii) the implications of shifts in NGO financing that has resulted in greater financing through commercial activities and micro-finance revenues (iv) the nature of Government-NGO partnerships, their respective roles and contracting arrangements.

**There is consensus that gaps and weaknesses in the regulation of NGOs need to be addressed as a priority.** The organizational forms of NGOs in 2005 are very different from those for which the existing legislation was designed. The need for better external regulation and supervision is felt particularly strongly for the vast micro-finance sub-sector, which now handles around \$470 million worth of members' savings. Despite the scale of micro-finance provision in Bangladesh, the sub-sector is distinctly under-regulated when compared to other countries. The potential for financial irregularity within NGOs has also directed attention to the current state of NGO corporate governance. The need for improved external regulation was also underlined by the 2002 split in ADAB, the apex association of development NGOs in Bangladesh, which formerly played some role in self-regulation of the sector.

**Concern from within Government about alleged partisan political activity and financial irregularities has placed the need for improved regulation of NGOs on the public policy agenda.** The renewed emphasis on advocacy with respect to the state and, in some cases, on social mobilization since the 1990s has produced its own controversies, highlighting graphically how fine the line between civil society activism and partisan politics is in Bangladesh. The Government-NGO relationship has deteriorated as foreign funding of a handful of NGOs, including that of a large national NGO (Proshika), have been frozen and due to proposed amendments to regulations

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<sup>19</sup> White 1999; Goetz 2001

<sup>20</sup> Close personal relations between members of the elite have played an important role in smoothing Government-NGO relations (Hossain forthcoming). Professor Yunus of Grameen Bank admits that he has used such connections to 'overcome impossible bureaucratic hurdles' (Yunus 1999: 168), while Lewis *et al* (1994) note that in its early years, relations between the NGOAB and the NGOs were smoothed considerably by the fact that an NGOAB Director had been at university (a 'batchmate') with some NGO leaders.

<sup>21</sup> Hossain 2005

governing foreign-funded NGOs that were perceived as heavy-handed. In response to strong criticism the draft legislation has been withdrawn, pending further rounds of amendment.<sup>22</sup> In this context, the increasing prominence of NGO advocacy work has stimulated debate about the political space and limits to NGO activism.

**The public image of the sector has been affected by what is perceived as an illegitimate shift into for-profit activity.** Commercial enterprises have been established by NGOs of all sizes, though enterprises sponsored by the Grameen Bank, BRAC and Proshika are larger, in diversified sectors and therefore more visible. Diversification into profit-making activity enables such organizations to reduce their dependence on donor funds for their development programs. Certain ventures have also had clear positive developmental consequences by entering new markets (e.g. mobile phones for the rural poor) and by linking rural and urban markets. However, the entry of NGOs into for-profit activities is resisted by the commercial private sector on the grounds of unfair competition; questions are raised concerning subsidies to the equity base of NGO commercial activity, and about whether the tax exempt status of NGOs provides an implicit subsidy to their commercial operations. The growth of micro-credit and the perception that NGOs are generating large surpluses has meant increased public scrutiny and debate over the level of interest rates. These issues are linked to larger questions about whether the pursuit of financial sustainability diverts attention away from serving the poor and about the impact of micro-credit.

**The evidence on service quality levels and development impact of NGO programs remains limited.** The scale, geographical coverage and type of activities that NGOs engage is often described on an anecdotal basis or by focusing on a single institution. Claims that NGOs in Bangladesh are a ‘parallel Government’ have seldom been tested against household and other survey data that are representative nationally and that measure scale and access across a range of services. Moreover there is a paucity of well designed impact assessments of entire programs and those that exist are often not disseminated effectively outside the development and academic community.

**Government contracting of NGOs has benefits as well as costs.** The level of financing going to NGOs through Government systems has increased since the mid-nineties. This trend clearly has its benefits as the sustainability of certain programs is a function of these eventually being absorbed into the Budget. However it also poses a few challenges. One it increases the risks associated with NGO advocacy work, as organizations dependent on official financing are less likely to risk criticising Government. Second, the lure of Government contracts have attracted more ‘fly-by-night NGOs’ and tainted the image of the NGO sector. Third increasing use of NGOs to deliver public services raises issues of the role of local Government and communities in service provision and monitoring as well as accountability issues. We elaborate on these issues in the next section.

### **1.3 Assessing Service Provision for the Poor in Bangladesh: an analytical framework**

The report assesses the NGO contribution in Bangladesh using an analytical framework about how to improve service provision for the poor. This framework is based around themes developed by the World Development Report (WDR) 2004. Despite the current emphasis on context and diversity, there are some general analytical starting points from which to assess different options for service provision in developing countries. These include assessing: a) the types of

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<sup>22</sup> Newspaper reports beginning in February 11 and 14, 2004; most recently, November 2, 2004.



services provided; b) the relationships between providers, policymakers and service-users; and c) the overall national political context for public and private service provision (see Box 1.1).

### 1.3.1 *The characteristics of services*

**Analysis of the characteristics of NGO services will provide debates about the appropriate role of NGOs with empirical substance.**

The case for public intervention classically rests on the grounds that markets fail to provide enough of the services society deems desirable: public goods, goods with positive externalities, about which information is imperfect, or which contribute to equity and social justice (see Box 1.2). A case for public intervention does not mean that government necessarily provides the service: it may be more effective if government enables others to undertake provision, and then simply regulates or monitors the arrangement. The appropriate intervention depends ultimately on the capacities of the providers available, the availability of finance, and how well the resulting arrangements accommodate political goals.

Chapter Two analyzes four key NGO activities – micro-finance, education, health and advocacy - to provide a picture of the type, scale, and impact of NGO activity. This chapter adopts a ‘public finance’ approach, describing spending patterns and assessing the equity and efficiency of micro-finance, education and health services. NGO activities are discussed further in Chapter Three, which looks at NGO commercial ventures in the context of changing trends in NGO financing. The rationale for intervention is not static, making it necessary to re-visit key sectors in which market failure has prompted a role for NGOs and/or the public sector in the past. The conditions underlying the case for public intervention or NGO provision may change, as certain development targets are achieved or when the capacity of other providers – communities, local Government and the private sector – improves.

#### **Box 1.1: Eight sizes fit all: lessons from the WDR 2004**

What works to improve service provision for the poor? The many examples documented by the WDR 2004 highlight how success comes in many shapes and guises: pro-poor service provision is found in a range of contexts with no single template for success. Distilling lessons from all of this diversity, however, the WDR 2004 outlines eight sets of basic service provision arrangements which appear to deliver quality services to the poor in most contexts.

The eight sizes that ‘fit all’ depend on a number of factors: the political system, the characteristics of the service-user population, and on the difficulty of monitoring the service in question. Under pro-poor regimes whose populations have homogenous service needs, for instance, it may be best for central or local government to finance the service, while provision and regulation are contracted out (size 1) or retained by the public sector (size 2). Whether size 1 or 2 fits best will depend on how difficult it is to monitor provision.

Where service-users’ needs are more diverse, local government financing is more appropriate, with the choice of contracting out (size 3) or local government provision (size 4) again depending on the difficulty of monitoring contracts.

Where the political context does not favour pro-poor outcomes, services are more appropriately delivered in ways which strengthen the power of users over service delivery. These modes are necessarily more experimental and may involve different modes of contracting (size 5), self-monitoring provision (size 6), community control (size 7), or market-type mechanisms (size 8).

Source: World Bank 2003.

There is also a case for public intervention to involve NGOs because some services are difficult to monitor or regulate. These tend to involve ‘incomplete contracts’ - activities whose process or outcomes cannot be quantified against pre-set targets. Immunization outcomes can be measured in terms of the population covered, for example, whereas the performance of schoolteachers is less easily quantified. Under such conditions, the incentives for good service provision may not be produced within conventional bureaucratic or profit-oriented organizations. Organizations which can create internally-generated incentives to perform, such as the presumed altruism of NGO employees, may be better suited to providing such services.<sup>23</sup> We explore issues of NGO management, incentives and organizational culture in Chapter Five.

### 1.3.2 Institutional actors and relationships of accountability

An assessment of how NGOs can help improve services to the poor requires an understanding of relationships between poor service users, politicians or policymakers, and service providers. This is necessary because it is the links between these actors that create the relationships of accountability that govern service provision, and ultimately determine its quality. Accountability may be exercised through what the WDR 2004 calls the ‘long route’ – the set of relationships that connect service-users to service-providers through their links to policymakers – or the ‘short route’ - the relationships that enable users to hold service-providers directly to account. As citizens, service users may in theory influence the quality of services by using their political power as voters with respect to policymakers, but in practice this rarely results in effective influence over policy. Advocacy efforts by NGOs and other actors may help bridge this gap, and some Bangladeshi NGOs have made efforts in this direction. But as Chapter Two documents, there is well-placed skepticism about the capacity of the NGO sector to mount an effective challenge to Government in sectors where many of its members seek Government support and/or financing. Nevertheless, NGOs have helped communicate the needs of poor service-users to policymakers through the less direct ‘demonstration effect’, proving that it is possible to design services that reach the poor, and poor women in particular.

Even when citizens are able to influence policymakers, the other half of the ‘long route to

#### Box 1.2: Market failures and the case for intervention

Market failures include instances in which the kind or quantity of a service that society deems desirable is not made available through the market, making the case for public intervention.

**Public goods** are defined by two characteristics. Once produced, the consumption by one person of a public good (clean air or malaria control, for example) does not reduce its availability to others. And once produced, people cannot be prevented from consuming a public good without having paid for it.

Public intervention into service areas which are not public goods can be justified on the basis that they generate **externalities**. A positive externality is a beneficial side-effect beyond that gained by the consumer herself, which usually accrues to the wider society. But goods with positive externalities may be under-provided unless governments intervene. Immunization, for example, generates important positive benefits for the wider society. So the case for public funding for immunization is usually made on the grounds that society benefits from having more children immunized than households would be willing to pay for themselves.

Differences in access to or **imperfect information** about services can also cause market failures, for example, by encouraging people to use services at levels below that which would benefit the wider society or themselves. In such cases, government may need to intervene by regulating the service or improving access to information about its benefits, but it may not need to provide the service itself.

<sup>23</sup> Besley and Ghatak 2001

accountability' - the 'compact' between providers and policymakers - may impede service improvements. This may be because policymakers are too close to providers to regulate or monitor provision adequately, or, because educated, urban public sector employees may not be inclined to serve the needs of poor, rural communities. Solutions to these problems in a number of countries have included growing reliance on public-private partnerships. Because efficiency and quality cannot be guaranteed by mimicking market forces and must necessarily rely to some degree on trust, NGOs have tended to be favored as substitute service providers. It is conventionally assumed that NGOs have the edge on other frontline providers because they a) reach poor, remote communities; b) are more flexible, responsive and experimental; c) feature internal incentives for staff performance; and d) may be more cost-effective than other providers of services to the poor. The analysis here takes a closer look at the empirical evidence about the NGO advantage in the Bangladesh context. It is against this context that an emergent area for analysis is the increasingly important role of public-private partnerships in sub-contracting arrangements.

The 'short route' to accountability, or the relationship linking providers and users, tends to be weakest where users are socially and physically distanced from providers, as is characteristic of public sector provision in Bangladesh. But it may be strengthened where users can behave as clients exercising choice, or are empowered to participate in provision, as in forms of 'institutionalised co-provision'<sup>24</sup>. The increasing prominence of NGO services reflects their comparative advantage in bringing services directly to poor users. However it also highlights the need for a closer look at the conditions for accountability by NGOs to beneficiaries - conditions which cannot be taken for granted, and which are assessed in Chapters Two and Five. Chapter Four analyses the mechanisms and arrangements for NGO accountability to Government, donors and beneficiaries through its analysis of the regulatory, legal and fiduciary issues. Contractual relations between Government and NGOs are explored in Chapter Three. Together these provide an account of the half of the 'long route to accountability' which links policymakers and providers.

### 1.3.3 *The Political Context of Public and Private Service Provision*

**The political context for public service provision in Bangladesh is mixed.** On the positive side, Bangladesh has seen a rising share of public spending allocations going to the social sectors and to pro-poor programmes within these sectors. Yet the weakness of public sector reform efforts to enhance efficiency or to tackle the serious problem of corruption has resulted in weaknesses in delivery systems that have diluted the impact of pro-poor allocations<sup>25</sup>. The literature also suggests there may be indirect positive and negative consequences of the prominent service provision role of NGOs in the Bangladesh context. The positive side-effects of NGO services may include incentives for public sector providers to improve performance out of a competitive threat or positive example<sup>26</sup>. On the negative side, to the extent that decisions about the financing of NGO services in Bangladesh take place among donors and their NGO partners, these are divorced from national policy processes. This reduces the possibility of feedback mechanisms creating strong political coalitions in support of public services<sup>27</sup>. This raises questions about the desirability of further NGO expansion that will be dealt with in Chapter Five.

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<sup>24</sup> Joshi and Moore 2004

<sup>25</sup> World Bank 2003b

<sup>26</sup> Levisay *et al* 2003; White 1999

<sup>27</sup> Davis 2001

**The political context for NGO service provision is similarly mixed.** As discussed in section 1.1.1 successive Bangladeshi Governments have permitted and even encouraged a role for NGO service provision, in recognition of the overarching goal of poverty reduction. The space permitted NGO activities, coupled with the rising importance of Government-NGO partnerships is suggestive of a political context generally in favor of pro-poor service provision. However, the essentially voluntary character of NGO service provision means there are no official or NGO channels through which service-users may call NGO service providers to account. As is the case in other aid dependent developing countries, donors in Bangladesh frequently intervene in the compact between providers and policymakers, both through their general influence over public spending but also through their direct funding to service providers. This may cut out the role of policymakers in the compact, further reducing the scope for accountability to service-users through the 'long route'. For these reasons there may be longer-term political implications of a stronger reliance on NGO service which work to the detriment of accountability to service-users. As the report details below, recent events highlight the vulnerability of service provision arrangements which depend on the occasionally volatile relationship between NGOs and Government. Chapters Three and Five analyze how this relationship can be made less fragile with the help of a stronger legal and regulatory foundation and the development of a strategic compact between Government, donors, NGOs and clients.

**An analysis of NGO service provision needs to relate to the overall service delivery framework in Bangladesh, including that of the private sector.** There are many successful examples of impressive service delivery outcomes in Bangladesh. As discussed earlier they have resulted from the pluralist service provision system comprising Government, NGOs and the private sector. At the same time there are certain clear areas for improvement in both the public sector (discussed above) and the private sector. Private sector services in education, health and banking, have rudimentary corporate governance arrangements, are overseen by an over-stretched regulatory framework and in many cases are linked to the politics of the country. The analysis of NGO activities, their corporate governance and financing arrangements need to be considered in light of this more general framework of service provision in Bangladesh as a relative benchmark of NGO activities.

## Chapter 2: Key Activities and Their Impact: An Assessment of NGO Performance

This chapter takes a closer look at the main activities of NGOs, and their impact, in Bangladesh. It focuses on four key areas of NGO activity: micro-credit, education, health, and advocacy. The chapter provides an overview of the key issues, expenditure patterns and targeting in each of these sectors and discusses the available evidence on the impact at individual, household and community levels of these interventions.

### 2.1 Defining and classifying NGOs in Bangladesh

**The development-oriented NGOs in which we are interested here are a sub-set of a larger body of ‘non-governmental organizations’.** In Bangladesh, civil society includes (i) approximately 45,000 clubs, local-level organizations, religious organizations, foundations and development-oriented NGOs which are registered with the Department of Social Welfare (ii) national and local trade unions, professional and business associations and (iii) numerous local community-based organizations (CBOs), including savings, religious, community development or social welfare groups, many of which may be temporary and informally constituted.

**Although part of the wider body of civil society, development-oriented NGOs in Bangladesh have a distinctive set of features.** They constitute a coherent set of organizations, readily identifiable on the grounds that they feature most or all of the following (i) a tight focus on the alleviation of poverty and on disadvantaged groups, through direct delivery of services to poor people and/or advocacy and social mobilization activities aimed at improving services to, organizing or establishing the rights of the poor (ii) a formal organizational presence (eg a board or formal governing structure; institutionalized reporting and accounting procedures; legal registration with relevant authorities) (iii) receipt of foreign funds, either directly from aid donors or indirectly through contractual arrangements with Government agencies or other NGOs (iv) Bangladeshi staff and management in most cases and a predominance of professional as opposed to volunteer staff and (v) a secular orientation.

**Size matters: both the sector as a whole, and individual organizations within it, stand out because of the scale of their activities.** Taking NGO Affairs Bureau (NGOAB) and Association of Development Agencies in Bangladesh (ADAB) registration as a reasonably reliable indicator of involvement in development activity, the size of the development-oriented NGOs can be pinned down more precisely: by late 2004, 1882 NGOs were registered with the NGOAB, with around 1100-1200 receiving foreign funds.<sup>28</sup> At the same time, the 2004 list of NGOs compiled by the apex body ADAB shows around 2152 NGOs. Hence for the purposes of this study we assume there are roughly 2000 development NGOs in Bangladesh.

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<sup>28</sup> Information from NGOAB, October 2004.

**Box 2.1: World Bank Survey of NGOs in Bangladesh**

Lists from NGOAB, ADAB and of branches of larger NGOs were merged to compile a list of 6559 stand-alone NGOs, NGO headquarters offices, and NGO branches. 35 sub-districts, out of a total of 507, were selected randomly, the NGOs in each again counted, and a stratified sampling technique used to ensure sub-samples of different types of organization were included. The survey was administered in 2003 to 310 NGO branches as well as head offices of small NGOs, where these are directly involved in development work.

Two questionnaires were administered, one to the manager/ director of the field NGO, and one to a focus group in the community in which the NGO was operating. The NGO manager was asked about advocacy, and service-delivery activities; partnerships and sub-contracting arrangements; coverage, target groups, fees for services; religious orientation; staff, their qualifications and evaluation procedures; the NGOs' assets and revenues; networking with other NGOs and the organization's governance structure. The community group were asked to assess the community's needs; to list NGOs/activities in their area; to evaluate NGO activities and to compare the performance of different service providers, including local and national government, NGOs, private sector and community actors.

Amongst these development NGOs, a small group of very large NGOs stands out as having grown to unprecedented size and importance. One illustration is that out of all the branches of development NGOs compiled for the World Bank NGO survey (see Box 2.1), 40% were BRAC and ASA branches. In another sample of 720 NGOs, 90% had programs in less than five (out of 64) districts and only three NGOs had programs in more than 200 (out of 470) sub-districts. The dominance of large NGOs is even more pronounced when focusing on the micro-credit sector. There are around twelve hundred microfinance institutions (MFI), most of whom are NGOs<sup>29</sup> but the industry is dominated by four large MFIs (BRAC, Grameen, ASA and Proshika) that serve around 12.3 million or 87% percent of all clients. After the "big four", there are only ten NGOs who have more than 100,000 borrowers.

There are other ways of defining a large NGO. One review included NGOs with a large coverage but also those that may be small in size but have a significant impact on policy through advocacy work. Ten NGOs were included in this study and they accounted for 85 per cent of all donor funding to NGOs.<sup>30</sup> This sub-category of very large organizations, give the sector as a whole much of its distinctive character. BRAC, Grameen and ASA, employ tens of thousands of employees and handle multi-million dollar budgets. These big organizations, have also provided models for the programs and organizational structures and practices of other, more recent entrants. They continue to provide leadership and direction for the sector as a whole through the NGO associations, sectoral umbrella organizations and national policy arenas.

## 2.2 The range and emphasis of NGO activities

**The range of activities undertaken by the development NGO sector as a whole is wide**, including micro-finance; health and education services; social safety net programs; agricultural extension; social forestry and environmental protection; safe water and sanitation; disaster

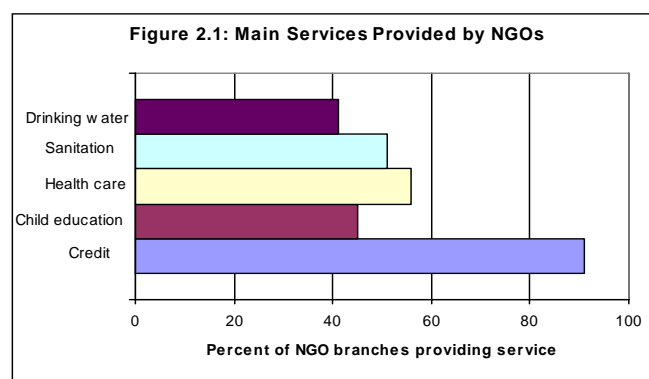
<sup>29</sup> One notable exception is the Grameen Bank which is a specialized bank.

<sup>30</sup> The review covered BRAC, ASA, Proshika, RDRS, CARITAS, TMSS, CCDDB, Buro Tangail, HEED, FIVDB and Nijera Kori. It also included data from Gonoshastha Kendra and Grameen Bank, although the latter is not technically an NGO (DFID 2000).

management and relief; and legal and human rights education<sup>31</sup>. Interventions include the provision of credit, training, inputs and support for institution-building; the provision or co-provision of schools, clinics or mobile health-related services; the training and supervision of service-providers and the design and production of teaching and training materials. Larger organizations also undertake networking, training, research, monitoring and evaluation activities. Advocacy and policy dialogue have become increasingly prominent since the 1990s<sup>32</sup>, and commercial enterprises are growing in importance.

**Clients are offered a strikingly homogenous set of services, with 92 per cent providing micro-credit.** While there are many different interventions across the sector as a whole, the types of services on offer to clients are remarkably homogeneous (see figure 2.1). The World Bank 2003 NGO survey shows that most NGOs offer between four and five different services. Credit was by far the most common activity, with around 92 per cent of all NGO branches providing it. The second most common area of service activity is in health and sanitation (slightly more than half of NGO branches) followed by the provision of child schooling and provision of clean drinking water. However, NGOs do differ in their 'product range' within these sectors as the discussions on the various sectoral interventions will illustrate. The 2003 World Bank NGO survey results also illustrates that the main services provided by NGOs are in line with the priorities of the community (table 2.1) and Annex Figure 2.1 illustrates the main methods by which communities are consulted.

**NGOs are also closely involved with advocacy** and public awareness work. In the NGO survey, 93 per cent report attempting to raise awareness about at least one issue, with the focus on sanitation, health and nutrition and 42 per cent report having been involved in advocacy or lobbying the Government over the previous year.



Source: World Bank NGO survey

**Table 2.1: Focus Group Rankings of Community Priorities May 2003**

Service	Groups that mentioned it as a priority	
Access to credit	251	81%
Health care	224	72%
Safe drinking water	210	68%
Employment Generation	182	59%
Non-formal Child Education	181	58%
Good sanitation (waste disposal)	156	50%
Agricultural training for adults	96	31%
Roads Construction/repair	87	28%
Non-Formal Adult Education	79	25%
Electricity System	69	22%
Other (specify)	49	16%
Transportation services	46	15%
Land rights/tenure	35	11%
Telephones/ other communications	13	4%

<sup>31</sup> Zohir 2004

<sup>32</sup> Lewis forthcoming; Stiles 2002

### 2.3 Who do NGOs reach and where do they operate?

**Some NGOs have responded to criticism about the sector's neglect of hard-to-reach areas and groups.** Criticisms of NGOs frequently focus on whether they reach – or even attempt to reach – marginal and very poor areas or groups. The regional imbalance of NGOs led to concerns about overlapping NGO programs and under-served pockets<sup>33</sup>. Microcredit coverage remains uneven, varying from 100 per cent of households below the poverty line in Meherpur district to only 31 per cent of poor households in Sunamganj<sup>34</sup>. The 2003 World Bank survey also shows considerable variation: while 17 thanas<sup>35</sup> have only one NGO, while Mohammadpur in central Dhaka boasts 192 NGOs. The average number of NGOs per thana across the country is 15.

Remarkably, over the 1995-2000 period, the proportion of rural Bangladeshi communities with at least one NGO program almost doubled (see figure 2.2). At the same time the average number of NGO programs within communities trebled and coverage by BRAC, Proshika, Caritas and the Grameen Bank more than doubled.<sup>36</sup> Coverage by other NGOs rose even more dramatically, but from a lower base, from 18 to 48 per cent of all communities. Credit, education and family planning services were the major areas of growth over the second half of the 1990s. Figures 3 and 4 both highlight the dominance of credit among NGO services.

New NGO activities were not necessarily located in the poorest or most deprived communities. Evidence from the 2001 census shows that the concentration of NGOs per capita was lowest in the poorest of the 35 sub-districts sampled for the World Bank NGO survey, and highest among the middle quintile<sup>37</sup>. Within sub-districts NGO concentration was highest among the second poorest quintile group, but lowest among the poorest<sup>38</sup>. While these results are to be treated with caution, as the findings of a random sample of 35 thanas, they are consistent with other research results. Micro-credit services have not necessarily been targeted to reach the poorest communities; and the poorest may even have been systematically excluded from social welfare services.<sup>39</sup>

Some NGOs have made special efforts to reach more inaccessible groups and regions. Addressing the complex constraints of remoteness, ethnic diversity and armed conflict has proved challenging, however: success in extending NGO service coverage to the Chittagong Hill Tracts, for example, has required strong donor support coupled with willingness to experiment and wait for results (see Box 2.2).

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<sup>33</sup> World Bank 1996

<sup>34</sup> PKSf 2003

<sup>35</sup> Sub-district administrative units, also known as upazilas. There are 507 upazilas in total.

<sup>36</sup> Fruttero and Gauri 2003. ASA was excluded because it would have had to have been categorised differently in the two years.

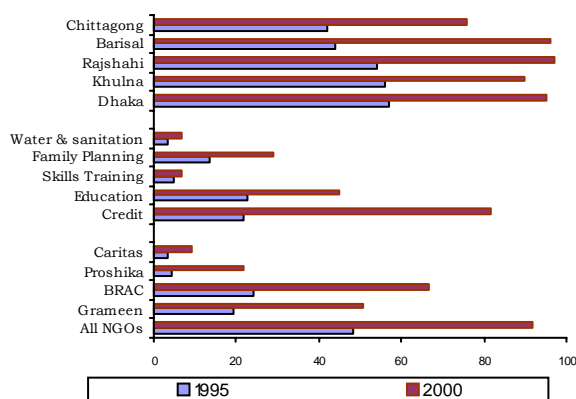
<sup>37</sup> Fruttero and Gauri *op.cit.*

<sup>38</sup> Although their location decisions may reflect targeting of the poorest within communities, a possibility that Fruttero and Gauri were unable to assess.

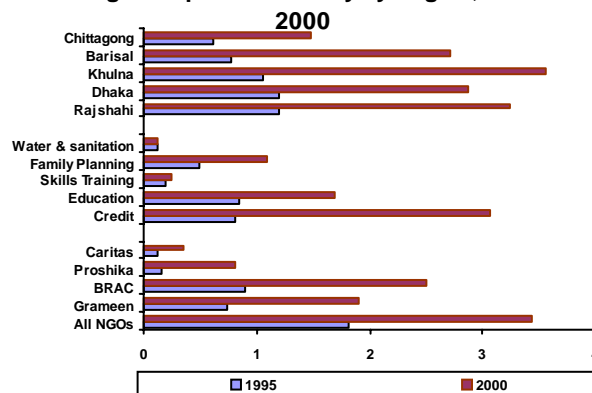
<sup>39</sup> Amin *et al* 2003; Matin and Hulme 2003, Rahman and Razzaque 2000



**Figure 2.2: Communities with at least one NGO program, 1995-2000**



**Figure 2.3: Average Number of NGO Programs per Community by Region, 1995-2000**



## 2.4. A closer look at three services

### 2.4.1 Micro-credit: facts and issues

Bangladeshi NGOs are best known for their pioneering, large-scale provision of **micro-finance services**, principally tiny collateral-free loans to poor women. Most MFIs are very small, and as table 2.2 shows, Grameen Bank, BRAC, ASA and Proshika, between them lend to 86 per cent of the 14.3 million active borrowers. In the macro context, micro-credit loans constitute around 5% of total private sector credit in the economy (see Annex table 2.1).

**Table 2.2 The Scale of Non-Government Microfinance Activity**

	Number of members (millions)	Number of active borrowers (millions)	Outstanding loan portfolio (US\$ mill)	Member savings (US\$ mill)
<b>Big Four<sup>1</sup></b>				
Grameen Bank	3.6	3.95	803.63	212.87
BRAC	4.5	4.03	237.62	118.87
ASA	2.7	2.77	196.37	46.2
Proshika	2.8	1.54	11.55	24.75
<b>Subtotal</b>	<b>13.7</b>	<b>12.29</b>	<b>1,249.18</b>	<b>402.64</b>
PKSF's other partners	1.7	1.25	46.36	39.24
Other NGO MFIs	3.9	0.8	54.64	22.19
<b>Subtotal</b>	<b>5.6</b>	<b>2.05</b>	<b>100.99</b>	<b>61.42</b>
<b>Total</b>	<b>19.3</b>	<b>14.34</b>	<b>1350.17</b>	<b>466.66</b>
Big Four as % of total	71%	86%	93%	87%

Note: 1/ Loan outstanding and member savings are cumulative figures.

Figures for the Big Four are from December 2004; figures for other NGOs are from June 2004.

The growth of the micro-finance sector took place in several stages. The origins of micro-finance can be traced to action-research undertaken in the 1970s, at a time when academics and activists were developing strategies for dealing with the post-war reconstruction needs of the new Bangladesh. The Grameen-model centering around group-based credit delivery with peer monitoring was developed by a team led by Professor Muhammad Yunus. By the 1980s, small-scale credit was recognized as an important potential means of tackling the roots of rural economic oppression, empowering poor women, and channeling resources to poor rural 'target groups' in ways that would avoid elite capture. In line with this a number of NGOs began to emphasize the delivery of services, particularly credit, and to reduce their focus on strategies of social and political mobilization.<sup>40</sup>

Through the 1980s and early 1990s, NGOs started to develop the managerial capacity, program design, and organizational features that paved the way for the expansion. NGOs opened new branches that simulated practices and organization of existing branches, a process enabled by the simple, standardized nature of the product being offered and the homogeneity and density of the population. Donors contributed to the expansion of revolving loan funds in the early 1990s, and PKSF, around the same time was established to provide wholesale financial and technical support in the sector. Expansion of the mainstream credit services continued apace through the mid 1990s, while research and experience were contributing to the diversification of the sector to meet the needs – including the non-credit needs - of different client groups. There were a number of factors underlying the success of scaling up in Bangladesh (i) strong institutions were built on the back of effective leadership, appropriate human resource management systems and established practices of experimentation and institutional learning (ii) constructive donor-client relations, including appropriately timed financial and other support; (iii) the presence of an enabling macroeconomic and a liberal regulatory environment (iv) population density, ethnic homogeneity and religious tolerance, all of which contributed to the ease and rapidity with which new practices of rural women taking loans from NGOs spread (v) the presence of a professional autonomous apex body (PKSF)<sup>41</sup>.

#### Box 2.2: Tackling poverty in remote regions: the Integrated Development Foundation

The diverse ethnic minority groups in remote, conflict-ridden Chittagong Hill Tracts (CHT) are frequently overlooked by NGOs. The Integrated Development Foundation (IDF) made it its mission to work among these communities, starting micro-credit operations with \$7,500 from the Grameen Trust in 1993. Now the largest MFI in the CHT, IDF covers 45,000 families in 1300 villages across five districts. An evaluation in 2003 found it had successfully generated additional employment and enabled loanee households to accumulate capital and enter new occupations.

Getting started was difficult. Few NGOs had been present to date and it took more than a year and the support of the Headman before initial suspicion wore off and the confidence of local people was gained. But the need for financial services was great, as interest rates on informal credit were high and the asset-less poor lacked access even to these sources. As a result, once IDF was established locally, people came from neighboring areas to participate.

An important element of IDF's success has been that donors recognized the extra constraints they faced, and proved willing to support their activities over a longer period. Swedish International Development Agency (SIDA) supported IDF in its efforts to test and expand the model over an eight-year plan. IDF has diversified its activities, and in addition to a range of financial service products is also active in health, agricultural and rural livelihood activities, housing and renewable energy, disaster management and environmental work.

Source: IDF Annual Report 2003, [www.idfbd.com](http://www.idfbd.com)

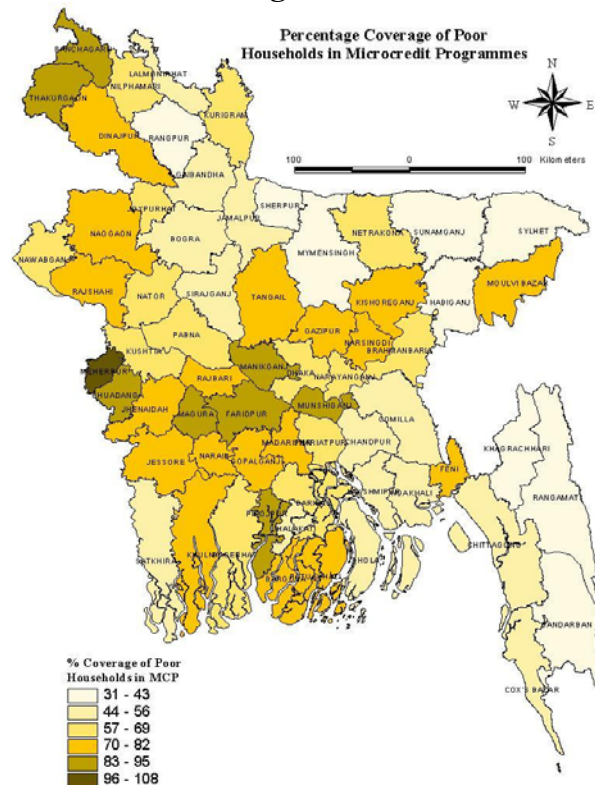
<sup>40</sup> ASA is the best known of the NGOs that made this transition (see Rutherford 1995 for a detailed account).

<sup>41</sup> More details on the determinants and impact of the scaling up of micro-credit can be found in Zaman (2004)

**Microfinance programs are reasonably successful at reaching the poor, though there are under-served pockets of highly poor districts.**

As was noted above, the micro-finance sector in Bangladesh is one of the world's largest, with around 37% of all households in the country accessing micro-credit<sup>42</sup>. However, geographical coverage is varied, with coverage thinnest in the poorer, more remote and less populous districts of the north and southwest. A recent detailed micro-credit program mapping exercise found that a significant number of highly poor districts, particularly in the north-west<sup>43</sup> have relatively few MFIs operating, and consequently a lower number of poor borrowers compared to better-off parts of Bangladesh (see figure 2.4. below). Similarly, the relatively prosperous central districts have a larger share of their population accessing micro-credit. This is not altogether surprising. Compared to a targeted safety net program such as a public works program, the extent that micro-credit can be put to good use is a function of the physical and economic endowment of their locality. Hence both the demand and supply of micro-credit is lower in these poorer areas.

**Figure 2.4**



Source: PKSf 2003

<sup>42</sup> When converting the number of clients with access to micro-credit (14.3 million) to the number of households with access, we need to take into account the number of borrowers who borrow from multiple sources and the number of households with more than one individual who borrow from micro-finance institutions. A recent survey suggests around 33% of households meet either one or both these criteria. Hence, we estimate that around 9.6 million households in Bangladesh have access to micro-credit which represents around 37 % of the total number of households in the country.

<sup>43</sup> The Nilphamari, Lalmonirhat, Rangpur, Kurigram, Gaibandha, Sherpur, Jamalpur districts in the north west all have greater than average levels of poverty. However, these districts also have a relatively lower share of micro-credit coverage measured in terms of the ratio of borrowers to population.

A large proportion of extremely-poor households, measured by initial landholding size, join microcredit programs<sup>44</sup>. For instance in the most comprehensive nationwide survey of micro-credit borrowers carried out in Bangladesh thus far, sixty percent of the sampled members have less than twenty decimals of land<sup>45</sup>. At the same time it has been estimated that certain groups of extreme-poor households do not take part in micro-credit programs due to a number of constraints (fewer income sources, worse health and education, demographic challenges etc) which dissuade them from borrowing<sup>46</sup>. The past five years has seen a number of new efforts to reach this group, by offering smaller loans sizes, more flexible repayment schedules and more intensive supervision<sup>47</sup> (see also Box 2.3).

Several studies also show that between 15-30 percent of microcredit members are from 'non-target' households measured in terms of land<sup>48</sup>. However these households are typically marginal farmers and can be considered part of the 'vulnerable non-poor' group, prone to transient bouts of poverty.

There is also evidence which suggests that households who join microcredit programs a few years after the village group has been established tend to be less poor compared to the members who join at the start of the program<sup>49</sup>. This feature of better-off households joining over time has also been noted as a general rule of thumb in many targeted anti-poverty programs worldwide<sup>50</sup>.

Another new area of expansion is in the direction of micro-enterprise lending, that is, larger loans than are usually disbursed in mainstream micro-credit, to enterprises that extend beyond the livelihood portfolio of the household. Micro-enterprise lending is not always provided to the poor, although the enterprises involved may employ poor people. New flexible savings products for the poor are also emerging, as well as various forms of insurance.

**Box 2.3: Combining financial services with social protection: the IGVGD program**

At least one major NGO program in Bangladesh has demonstrated that micro-credit can be linked to social protection programs in order to provide both the livelihood protection and the livelihood promotion functions necessary to tackle extreme poverty. Starting in 1985, BRAC has worked with the Government of Bangladesh and the World Food Program (WFP) to integrate a program of credit and training with a targeted feeding program for the very poorest households through the Income Generation for Vulnerable Group Development (IGVGD) program. At any time IGVGD covers around 200,000 beneficiaries. Extremely poor households are selected by local elected officials to receive a VGD card entitling them to receive 30kg of wheat per month over a 18 month period. BRAC provides training in poultry rearing and then micro-credit to start an income-generating activity. Evidence suggests that the IGVGD program has been highly successful in reaching the poorest and has on average had a positive impact in terms of permanent improvements in beneficiaries' incomes and assets. Hashemi (1999) shows that improvements peaked in the period immediately after the program ended, when the loss of the wheat inputs had not yet been felt; three years on, however, most households showed sustained improvements in economic status. In addition, by 2000, 66 per cent of IGVGD participants were moving into standard microfinance programs, of these around two-thirds entered the BRAC credit program, but one-third were joining other NGOs, highlighting an important 'grooming' function of the program.

<sup>44</sup> Husain 1998, Zaman 1999, Khandker 2003

<sup>45</sup> Khandker (op.cit)

<sup>46</sup> Hashemi 1997

<sup>47</sup> PKSF began a program with 19 of its partner NGOs to pilot various approaches for reaching the very poor in 2002, which by March 2004 had a combined total of more than 24,000 active clients, while by October 2004 ASA reported having 58,000 very poor clients. Grameen Bank's 'beggars' program has \_ clients with loan sizes starting as low as 500 taka (?).

<sup>48</sup> Montgomery et al 1996, Zaman 1999, Khandker 1998. It is interesting to compare this figure with Copestake's (1992) evaluation of India's Integrated Rural Development Project (IRDP) where the proportion of non poor households ranged up to 36%.

<sup>49</sup> Matin 1998

<sup>50</sup> Lipton 1996

**A focus on financial sustainability is now the norm in the industry.** A sample of 18 NGOs ranging in size and geographical presence were selected to assess the financial sustainability of their programs between 2001-2004. The analysis suggests that the sector has made impressive progress towards financial sustainability and that ASA stands out as the most cost-efficient by far. Portfolio quality has been consistent over time and remains good, partly because under PKSF rules MFIs are required to have sound approaches to provisioning for bad debts. (see table 4.2).

**There is now greater competition in the micro-credit market.** Detailed borrower-level case histories show that it is far easier to switch from one MFI to another and ‘waiting times’ for accessing credit are far shorter than a decade ago<sup>51</sup>. Complementary service provision means the larger organizations, at least, do not compete solely on the basis of price (see Box 2.4). Profits are recycled, fueling growth and providing NGOs with a cushion against the risks entailed in growth. There is, however, some cross-subsidization within micro-finance programs, so that, for example, lending to poorer groups and areas is subsidized by the profits of mainstream lending.

**Sources of MFI funding have diversified since the mid-1990s.** Dependence on donor support has declined sharply (see detailed discussion on donor trends in chapter three) and PKSF’s total contribution to revolving loan funds varies according to the size of NGO. PKSF sources average around 45% for its small clients and around 25% for its two largest clients. Members’ savings and own capital, much of it from retained profits, are increasingly important sources of financing and their share grows with the size of the NGO. For instance the share of savings in the revolving loan fund of very small NGOs is approximately 23% while for the Grameen Bank it is over 50%. These growing sources, together with the - still latent - potential for increasing access to commercial funds points towards an overall trend in MFI financing towards increasingly non-subsidized, or commercial sources of funds.

**The MFI sector remains comparatively under-regulated in international perspective.** Despite its scale and prominence, the Bangladesh micro-finance sector is comparatively under-regulated. Government, donors, and NGOs are increasingly focused on the need to develop a supportive regulatory framework with which to build a stronger micro-finance sector better able to serve the needs of more poor people. Chapter Four discusses legal and regulatory issues in more depth.

**The Government also has a number of small micro-credit programs in a range of ministries.** We estimate that there are around 800,000 such borrowers with the Bangladesh Rural

**Box 2.4. High interest rates but still a popular micro-lender: BURO, Tangail**

At 20 per cent flat, BURO Tangail’s interest rate is higher than that of any other MFI. That it managed to grow by 65-67 per cent (numbers of loans and amounts disbursed) each year over the 2000s testifies to its remarkable ability to retain and attract clients in an area where there are many competing MFIs. From its experimental origins in 1989, BURO, Tangail was different from other MFIs in that it was committed to offering open access savings to its clients and it now offers one insurance, three savings and nine credit products. Buro Tangail remains a relatively small MFI compared with Grameen, BRAC and ASA. They now plan to scale up and are actively seeking commercial sources of financing to do so. Buro Tangail’s experience shows that offering flexible financial services attracts clients, who are prepared to pay a higher price for the additional services.

Sources: BURO, Tangail (2004); Hossain (2005); Wright and Hossain (2001)

<sup>51</sup> Personal communication with Stuart Rutherford, currently conducting field research in selected Grameen Bank villages.

Development Board having the largest share. Interest rates are between 10% and 12% flat, slightly less than the average NGO rate. At the same time, it is not clear the extent that these programs target the poor and while they report repayment rates between 77% and 100%, it is not obvious how those rates are calculated. In general, these programs have treated microcredit as one of several inputs in a rural development project. Funding is provided from multiple sources with the regular department budgets covering some or all staff and operating costs, usually without any clear way of allocating costs between different functions and programs, and donor funding and annual development budget allocations covering the loan funds and some incremental costs. As a result most program managers do not know the actual cost of their microfinance programs or assess the sustainability of the programs, except to note that most programs obtain grant subventions from the Budget on an annual basis.

#### 2.4.2 *The impact of micro-credit in Bangladesh*

**Micro-credit has had a positive impact on several individual and household outcomes in Bangladesh, most clearly on consumption smoothing and social indicators.**

Analysis of a large representative survey of micro-credit borrowers, and an appropriate control group, shows that consumption *variability* is 47% lower for eligible Grameen households and 54% lower for eligible BRAC households compared to a control group. This consumption smoothing is driven by income smoothing as evidenced by the significantly lower labor supply variability experienced by micro-credit members compared to the control group<sup>52</sup>. The importance of this result cannot be over-emphasized given the fact that seasonal deficits play a key part in the poverty process in Bangladesh.

Aside from micro-credit's contribution to stabilizing incomes, there is also evidence that micro-credit, on average, raises the level of household income. A recent panel analysis of households over the 1992-98 period shows that for every 100 taka lent to a woman, household consumption (a proxy for income) increases by 8 taka<sup>53</sup>. Somewhat surprisingly, the impact appears to be greater for households who started off extremely poor (18 percentage point drop in extreme poverty in seven years) compared to moderate poor households (8.5 percentage point drop). These results differ from earlier evidence that pointed to moderate poor borrowers benefiting more than extremely poor borrowers due to the fact that the poorest have a number of constraints (fewer income sources, worse health and education etc) which prevent them from investing the loan in a high-return activity.<sup>54</sup>

There has been limited work on the aggregate poverty reduction impact of micro-credit at the local or national level in Bangladesh. The panel data discussed above has been used to show some positive externality due to micro-credit programs but that the overall spill-over benefits are somewhat limited. For instance, the net contribution of micro-credit on moderate poverty for non-participants is a small decline of 1.1 percentage points between 1991/92 and 1998/99 compared to a decline of 8.5 percentage points by borrowers in the same village. So while borrowers clearly benefit from micro-credit, non-borrowers do not gain as much from additional employment or from additional demand for their products. The impact on extreme poverty is estimated to be somewhat greater; 4.8 percentage points for non-borrowers and 18.2 percentage points for borrowers over this seven year period.

<sup>52</sup> Morduch (1999). The estimates of labour supply variability is 39-46% lower for microcredit members compared to a control group.

<sup>53</sup> Khandker (2003)

<sup>54</sup> Montgomery et al 1996, Wood and Sharif 1997, Zaman 1999

The impact of micro-credit on non-income indicators in Bangladesh is also broadly positive. There is now convincing evidence based on a representative household survey that takes into account common methodological problems such as selectivity bias, that access to micro-credit empowers females to discuss family planning issues with their spouses, leads to women taking a greater role in household decision making, having greater access to financial, economic and social resources and to greater mobility<sup>55</sup>. These findings are in line with other work on micro-credit and female empowerment in Bangladesh.<sup>56</sup> There is also clear evidence that participation in micro-credit groups leads to high child school enrolment and better health outcomes<sup>57</sup>.

The discussion on the impact of micro-credit would be incomplete without referring to the broader package of interventions that are provided with micro-credit. MFIs vary significantly in Bangladesh in terms of non-credit services though typically they include training, related business development services and social messages on education, health and civic rights. One carefully designed study finds that these non-credit interventions raise self-employment profits in rural Bangladesh by 125% while the combined impact of credit and non-credit interventions on self-employment profits is 175%<sup>58</sup>.

Turning now to the fact that the discussion above has focused exclusively on benefits without referring to costs. There has been very little cost-benefit work done in the micro-finance literature. Analysis of the Bank of Agriculture and Agricultural Cooperatives (BAAC) in Thailand concludes that “*clearly some non-zero subsidy could be justified*”.<sup>59</sup> Cost-benefit ratios for three major micro-finance programs in Bangladesh compare favorably with other safety net interventions according to one study<sup>60</sup>. Another study assesses the cost-effectiveness of the Grameen Bank and concludes that “*Grameen probably was a good investment*”.<sup>61</sup> There are a number of reasons why there is such a limited amount of evidence of cost-benefit work and why the studies cited above are somewhat tentative in their conclusions. The methodological limitations to measuring the cost-effectiveness of micro-credit are numerous, the principle ones being that program costs vary considerably depending on what stage an MFI is in their growth strategy, many benefits resulting from micro-credit are difficult to measure (e.g. change in social status) and that the benefits from borrowing has been shown to vary with time. The difficulty with measuring the discounted value of these benefits and the highly variable cost implications of an MFIs expansion strategy means that the type of cost-benefit work that is possible with building a road, for instance, is far more complex in micro-finance.

### 2.4.3 Health: facts and issues

**NGO health expenditure has expanded over the past decade but remains relatively small compared to private health spending.** NGO spending on health and nutrition activities is

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<sup>55</sup> Pitt et al 2003a

<sup>56</sup> Amin et al 1994, Hashemi et al 1996

<sup>57</sup> Khandker 1998

<sup>58</sup> McKernon (2002). Selection bias is addressed by jointly estimating program participation and profit equations and village level fixed effects are used to control for program placement bias.

<sup>59</sup> Townsend and Yaron (2001)

<sup>60</sup> Khandker (1998)

<sup>61</sup> Schreiner (2003)

nine per cent of total health expenditure and around 0.3 percent of GDP, a three-fold growth between 1996 and 2002 (see table 2.3). The bulk of total spending on health services is by households on private care (64% in 2001/02). The ratio of Government and NGO spending on health is around 3:1.

Table 2.3 The share of NGO health spending						
	1996-97	1997-98	1998-99	1999-00	2000-01	2001-02
<b>(as % of Total Health Expenditure)</b>						
Ministry of Health	27.6	28.3	27.2	25.3	23.1	23.3
NGO	2.9	3.0	4.1	6.9	8.8	9.2
Household	64.1	65.1	65.7	65.1	64.8	64.2
<b>(as % of GDP)</b>						
MOHFW	0.9	0.9	0.8	0.8	0.7	0.8
NGO	0.1	0.1	0.1	0.2	0.3	0.3
Household	2.0	2.0	2.0	2.0	2.1	2.1

Note: MOHFW = Ministry of Health and Family Welfare; HH = Households

Source: Bangladesh National Health Accounts

**Larger NGOs are becoming increasingly dominant in health.** A survey of 149 NGOs involved in health and nutrition sector activities<sup>62</sup> highlights the growing dominance of the five largest NGOs in the sector, whose spending almost doubled between 1999 and 2002, reaching 73 per cent of total NGO health sector spending<sup>63</sup>. In contrast, spending by small NGOs declined in absolute terms, from Tk 819 million (16 per cent of NGO health spending) in 1999 to Tk 486 million (6 per cent of NGO health spending) in 2002.

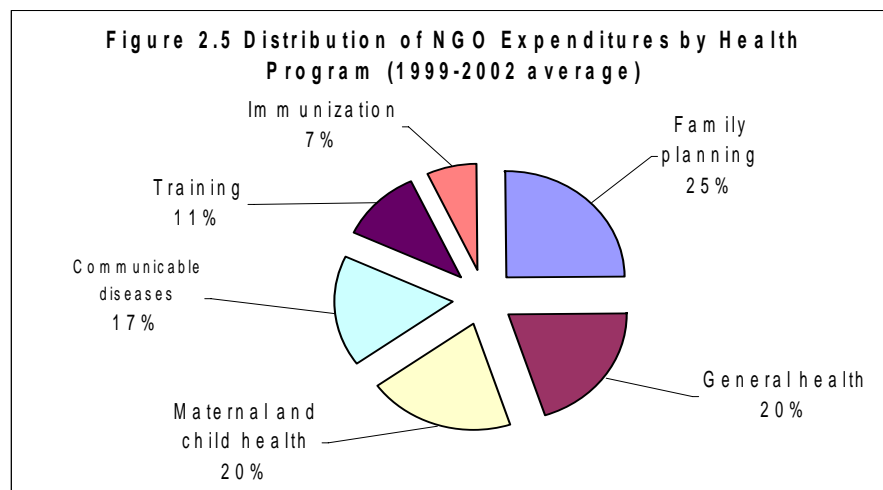
**The high burden on poor households of medical expenses in Bangladesh makes a strong case for NGO provision of health services.** Illness within poor families is a major feature of impoverishment and downward mobility. While NGO facility-based curative health services are a small proportion of such services in total, the community based health delivery approach contributes to reducing inequities by improving access for poor rural women for whom distance to health facilities is a major determinant of their use<sup>64</sup>. Spending by NGO health facilities is more progressive than in public or private facilities with the rural poor in general successfully exempted from fee payments.

<sup>62</sup> The sample was drawn from a list of NGOs surveyed under the previous 'National Health Accounts' (NHA-1) combined with a list of NGOs involved in health and nutrition activities from the health NGO umbrella organization, Voluntary Health Services Society (VHSS).

<sup>63</sup> MOHFW 2003

<sup>64</sup> see also Levisay *et al* 2003





However expenditures by public health facilities benefit the rich, surprisingly even more than those by private clinics (see table 2.4). For instance, around 32% of public health expenditures went to the top quintile compared to 27% for private facilities and 19% for NGO health facility expenditures. Family planning tops NGO health spending closely followed by general health and maternal and child health (see figure 2.5).

**Table 2.4 National Health Expenditure by Quintile**

Quintile	Public health facilities	Private health facilities	NGO health facilities
1	14.7	16.4	20.2
2	17.2	17.2	14.1
3	15.5	18.2	22.5
4	20.6	21.1	23.8
5	32.0	27.2	19.4

*Source : National Health Accounts-2*

**NGO facility based care is relatively micro in scale.** Comparisons of NGO and public sector health service provision are difficult because of differences in scale and service delivery modes. NGOs use community health workers to provide door to door services. These workers provide health education on family planning, immunization schedules, pregnancy related care, nutrition education, tuberculosis control, basic hygiene and so forth. Community health workers also provide curative care for basic health problems and refer complicated cases to local public and private health facilities (see Box 2.5 on one of the largest NGOs in the health sector - Gonoshasthaya Kendra). NGO facility based services, on the other hand, cover only a small fraction of the population. The 2000 nationwide Household Income and Expenditure Survey (HIES) found that around 4% of women obtained post-natal care from NGO facilities and that only 2% had received immunization services from NGO health centers.

**The provision of water and sanitation services by NGOs is also critical to achieving health outcomes.** Around 700 NGOs now work in the water and sanitation sector, with

international, national and small local NGOs commonly working in partnership. The policy context is strongly supportive of NGO involvement, in recognition of the scale of the need and the shortfall in present provision, as well as of NGO capacities to stimulate behavioral change and to target and supply credit to poor rural women. The two major policies on water and sanitation, the National Safe Water Supply and Sanitation Policy (1998) and the National Water Policy (1999) both encourage and support a role for NGOs. The target group approach and practices of beneficiary training and community-based group meetings have been vital for transmitting messages to rural populations about arsenic contamination, open defecation, the use of safe water, and hygiene. Another key intervention is the provision of micro-credit for sanitary latrines and shallow tubewells.

**Government-NGO collaboration is increasingly important in the health sector.** NGO involvement in the health sector has to date been principally financed by donors, although growing recognition of the potential importance of NGO involvement in the sector has led to greater linkages with Government. While direct donor support to NGOs rose in absolute terms between 1999 and 2002, the share as a proportion of the total declined from 78 to 67 per cent. This declining share reflects the sharp growth in resources channeled through Government to NGOs, which rose from 12 to 26 per cent of total funding between 1999 and 2002<sup>65</sup>.

Public-private collaboration in the health sector has taken a variety of forms and an early successful case was the National Tuberculosis Program. From 1994, the Government signed annual MoUs with BRAC and the Leprosy Coordinating Committee (an umbrella organization of health NGOs) to co-provide tuberculosis curative services through rural community health workers. Cure rates of 85 per cent were recorded, and the BRAC program was found to cure three patients for every two in the Government program. The success of this collaboration is widely recognized and attributed to the clarity with which the different roles and responsibilities of actors were identified and formulated.

Examples like the National Tuberculosis Program have demonstrated the benefits of harnessing NGOs' advantages with respect to reaching poor rural communities to achieve wider public policy goals; the Government has recently indicated its intention to collaborate further with NGOs, including by developing a 'Strategic Framework' for NGO contracting.<sup>66</sup> These new directions in public policy mark the beginnings of a process of separating the financing and provision of health services<sup>67</sup>. One implication of a larger role for NGOs in service provision thus includes the scope for improving the 'long route' to accountability to poor service-users, through the separation of policy-making and provisioning functions. Chapter three discusses the experience and future directions with NGO contracting in greater detail.

<sup>65</sup> The share of NGO funding attributed to transfers between NGOs averaged around 9 per cent during this time (MOHFW 2003).

<sup>66</sup> Prominent programs involving contracts with NGOs include the NGO Service Delivery Program (NSDP), through which 41 NGOs deliver clinical services to 22 million people across 61 districts, including communities not served by Government services; the Bangladesh Population and Health Consortium (BPHC), a DFID-support program supporting NGO community work in training, management and MIS and the Urban Primary Health Care Project (UPHCP), a predominantly ADB-supported project in which responsibility for PHC has been given to the Ministry of Local Government and Rural Development (MOLGRD) and urban primary health care centers constructed in 16 partnership areas.

For example, Forsberg and Sundewall 2004; Loevinsohn 2001; Loevinsohn and Harding 2004).

<sup>67</sup> Forsberg and Sundewall 2004

**Box 2.5: The Gonoshasthaya Kendra (GK) Story: cost-effective health care for the poor**

The GK story started during the liberation war when a group of young Bangladeshi doctors working in the UK returned home to provide health care for freedom fighters during the 1971 liberation war. After liberation, the team moved to implement their dream of providing affordable health care for rural Bangladeshis. Their approach was to cover a selected thana (or Upazilla) through a health pyramid with a hospital at the apex, health centers in each union run by paramedics and visited on a regular basis by doctors from the apex hospital and finally relying on village based community health and family planning workers. The impact of this approach is reflected in the table below, though clearly the figures below do not control for potential program placement bias. The idea behind this was to use the health pyramid effectively and reduce unit costs of health care to a level that could be sustained by the local population. Every household would pay a monthly insurance fee for full coverage plus a small co-payment of 2 taka (3 cents) for each visit. Today the system covers around one million people in rural areas and another one hundred thousand in urban areas. One original idea that had to be modified was the use of rural health insurance premiums to cover the full cost of care. Based on assessments of the ability to pay, the finding is that in rural areas about 60% can be covered by these HMO type payments. The remaining has been subsidized by GK through its revenue earning operations such as GK Pharmaceuticals.

GK Pharmaceuticals started as an effort to reduce the high cost of medicines in Bangladesh by establishing a generic drug manufacturing facility. Despite helping reducing the cost of drugs – the pharmaceuticals venture has at the same time been a profit maker and the profits have been used to finance the deficit in the health care operations. The high cost of medicines and the sale of less than useful high profit prophylactic drugs by manufacturers led to another effort spearheaded by GK which became the global precursor for the essential drugs policy. The successful efforts in Bangladesh led the WHO and others to successfully promote this in other parts of the world. GK has also spearheaded the anti-smoking movement in Bangladesh and campaigned for social equality for all. GK's recruitment policy is that at least 60% should be women at all levels.

**Vital events rates in Gonoshaysthaya Kendra (GK) areas compared with national averages, May 2004-March 2005**

	GK Area	National average
Crude death rate per thousand	3	9
Neonatal mortality per thousand live births	18	41
Post-Neonatal mortality per '000 live births	11	24
Infant Mortality per thousand live births	28	65
Maternal Mortality ratio per 100,000 live births	153	320

#### 2.4.4 The impact of NGO health programs

While no data are available with which to directly compare user satisfaction levels in Government as compared to NGO services, there is some evidence about overall satisfaction levels with each. User satisfaction with Government services appears to have declined over the 2000s, with Government services having received a rating of 'good' from 38 per cent of respondents in 1999 but only 10 per cent in 2003; meanwhile 'bad' ratings rose over the same period from 38 to 45 per cent.<sup>68</sup> A different study used an exit poll of 817 users of NGO facilities found high levels of approval of a number of aspects of the service: more than 90 per cent of clients felt that the provider had spent enough time and asked questions, for example, and were willing to recommend the facility to

<sup>68</sup> The proportion of respondents who rated private and NGO services as 'good' rose in the same period from 25 to 37 per cent. However, NGO services were not distinguished from private services and as private for-profit providers are overwhelmingly dominant in the health service market, this figure cannot be treated as evidence of rising approval ratings for NGO health services.

others<sup>69</sup>. Problems and inadequacies remain with NGO services, however as half of the NGO centers did not have a full complement of basic supplies or equipment.

Multivariate analysis using the data from the Child Nutrition Survey 2000 shows that the presence of BRAC or Grameen Bank in a village can have a significant effect on malnutrition. Results show that the presence of one of these organizations can lead to a decline of about 20 percent in moderate and severe malnutrition among the poor<sup>70</sup>, controlling for a set of other household and community factors. The explanation for this includes (i) the use of micro-credit for consumption-smoothing purposes (ii) the impact of nutritional education during weekly group meetings and (iii) the impact of nutritional supplements and education directly provided by health workers.

There is also other credible evidence that points in a similar direction. Panel data suggests that between 1992 and 1995, severe malnutrition (as measured by mid-upper-arm circumference) declined significantly for children of BRAC members compared to a control group of non-members<sup>71</sup>. Similarly the survival probability of children belonging to BRAC households is better than that for children from poor non-member households, primarily due to mortality differences in the immediate post-natal months. The same study also shows that BRAC members had a significantly higher probability (0.57) of using family planning compared to both poor non-members (0.50), as well as compared to wealthy households in the village (0.51).

Our earlier analysis refers to the impressive partnership between Government and NGOs in controlling the spread of tuberculosis. A comprehensive evaluation shows that the prevalence rates of tuberculosis cases in the program intervention sub-districts was half that in the non-programme comparison sub-districts<sup>72</sup>. One of the most important facets of tuberculosis control is detection and the role of NGO community health workers in door to door identification of potential TB cases was a key part of an effective campaign against the disease. Moreover, given the social stigma associated with the disease, there is low attendance at government health facilities and the doorstep counseling and treatment services provided by community health workers is a key part of the strategy. Other important factors cited are the regular availability of free drugs through the community health workers, the availability of sustained donor support for this program and the technical support provided by the Government to the NGO intervention.

#### 2.4.5 *Education: facts and issues*

**NGO education services are targeted to the poor.** Around 46 per cent of NGO branches in the World Bank NGO survey provide child education services, with a further 25 per cent involved in adult education<sup>73</sup>. As many as 1.5 million children, or around eight per cent of all currently enrolled primary students, are in NGO primary schools. Of these 1.2 million alone are enrolled in BRAC's network of 34,753 non-formal primary schools.<sup>74</sup> As figure 2.6 illustrates the majority of students in NGO schools are from the bottom two socio-economic quintiles in contrast to Government and other schools.

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<sup>69</sup> AHI 2004

<sup>70</sup> Deolalikar 2002

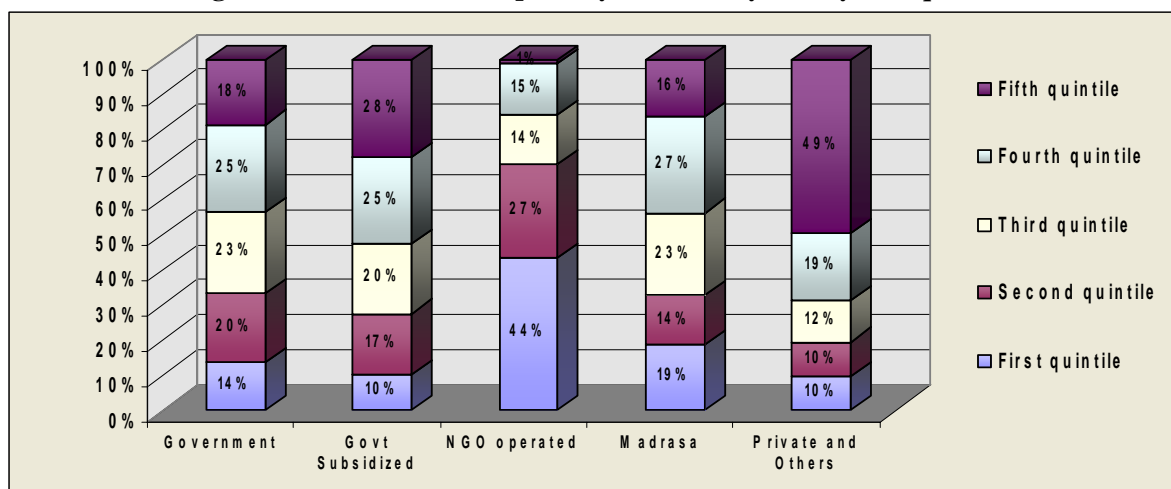
<sup>71</sup> Chowdhury and Bhuiya

<sup>72</sup> Chowdhury et al 1998

<sup>73</sup> Gauri and Galef 2004

<sup>74</sup> BRAC Annual Report 2003

Figure 2.6: Distribution of primary students by facility and quintile



Source: Authors estimates from Household Income and Expenditure Survey 2000

**The share of non-salary inputs in NGO primary school expenditure is far larger than in Government schools.** Unit costs in NGO primary schools, at around \$17 per student per year are slightly lower than in Government primary schools. Notably the composition of expenditures in NGO schools is sharply different. As table 2.5 illustrates NGO schools spend only about a half of their recurrent expenditures on teacher salaries in contrast to Government schools where the equivalent figure is 95%. This is largely due to the fact that NGO primary school teachers are less qualified and are prepared to accept a far lower salary scale<sup>75</sup>.

Table 2.5: Composition of Education Expenditure in different types of schools

Main Expenditure Item	Total Expenditure				Recurrent Expenditure			
	Govt.	Private	Madrasa	Non-Formal	Govt.	Private	Madrasa	Non-Formal
Salaries (teachers & others)	81.8	61.3	81.5	49.6	94.6	87.4	93.9	51.1
Physical facilities	12.4	27.5	11.8	0.9	-	-	-	-
Materials/Stationery	1.4	3.2	1.8	30.9	1.6	4.6	2.1	31.8
Rent	0.5	0.3	0.5	15.3	0.6	0.4	0.6	15.8
Fixed assets	1.1	2.4	1.4	2.0	-	-	-	-
Other Expenditure	2.8	5.3	3.0	1.3	3.2	7.6	3.4	1.3
<b>Total</b>	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: CAMPE, Education Watch Report, 2001.

NGOs involved in education range from large NGOs which provide nation-wide education programs and services (teacher training, materials development) to a large number of very small NGOs operating mainly at sub-district level, which provide education directly and rely heavily on

<sup>75</sup> NGO primary school teachers are paid around Tk1200 per month (World Bank NGO survey 2003) against around Tk2,700 per month in government schools, excluding benefits and allowances of around 75 percent of basic salaries. Moreover, government schools generally have teachers with longer years of service (an average of 19 years against four years in NGO schools).

the larger NGOs for financing and technical support. In between, there is a group of medium-sized NGOs which provide both education and some educational services to local-level NGOs, and which have a significant regional presence<sup>76</sup>. Annex table 2.2 provides estimates of the numbers of NGO educational centers and learners under NGO programs.

**NGO education programs in Bangladesh remain best known for their non-formal primary education programs**, which are widely understood to be high quality and cost-effective interventions which reach the poor, and in particular poor girls. Box 2.6 describes the BRAC Non Formal Primary Education (NFPE) program, by far the largest NGO education program in Bangladesh.

**Coordination between Government and NGO education programs in primary education remains weak.** NGO schools are not formally recognized in official statistics on primary education. Since the closure of the Department of Non Formal Education (DNFE) there has been no mechanism to coordinate Government-NGO activities. CAMPE, the national network of education NGOs, and the Government have attempted to coordinate the activities of NGOs involved in education<sup>77</sup>, while individual large NGOs such as BRAC and FIVDB are involved in contracting and coordinating the activities of their small partner NGOs.

**NGO education programs depend largely on donor financing.** Donor financing has been relatively stable over the last five years, and remains vital to NGO education programs (see Annex table 2.3). However, dependence on external financing leads to concerns about sustainability. The bar on funding Proshika has led to most of its schools being closed (see Box 2.8) and the GSS education program has resumed on a limited scale following the withdrawal of donor funding (see Box 4.1). Student fees and cost-recovery are rarely feasible given that NFE programs serve poorer populations and community contributions are relatively small. The most realistic option for NGOs to reduce their reliance on donor funds is through stronger relationships with the Government. However, problems with Government arrangements for contracting NGOs need to be addressed as a first step (see chapter three for more details).

**There has been a strategic shift into pre-primary and secondary education by the dominant NGO in education which has led to greater collaboration with Government.** The number of primary schools has changed little over the past decade and there appears to be growing focus on other areas. The growing number of BRAC pre-primary schools is designed to fill a gap where the State has little presence and where NGO schools are seen as important to fill this void. Children passing out of BRAC pre-primary schools are admitted into Government primary schools. In secondary education the Ministry of Education has given permission to certain NGOs to develop the capacity of secondary school teachers, school management committees and communities. This role as a facilitator of better quality education is likely to yield greater results for larger numbers of people than if NGOs focused on becoming a direct provider of post-primary education.

<sup>76</sup> Large national NGOs are essentially BRAC, Proshika, DAM, FIVDB and the smaller/regional ones include Jagarani Chakkra, BDS, CODEC, Uttaran, UCEP and Concern

<sup>77</sup> Around 700 NGOs are affiliated to the Campaign for Popular Education (CAMPE), the umbrella organization for education NGOs set up in 1991.

### Box 2.6 BRAC's Non-Formal Primary Education Program (NFPE)

BRAC's NFPE program is the biggest non-formal primary education program run by an NGO, with 34,753 centers nationwide and 1.2 million learners presently enrolled in BRAC non-formal primary schools. BRAC schools are found in more than 450 upazilas across the country, and an additional 200 small NGOs are contracted to run a further 2250 schools using its model through its Educational Support Programme (ESP). Since 1985, BRAC's NFPE program has focused on bringing non-formal primary education to the children of the poor, targeting girls in particular. The curriculum is learner-centered and includes Bangla, Mathematics and Social Studies, with English from Class 2. In 1998, the improved program was expanded to four years, covering the primary curriculum for Classes 1-5. Government textbooks are used in Classes 4 and 5. School hours cover 2.5 hours, 6 days a week, over 268 days a year.

The quality of the teaching-learning materials and the emphasis on teacher-training contribute to better educational outcomes than in other types of mass schooling in Bangladesh. Teachers are trained for 12 days initially at a residential BRAC training center, followed by monthly refresher sessions. The 30:1 pupil-teacher ratio in BRAC schools compares favourably with Government schools and contributes to effective teaching. The per student cost of BRAC schooling is about \$17 compared with around \$20 in Government primary schools. Teacher unit costs are much lower than in formal primary schools and almost 30 per cent of the NFPE budget is allocated to effective management and supervision of schools.

Along with other NGO non-formal education programs, BRAC's NFPE is credited with having helped improve the educational prospects of poor girls in Bangladesh, contributing to closing the gender gap at primary. At least 70 per cent of the students must be girls from the poorer households in the community. But girls are also encouraged to enrol by the predominance of women teachers (97 per cent of NFPE teachers are local married women) and the presence of Parent Teachers' Associations. That schools are local minimises the time and trouble of travel and timetables are set to allow for the domestic responsibilities shouldered by school-aged girls. With around 90 per cent of the some 2.6 million BRAC school graduates estimated to have entered the formal system, the system has also provided access to formal schooling for a large number of girls from poor families.

Sources: BRAC Annual Report 2003; Nath 2002; Sukontamarn 2004

#### 2.4.6 The impact of NGO education programs

**Efficiency indicators in NGO schools are noteworthy.** Attendance in NGO schools was estimated at 85% compared to 55% in Government schools. The completion rate for NGO schools tends to be higher than the average of 68 per cent in formal schools, with BRAC at 93, FIVDB at 85 and Proshika at 90 per cent. However while the transition rate from NGO primary schools to Government secondary schools is impressive, drop-out rates in the first year of secondary remain high<sup>78</sup>.

**Exposure to NGO schools has a greater impact on female enrolment relative to Government schools:** There is clear evidence that NGOs set up schools in villages where there are a higher proportion of children with no schooling – these are also villages where typically adults have lower average schooling<sup>79</sup>. After controlling for a range of individual and household level characteristics and village level fixed effects, exposure to a NGO school in a village has a greater impact on girl enrollment than for boys, while there is no gender difference for Government schools. This impact is greater for girls from poor households residing in rural areas.

<sup>78</sup> Avalos 2003

<sup>79</sup> P Sukontamarn 2004

**The impact of NGO schools on test scores is highly significant.** Test score data from the nationally representative Assessment of Basic Competency (ABC) survey of 3360 children carried out in 1998 has been used to assess the quality of education in NGO schools<sup>80</sup>. The results show that after controlling for a range of factors that could influence test scores, attending an NGO school increases both the reading and writing test scores significantly more than attending a Government school. Relative to children who have never been to school, attending an NGO school increases the scores for reading skills by 22% for girls compared to 8% if the girl child attends a Government school. The figures for writing skills are 31% for girls in NGO schools and 10% for girls in Government schools. The NGO school “premium” for boys is slightly narrower but still very striking for both reading and writing skills<sup>81</sup>.

While NGO school students achieve better educational outcomes than students of other types of school, overall achievements on a number of basic competencies are still relatively low. Only 38% of NGO school students satisfied the basic education criteria, compared with 21% in Government schools. However, more recent evidence suggests NGO school students

**Table 2.6 Literacy rate by type of school**

School type	literacy rate (class IV-V)	Literacy rate (overall primary)
Government	62	46
Private	63	33
Non-formal (NGO school)	97	60
Madrassah	65	54
All	65	45

Source: CAMPE 2003

score well in both absolute and relative terms in terms of literacy (see table 2.6)

## 2.5 NGOs and advocacy issues

**NGO advocacy activities have intensified since the return to democracy in the 1990s, presenting a more direct – but still cautious - challenge to successive Governments.** The emergence of a multiparty electoral democracy made space for the intensification of NGO advocacy work in the 1990s. NGO involvement in advocacy work in the 1970s and 1980s had been sporadic, mainly limited to the ‘demonstration effect’ or instances when their own activities highlighted the need for policy shifts. For example, Proshika’s program of providing livestock to members was suffering from the public sector monopoly on livestock vaccination in the 1970s; Proshika advocated the training and licensing of its group members as ‘para-vets’, which enabled them to break the monopoly, extend coverage, and help create new livelihoods for members.

By the late 1980s, a number of now large service delivery NGOs began to perceive service delivery goals as conflicting with their social development strategies: on the one hand, episodes of social conflict and clashes with local representatives of the state endangered programs and loan recovery; on the other, competition between NGO MFIs and pressure from donors to show results entailed reducing the emphasis on conscientization and group mobilization. The late 1980s saw the beginning of the use of Public Interest Litigation (PIL), now an important advocacy tool, to address

<sup>80</sup> Nath et al (1999) and Sukontamarn (op.cit)

<sup>81</sup> Sukontamarn op.cit



a growing range of concerns – civil liberties as well as environmental concerns, social and economic rights.

Good governance became a leading focus of NGO advocacy from the 1990s: a donor-coordinated initiative – the Development Partnership – was established to address local governance; the Fair Election Monitoring Alliance (FEMA) was set up as an independent election watchdog, in 1995; and 1996 saw the establishment of the Bangladesh chapter of Transparency International, focused on anti-corruption activities. Proshika was the earliest of the large NGOs to institutionalize its advocacy activities, with the establishment of the Institute for Development Policy Analysis and Advocacy (IDPAA) in 1994. It was not until 2002 that BRAC followed suit with its own separate advocacy unit.

Most NGO branches participate in public awareness campaigns designed to promote mass awareness of issues such as sanitation, nutrition, rights and gender (93 per cent of NGO branches according to the World Bank NGO survey). In addition, 42 per cent report lobbying national or local authorities. Of these, a higher proportion reported having met with the authorities in order to lobby for financial support for their own or other local NGOs, with only 20 per cent reporting their lobbying goals as including policy change. This suggests that NGO advocacy - in the sense of lobbying for policy change – is carried out by selected NGOs and mainly from their headquarters level. NGO advocacy activities are increasingly prominent, institutionalized and coordinated in the areas of good governance, state compliance with constitutionally guaranteed laws and universal human rights, and developmental rights. Box 2.7 summarizes the advocacy strategies and practices of seven organizations taken as representative of NGO advocacy activity.

The scope and nature of NGO advocacy work is influenced by (i) official control over NGOs through formal registration requirements and other legislation (ii) the fine line between party political activism and advocacy from within civil society and (iii) the scope for protecting the political space, including through support from donors, NGO champions and influential individuals within Government, and through media activism.

Unlike other areas of NGO activity, ‘advocacy’ often cuts across sectoral spaces and where it involves challenges to Government has the potential to conflict with NGO service delivery goals. The conflict arises because it is imperative for service delivery NGOs that they are granted permission – and as Government funding of NGO activity grows in importance, approval – for their activities. This contradiction meant many NGOs were hesitant to involve themselves in pro-democracy and related campaigns through the 1980s and beyond, and were correspondingly treated with mistrust by other parts of civil society<sup>82</sup>; there remains lingering skepticism about the scope for NGOs to combine effective pro-poor advocacy with service delivery.

Understanding the role and impact of NGO advocacy requires an understanding of the political space in which they operate, and the challenges and constraints they face. Where the ‘political’ line is drawn is a matter of continual negotiation and conflict between NGOs, other civil society actors, political parties and the state. This has been demonstrated most clearly since 2001 in the form of official actions to de-register or halt the activities of five NGOs (including Proshika) for

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<sup>82</sup> Lewis forthcoming

**Box 2.7: A selection of NGOs involved in advocacy in Bangladesh**

Fair Election Monitoring Alliance (**FEMA**) is the alliance of 180 NGOs and civil society groups involved in electoral monitoring and voter registration, established in 1995. FEMA's main activity is parliamentary, Union Parishad and Municipal election monitoring. This involves deploying thousands of monitors in polling booths on election days, as well as longer-term activities such as voter registration and post-election dispute resolution.

Transparency International Bangladesh (**TIB**) is the Bangladesh chapter of the international anti-corruption NGO which from 1996 has been advocating for administrative reform to improve transparency, exposing official corruption, and conducting research on related issues. TIB is engaged in **grassroots mobilization** through Committees of Concerned Citizens (CCCs) which aim to generate demand for good governance at the local level.

Bangladesh Legal Aid and Services Trust (**BLAST**) began in 1993 by providing legal aid services to the poor, and has moved on to legal literacy campaigns and networking of NGOs involved in good governance. A main activity is public interest litigation (PIL) which it has filed in the following areas: employment discrimination; public examinations; illegal land acquisition, construction and property development; iodine deficiency in salt; slum evictions; abuse of power by the police and other executive agencies.

Ain o Shalish Kendra (**ASK**) also began in legal aid services in 1986 and has since moved on to dispute resolution activities, legal/ rights awareness education, research, networking and lobbying. With BLAST, ASK has been involved in PIL on slum evictions; torture; illegal detention and arrest; gender discrimination in state and local government institutions; legal rights of children in custody; and factory working conditions.

Starting in 1976, **Samata** has focused on supporting poor people's rights to *khas* land (Government-owned land according to law available to the landless poor). Activities include mass gatherings and rallies of the landless to press demands on local government officials; research and dissemination activities around issues relating to landlessness and land rights, and advocacy with national and local level Government officials.

Through its Institute for Development Policy Analysis and Advocacy (IDPAA) set up in 1994, **Proshika** attempts to influence national policy, primarily through research and publications, and its program of advocacy training and capacity-building. Proshika has in the past been involved in highly public and confrontational advocacy activity such as campaigns against harmful pesticides and a controversial voter education program of the mid-1990s.

Although **BRAC** only established its own Advocacy and Human Rights Unit (BAHRU) in 2002, it has been involved in advocacy since the 1980s, primarily through 'proof of concept' and collaboration with public agencies. BRAC's main advocacy activity remains in social communication rather than directed at national policy agendas.

The **Rangpur Dinajpur Rural Service (RDRS)** is a multi-sectoral NGO that provides services and focuses its advocacy effort on pro-poor rights. RDRS has focused on media campaigning and workshops with local elites to promote women's rights and gender equality, provides legal aid for the poor and supports group members in accessing local resources.

their allegedly partisan bias during voter education campaigns in the run-up to the 1996 election. (see Box 2.8).

The description of advocacy activities by NGOs above illustrates the range of issues that advocacy NGOs cover and points to the fact that quantifying its impact is difficult. Nevertheless, the following section attempts to assess the impact of advocacy for electoral reforms, curbing corruption, protecting civil liberties and strengthening the rights of the poor, particularly women.

The Fair Election Monitoring Alliance (FEMA) campaigns have regularly presented a range of reform recommendations on electoral reforms. Measures that have been implemented in full

### Box 2.8. The controversy over Proshika

One of the largest NGOs in Bangladesh, Proshika has recently scaled back its service delivery programs significantly, following a clampdown on donor funding of Proshika by the Government. Accusations against Proshika range from serious financial irregularities, uncovered by a Government audit, to sedition. On the issue of fraud and mis-use of resources the donors who had been instrumental in Proshika's rapid growth in the 1990s rallied behind the organization and questioned the validity of the audit report, contrasting it to the clean bill of health given by successive annual audits carried out by Price Waterhouse Coopers. Meanwhile the Government accused PROSHIKA officials of plotting with the main opposition party, the Awami League, to overthrow the government. According to the seditious scheme, PROSHIKA officials are accused of encouraging thousands of group members across the country to assemble in the capital to launch an opposition platform. The timeframe of the alleged plot coincided with the April 30<sup>th</sup> 2004 deadline the Awami League had issued for dislodging the BNP-led coalition government. Proshika's President along with a number of other employees was arrested in May 2004 and is currently out on bail as the legal processes go on.

Proshika has been treading a fine line for about a decade. In the mid-1990s the Awami League launched a movement for a neutral caretaker government and Proshika played a prominent role in this campaign drawing criticism for within and outside the NGO sector for being involved in a highly sensitive political issue. During the 1996 elections Proshika was heavily involved in voter education programs along with other NGOs. The material in Proshika's program, and that of five other NGOs, was considered to be pro-Awami League by the BNP who lost that election. The same perception also prevailed in the 2001 election that the BNP won. At the same time the President of Proshika also headed the NGO apex membership body, ADAB and the BNP Government's misgivings about Proshika threatened to boil over to the rest of the sector. Draft legislation was prepared to strengthen controls over NGOs – this was strongly opposed by donors and NGOs and the legislation has not yet been discussed in Parliament (see chapter four). A separate NGO apex body, FNB, has been formed by NGOs who wanted to distance themselves from the perceived involvement in politics by Proshika.

Ultimately whatever the merits of the case for or against Proshika, it is the poor who have lost out. The lack of funding has resulted in a sharp squeeze on Proshika's education programs that at one point were only second to BRAC in terms of size. For instance in 2000/01 there was 10,100 Non Formal Primary (NFP) schools and 11,586 Adult Literacy Centers operating. In 2004/05, there are 450 NFP schools and a complete closure of the adult literacy program. The number of micro-credit borrowers who received loans in 2004/05 is around 40% of the 2000-01 number. The social forestry program, one of Proshika's flagship programmes, had 2419 part time caretakers and in 2004/05 there are only 54 left.

Looking forward this story has lessons for Government, donors and NGOs as the discussion on the 'strategic compact' in chapter five will further develop. NGOs ought to refrain from engaging in any form of partisan political activity and also be aware that advocacy campaigns can jeopardize service delivery activities. Donors need to retain institutional memory and further develop the capacity to properly monitor NGO activities and financing. Finally, the Government ought to develop mechanisms that to the extent possible protect service delivery to the poor while legal action against an NGO, or selected NGO staff, is in progress.

include allowing poll observers and monitors in polling booths and raising the security money for candidates to one million taka. Recommendations that were not implemented include giving the Election Commission the powers of the Returning Officers and those that were only partially heeded include empowering the Election Commission to stop polling in a constituency.

Transparency International focuses on advocacy related to anti-corruption and are best known for their country corruption index. The relative ranking of countries draws considerable attention and Bangladesh's ranking in particular is the subject of much debate and controversy. Less well known is Transparency International Bangladesh's analysis and advocacy on specific ministries

and themes. For instance the police are allowing TIB to monitor the governance of selected police stations. TIB's report on corruption in Chittagong ports was noted by a Parliamentary Standing Committee that resulted in an internal investigation by the Chittagong Port Authority. An initiative to introduce citizens report cards in local level service points (education, health, local administration offices) is putting the spotlight on key issues such as absenteeism and resource leakages, though its tangible impact on changing the status quo has thus far been limited.

Our assessment of advocacy on civil liberty issues that have resulted in public interest litigation cases suggest that in the vast majority of cases, the court withheld a final judgment, through various forms of interim rulings such as stay orders. However, there are also more occasional examples where proactive policy changes have resulted from public interest litigation. For instance following five such cases contesting the practice of holding females in police custody, legislation was amended twice since 2000 whereby the female victim's consent is now required before she is placed in police custody. The Bangladesh Environmental Lawyers Association (BELA) has also had some success in protecting the environment through public interest litigation.

The largest NGOs involved in advocacy issues regarding women's rights are the Mahila Parishad and Naripokkho. Together with other NGOs and civil society groups, sustained advocacy and awareness raising campaigns have led to legislation on violence against women (specifically 'acid-throwing') and setting up women's courts.

While the above examples point to areas where advocacy has had some positive effects, another example related to advocacy for rights of the landless is illustrative of more limited impact during the implementation of reforms. Samata, whose main goal is improving landless access to idle Government land ("Khas land"), has been effective in lobbying for amendments to the Vested Property Act so that the landless can get access to such properties. However, the implementation of these amendments is proving slow due to deficiencies in land records compounded by lethargy in the local Khas Land Distribution Committees.

While the impact of advocacy for pro-poor rights is hard to measure, setting targets for various outputs associated with these activities and making these publicly available is critical. As table 2.7 indicates, in 2004, RDRS met or exceeded most targets with respect to a range of goals set as part of its strategy to raise awareness of various social and legal issues facing the poor, particularly women.

**Table 2.7 Advocacy and awareness raising: RDRS's progress in 2004**

Indicators	Annual Target	Achieved
No. of women's rights protection and promotion cells functioning (at federations)	260	257
No. of federation leaders trained in mediation skills and village court	225	245
No. of group members had legal education	93600	93954
No. of adolescents trained in gender awareness and reproductive health	750	687
No. of pregnant mothers given orientation on family laws and birth registration	2340	30818
No. of mediations organized/handled at federation level	520	1739
No. of teachers trained in human rights and family laws	200	175
No. of popular theaters organized on gender issues	161	167

Source: RDRS Annual Report 2004

## 2.6 Cross-cutting themes

This chapter focused on three key services provided by NGOs – micro-finance, health and education – and at NGO advocacy activities. The empirical evidence presented here shows that these services are by and large successfully targeted to poor households, though there is some room for improvement particularly in terms of geographical concentration of NGO activity. The impact of these services is also clearly positive, and as Box 2.9 illustrates valued by the communities that they serve. However while the impact on their clients has been largely positive, the wider “macro” impact has been limited by the fact that the services are still relatively “micro” in certain aspects. For instance while micro-credit has a ‘macro’ reach, which has resulted in important benefits for borrowers, the ‘micro’ loan size has limited the extent of employment that it has generated. Similarly, while non-formal primary education programs have contributed to reducing gender disparities in access to schooling and students have better educational outcomes, the impact on national educational quality is limited by the fact that only eight percent of primary school students are in NGO schools. The Gonoshasthaya Kendra experience shows that in areas where NGO health interventions are intensive there has been clear improvements in outcomes. Nevertheless quantifying the NGOs contribution in improvements in national health indicators is difficult, particularly as a significant part of NGO work is in awareness-raising of various kinds such as simple cures (e.g. diarrhoea), sanitary practices, family planning and facilitating linkages with the public sector (e.g. tuberculosis program) all of which are hard to measure. Moreover, tackling the emerging priorities in the health sector, such as curbing neo-natal mortality, will require more facility based care an area where NGOs are still relatively ‘micro’. Hence a key issue that will be explored in the final chapter are the mechanisms by which NGOs can scale up further, or shift directions, to enhance their impact.

One issue that is central to the discussion in this chapter is the issue of joint and separate provision of NGO programs. There are NGOs that focus on one core activity – e.g. Transparency International focuses entirely on advocacy on anti-corruption and ASA provides one core service, micro-finance. Most NGOs though are multi-purpose. Our overall support for joint provision of social services by NGOs, such as health and education, stems from the economies of scale in senior management oversight when both functions are provided by one NGO. The important part is to keep accounts for different programs separate and all forms of cross-subsidies transparent. In the case of micro-finance, there may be greater opportunities in the future for a few large NGOs to spin-off their micro-credit operations into a specialized financial entity such as micro-credit banks. However for the majority of NGOs, joint provision of the various services is the most practical arrangement given the synergies between programs.

However, one area that is less clear-cut is whether the same NGO that provides services can also engage in advocacy work. The earlier discussion illustrated the broad range of advocacy activities and the extent of emphasis various organizations place on advocacy. It is clear that multi-purpose organizations such as BRAC and RDRS focus on providing services and their engagement in advocacy is relatively low-key and deliberately non-confrontational. RDRS’s effort to involve local Government officials, elites, religious leaders and the media on issues that are clearly relevant to the poor has meant that its advocacy efforts are seen as part of its overall poverty reduction mandate. Particularly where NGOs receive Government financing, or are in other types of partnerships with Government in delivering services, it is likely that multi-purpose NGOs will have to limit their advocacy activities to issues that do not directly challenge the State.

**Box 2.9 What affects the community perception of NGO services?**

A nationally representative survey of 310 NGO branches was conducted by the World Bank from March to May, 2003. Survey enumerators applied a questionnaire to NGO branch managers, and they also conducted, in the vicinity of each NGO, a structured group interview with randomly selected community members. The structured group interviews asked the community members to ascribe, collectively, performance ratings to the local NGO branch.

Most structured group interviews reported substantial satisfaction with the work of the NGOs and NGO branches. Some 92% of the groups were satisfied with the performance of the NGO, 72% felt the NGO was quick to respond, and 81% felt that the NGO representatives were good at what they did. The structured group interviews were also asked, without prompting, to name the priority needs in their communities. Access to credit, health care, and safe drinking water were rated as the topmost priority needs.

The groups were asked to participate in an imaginary willingness to pay for NGO services, to rate NGO performance along eight dimensions (which were aggregated into a final score), and to evaluate the altruism of NGOs. The data were aggregated, and various NGO attributes were included as right hand side variables in regressions that attempted to identify aspects of NGOs related to high levels of community satisfaction. The regressions included, as controls, observable characteristics of the focus groups thought to be related to high ratings, including the percentage of focus group members who were female, NGO employees, NGO members, and union parishad members.

The sector of work had no effect on NGO performance scores. Branches of big NGOs (BRAC, ASA, Proshika, and Caritas) also received similar ratings to other NGOs in the country. Older and established NGO branches were seen to have been performing better than more recently established branches, perhaps because older NGOs have had time to develop relationships with community members and build satisfactory service provision programs. The average salary of professionals in the NGO was positively related to all three measures of community satisfaction.

This report argues that in general separating these functions and having specialized organizations, those that deliver services and those that engage in advocacy, makes more sense than having organizations that mix the two. However, we also recognize that there are organizations that have combined the two successfully by ensuring that their advocacy work remains focused on issues that do not 'overstep the mark' and are still important for the poor, such as legal awareness and violence against women. We now move onto examining the sources of finance for NGOs and as part of this will assess how potential shifts in these sources affects the debate on the trade-offs between service delivery and advocacy.

## Chapter 3: Financing NGOs: Trends and Prospects

This chapter examines issues surrounding various forms of financing NGO activity, highlighting trends over time and their implications. The Chapter first looks at trends in sources of funds that are external to the NGO and at the institutional issues related to direct donor financing of NGOs and financing of NGOs through Government contracts and private charitable contributions. It then examines issues related to self-generated sources of funds focusing on interest income from micro-finance and revenues from commercial enterprises.

### 3.1 External Financing

The share of aid to NGOs as a portion of total aid to Bangladesh has risen from 14.4% in the first half of the nineties to 24.5% since then.. We estimate that total aid to NGOs rose from an average of \$232 million (0.7% of GDP) between 1990-95 to \$326 million (0.7% of GDP) between 1996-2004 while total aid to Bangladesh fell from \$1.62 billion (4.9% of GDP) to \$1.35 billion (2.9% of GDP) during this period (see table 3.1).

	Total ODA to central Government	<i>of which:</i>		Grants to NGOs	Total grant aid to Bangladesh	Share of NGO grants in total grant aid	Estimated funding to NGOs from loan sources	Total aid to NGOs	Share of total aid to NGOs in total aid to Bangladesh
		Grant	Loan						
1990-91	1,716	831	885	106.6	938	11.4	73.4	180.0	10.5
1991-92	1,574	817	756	121.6	939	13.0	71.8	193.4	12.3
1992-93	1,607	818	789	195.7	1,014	19.3	71.7	267.4	16.6
1993-94	1,530	710	820	171.0	881	19.4	67.9	238.9	15.6
1994-95	1,682	890	791	209.5	1,100	19.1	73.1	282.6	16.8
1995-96	1,346	677	669	259.3	936	27.7	65.8	325.1	24.2
1996-97	1,469	736	733	250.1	986	25.4	80.9	331.0	22.5
1997-98	1,209	503	706	206.9	710	29.1	76.1	283.0	23.4
1998-99	1,490	670	821	273.5	944	29.0	69.6	343.1	23.0
1999-2000	1,545	726	819	182.4	908	20.1	92.0	274.4	17.8
2000-01	1,327	531	796	250.9	782	32.1	71.1	322.0	24.3
2001-02	1,198	481	717	208.3	689	30.2	73.1	281.4	23.5
2002-03	1,428	510	918	279.6	790	35.4	111.3	390.9	27.4
2003-04	1,114	380	734	310.0	690	44.9	69.4	379.4	34.1

Source: Author's estimates based on data from ERD, NGO Affairs Bureau and IMF

A sizeable portion of external assistance to NGOs comes through Government agencies from funds disbursed by lending agencies. These funds are typically part of larger projects that combine funding for Government agencies as well as for NGOs. These projects are recorded in the Annual Development Programme (ADP) but since the portion of the projects that are channelled to NGOs are not recorded in the Budget it is difficult to provide accurate estimates of these flows. There has been a large infusion of multilateral resources to micro-finance since 1995 and a number of large multi-donor projects in education and health. Our estimates suggest that on

average 20% of external assistance, averaging around \$77 million a year, that is provided to NGOs comes through Government from lending agencies. Table 3.1 shows that the average share of funds going to NGOs since 1995 is approximately 23.3% of total aid flows to Bangladesh.

**Financial sustainability of micro-credit operations has led to shrinking dependence on external assistance for the typical NGO.** While the volume of external assistance to NGOs has grown in absolute terms over the past decade, the relative importance of donor resources has declined as micro-credit interest income has grown rapidly. This can be illustrated in several ways. First during the 1995-2000 period when the number of communities with at least one NGO program doubled (see figures 2.2. and 2.3), table 3.1 shows that the volume of external assistance to NGOs grew at a far slower pace. Second a study of eleven large NGOs showed that while donor grants accounted for 94 per cent of the combined income sources of the eleven big NGOs in 1989/90, they constituted only 35 per cent by 1998/99. A large part of this difference is now met by micro-finance interest incomes, members' savings and commercial funding.<sup>83</sup>

**An approximate break-down by sector suggests that health (31%) micro-credit (12%) and education (12%) receive significant shares of external resources channelled to NGOs.** This data is a rough approximation as it is compiled from a range of sources – moreover these are three year averages that vary significantly from year to year. Apart from these three sectors support to agriculture and rural development (agricultural extension, fisheries, forestry etc), social safety net programmes and social development / advocacy programmes also receive significant amounts of donor aid, though precise breakdowns are difficult to quantify. The total volume of bilateral donor funding for micro-finance has sharply declined over the past ten years and there has been a trend by bilaterals to move away from direct provision of revolving loan funds, at least through the use of grants, towards a focus on technical assistance, capacity building and, increasingly, innovation in the sector. Resources for revolving loan funds, are now being channelled almost entirely through PKSF for on-lending to NGOs<sup>84</sup>.

**Transfers to NGOs as a share of total resources transferred varies significantly across development partners.** A recent survey of five donor agencies suggests that this share varies significantly. Predictably multilateral agencies such as the World Bank provide the bulk of its resources to the Government of Bangladesh, with an average of 14% of total IDA disbursements over the past decade channelled to the NGO sector through Government line agencies or autonomous bodies such as PKSF (see Annex table 3.1. for details). Bilateral agencies shares are higher with DFID and CIDA spending approximately 29% and 20% on NGOs respectively, while the European Union estimates that it spends upto 45% of its resources in Bangladesh through NGOs.<sup>85</sup> Moreover the sectoral focus varies significantly by donor. Around 21% of DFID's funds to NGOs went to advocacy activities in 2003/04 and around 10% to 'enterprise development' compared with IDA that did not channel any resources to advocacy activities while spending around 70% of its resources to NGOs for micro-finance.

<sup>83</sup> Members' savings accounted for 12 per cent in 1998/99 (0 per cent in 1989/90); service charges, bank interest and own resources accounted for 31 per cent (up from 5 per cent in 1989/90); and bank and other borrowings accounted for 22 per cent (up from 1 per cent in 1989/90). Thornton et al 2000

<sup>84</sup> The World Bank disbursed \$282 million through the Palli Karma Shahayak Foundation (PKSF), for expanding microcredit outreach, over this period.

<sup>85</sup> Matsaert (2005)



### 3.1.1 Issues with direct donor-NGO financing

**There are a wide variety of donor-NGO partnerships in Bangladesh.** These are depicted in Annex table 4.2. The simplest form of funding revolves around project funding to provide very specific services. These involve no support to the wider institution generally, and the objectives of the funding are usually set by the funding agency. Donors often pool funds if the projects they are financing are large and involve big NGOs. This is the case for the various programmes with large NGOs where a donor liaison office provides an interface between donors and the NGO, promoting harmonization and reducing transaction costs.

**Another type of financing involves agreeing on a common vision between donors and an NGO, and then financing the whole range of an NGO's activities.** The consortium funding of Proshika Phase VI was an example of this, as has DFID's funding of Nijera Kori and Samata, the World Bank's funding of PKSF, and USAID's funding of Rupanter. This type of funding has very different parameters from project financing as the donor invests heavily in capacity building for the whole organization. A more developed form of this funding also includes an institutional development perspective that sees the institution transformed into a different legal entity by the end of the funding period (e.g. CIDA's funding of PDBF and USAID's funding of Aranuk). However experience shows a mixed picture with both types of funding. A key problem with partnership agreements has been that they have had the problem of trying to upscale the work of an institution too quickly with resulting NGO management strains, expansion problems and resultant over-funding<sup>86</sup>. Predictably, institutional transformation has also not been an easy path as the visions for change have at times differed between the NGO and funder, and these processes have taken a long time to be implemented.

**There is a re-emergence of project based financing and greater use of wholesale funds for smaller NGOs.** Donors have found that dealing with small and medium sized NGOs carry high transaction costs<sup>87</sup> relative to the scale of funding. This has led to a number of wholesale vehicles being created, where donors set the objectives of the programme, with an agency managing a pool of money for smaller NGOs<sup>88</sup>. The managing agency could be an international NGO or a consulting firm. The European Commission (EC) has also recently stipulated that any NGO contract be competitively tendered, which has resulted in the creation of large number of EC outcome based funds. At the same time the amount of funding of partnership agreements is being reduced due to the mixed experience described above with a return to a project based approach for large NGOs.

**NGOs face a high staff turnover in donor agencies and a wide array of different donor financial stipulations.** Staff turn-over in donor agencies results in lapses in institutional memory of the NGOs that their agencies fund<sup>89</sup>. The varied quality of financial reporting also stems from the many different formats imposed by donors, the concentration on cash accounting rather than accruals, and a focus on the specific project without assessing what is happening to the wider

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<sup>86</sup> DFID (2004)

<sup>87</sup> These costs are mainly in terms of staff time, accounting and financial reporting, as well as capacity building needs.

<sup>88</sup> An example of this type is Manusher Jonno, a DFID funded rights promotion fund, administered by CARE, and which screens, funds and provides technical assistance to smaller NGOs. Other examples are the various wholesale funds run by USAID (Health & Human Rights Funds) and CIDA's Canada Fund.

<sup>89</sup> Sultan 2004, DFID 2003.

institution<sup>90</sup>. A review of a ten year programme of support to NGOs in the agriculture sector<sup>91</sup> asserted that only 50% of NGOs fully adhered to financial obligations put in place by donors. The situation for smaller NGOs appears worse as most donors acknowledge that they are generally unable to comply with donor requirements, or all accounting and auditing standards<sup>92</sup>. Clearly several donor financial stipulations are unrealistic and there is an urgent need for harmonization in this area (see Chapter Four for more details).

### *3.1.2 Issues with Government contracting of NGO services*

As discussed above, NGOs also receive resources from Government – the largest share is through donor financed projects implemented through a particular line agency, and some resources financed through Government's own revenues. A recent example of the Government recognizing the value of contracting NGOs using its own resources is the one hundred crore taka allocation (\$16.7 million) to PKSF in the 2004/05 Budget to channel to NGOs to scale up a pilot program with the extreme poor.

**There are clear merits in having partnerships and contracting arrangements in social service delivery in Bangladesh.** As neither Government nor NGOs command sufficient resources and capacity in their own right, different modes of partnership have evolved over time. These range from formal collaborative and contracting arrangements to informal 'gentlemen's agreements'. There is cross-country evidence that contracting NGOs has resulted in rapid gains in service delivery outcomes, showing how non-state provision can go to scale cost-effectively<sup>93</sup>. Financing NGOs through the Government budget improves the comprehensiveness of the fiscal framework and leads to more rational and coordinated public policy choices.

**There are some notable success stories in contracting NGOs.** A current example of successful partnership between donors, Government, private sector and NGOs is in solar energy. An IDA financed project is financing 50,000 Solar Energy Home Systems (SHS) over five years. Government contracted the Infrastructure Development Company (IDCOL), a Government owned company governed by a Board with public-private representation and managed with considerable autonomy to implement the project. IDCOL has the operational autonomy to select NGOs and other partners, provides technical assistance, ensures equipment standards, and monitors progress. The Rural Electrification Board (REB), a highly regarded Government body, helps NGOs select areas in which to promote SHS.

NGOs raise awareness about SHS, and train household members in the use and repair of the SHS. Micro-credit loans are used to pay for these systems, and staff are trained to provide maintenance support during monthly repayment collection visits. The private sector manufactures and supplies SHS components, with quality monitored by IDCOL.

The project's successes to date include that the targeted coverage of 14,000 households in the first two years was achieved twice over: as many as 30,000 SHS units had already been distributed after two years. These successes depend on a number of factors (i) learning from earlier

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<sup>90</sup> Khan 2005

<sup>91</sup> ASIRP 2003

<sup>92</sup> Khan 2005, Irish & Simon 2005

<sup>93</sup> Loevinsohn and Harding 2004

### Box 3.1 Using an autonomous foundation to contract NGOs: lessons from PKSf

Bangladesh's famed micro-finance sector owes part of its success since the 1990s to the support it enjoys from the Palli Karma Shahayak Foundation (PKSF). Set up in 1990 as an autonomous non-profit organization, PKSf's remit has been to channel funds to NGOs to expand their micro-credit operations, carry out advocacy for the micro-credit sector and help build the capacity of the industry through hands-on assistance and formal training courses. PKSf currently lends to 222 NGOs, at 4.5% interest to small and medium NGOs and 7% to large NGOs. PKSf is also widely credited for sharpening the focus of many NGOs towards financial sustainability and also in setting appropriate standards that will ease the way for a strengthened regulatory structure for micro-finance.

An important factor behind PKSf's achievements is that it is widely acknowledged to be governed in a transparent, non-political manner. PKSf's internal governance is structured to ensure that Government has representation on its Board while also permitting PKSf full operational autonomy. The Governing Body provides for a balance of interests with representatives from Government, civil society and the private sector. The high profile and non-political stances of respected public figures on the Governing Body are central to PKSf's autonomy and legitimacy. Salary levels are also on average around 70% more than employees in public sector banks creating better incentives for performance.

PKSF lends to NGOs only after a strict screening process that includes a track record of implementing micro-finance programs, basic standards of internal governance and geographical location. The application process for becoming a partner organization is simple and advice and information are freely available from PKSf's Counselling Cell. The process of evaluating prospective partners is time-bound, and feedback is given to partners at each stage of the application process, including after rejections. Every year, PKSf receives hundreds of applications from small NGOs desiring to become a Partner Organization (PO) of PKSf. Thus far PKSf has found that around 10 percent of these NGOs meet PKSf's strict eligibility criteria to become a PO. The Counselling Cell offers advice on the changes an NGO needs to undertake in order to become a PKSf member.

Once an NGO becomes a PKSf Partner Organization, staff undertake field visits to assess the amount of its loan application based on its track record and capacity to absorb funds. Standard monitoring formats are introduced to maintain comparability across NGOs. Repayment rates are almost 100 percent due to strict monitoring and incentives for NGOs to repay in order to access new loan tranches.

initiatives with renewable energy (ii) the independence of IDCOL to select partners and monitor program activities and (iii) use of the country-wide NGO network of micro-finance organizations to channel financing to rural households (iv) regular interaction among the various partners.

There are other successful examples of contracting NGOs. The Palli Karma Shahayak Foundation (PKSF), an autonomous non-profit apex body for micro-finance offers a number of lessons about how to design a successful partnership between donors, Government and NGOs. Among other things, PKSf is a case of how to get the internal governance of an independent foundation right, and set strict eligibility criteria for NGOs to receive funds (see Box 3.1).

**At the same time there have been a range of practical problems with Government contracting of NGOs.** Key problems relate to delays, corruption in assigning NGO contracts, and the dampening of advocacy efforts by NGOs. The lack of transparency in selecting NGO partners has led to the emergence of dubious NGOs and has driven out a number of competent NGOs from

the bidding process. These are related to broader governance problems with public procurement in Bangladesh. NGOs also voice concerns over Government finance might imply greater political demands, and potentially a patron-client relationship with Government.

**Experiences with contracting in non-formal education offer clear lessons in what not to do.** Future collaborative arrangements need to avoid repeating the contracting errors made under the Integrated Non-Formal Education Project (INFEP), when NGOs were contracted to provide non-formal education programs. A selection process evolved in which proposals from NGOs were evaluated and selected through an inter-ministerial Subvention Committee that lacked specific evaluation criteria. Efforts to avoid domination by some NGOs meant that numerous smaller organizations were contracted and unqualified ‘fly-by-night’ NGOs emerged. Weak monitoring systems also made it difficult to ensure that programs were implemented according to agreed contracts. The Department of Non-formal Education (DNFE) was established in 1995 to facilitate Government-NGO collaboration; however, following problems with contractual processes and reports of corruption, DNFE was shut down in 2003.

A recent audit of short-listed NGOs in a new phase of an on-going World Bank-financed education project<sup>94</sup> found that 34 per cent of short-listed NGOs had dubious credentials, including one or more of the following: (i) they lacked a functional office; (ii) had less than two years of experience in non-formal education; (iii) submitted no or fake audit reports; and (iv) used fake experience certificates from local Government officials. NGOs will now be selected from a revised, shortened list, but this recent experience reflects the fact that contracting NGOs remains problematic in the education sector.

**A comprehensive assessment of contracting NGOs in the health sector has been carried out.** Contracting of NGOs by Government is increasingly important in the health sector, and efforts to gather lessons about what works and why are beginning to be made.<sup>95</sup> A recent comparative analysis of different models for contracting arrangements, in the context of a new large sector wide programme in the health sector, found that most lacked systems for monitoring performance or staff performance incentives.<sup>96</sup>

**These experiences offer a number of lessons for contracting NGOs.** Contracting systems need to use competitive bidding processes with simple, transparent application and approval processes and guaranteed processing times. The Request For Proposals ought to specify the consequences of providing incorrect information and ensure that the final selection would only be made following third party inspection of on-going programmes. The selection criteria for NGOs ought to include (i) a solid track record of past performance (ii) a management information (MIS), a robust accounting system, and appropriate fiduciary arrangements (iii) accreditation systems and mechanisms for monitoring performance and accountability (iv) effective systems for payment,

<sup>94</sup> The Post Literacy and Continuing Education Project

<sup>95</sup> Recent assessments include Cummings *et al* 2004; Forsberg and Sundewall 2004; Loevinsohn 2001; Loevinsohn and Harding 2004.

<sup>96</sup> The modalities of contracting NGOs include i) direct contracting by Government or a governmental body; ii) through or as a non-profit registered company; iii) using a contracted manager to manage arrangements with NGOs and provide M&E functions; iv) an independent trust; v) through direct funding from donors, usually through a contracting arrangement (see World Bank 2005). Prominent programs in health involving contracts with NGOs include the NGO Service Delivery Program (NSDP); the Bangladesh Population and Health Consortium (BPHC), a DFID-support program supporting NGO community work in training, management and MIS and the Urban Primary Health Care Project (UPHCP), a predominantly ADB-supported project in which responsibility for PHC has been given to the Ministry of Local Government and Rural Development (MOLGRID) and urban primary health care centers constructed in 16 partnership areas.

retention of user fees and performance-related pay and (v) mechanisms for social accountability through community participation.

### *3.1.3. Issues related to private charitable donations*

**Private charitable contributions are largely related to religious traditions.** A survey of 1062 households in 2001 shows around 70% of private charitable contributions go to religious institutions, (mosques and madrassas) with educational institutions (15%) a distant second followed by recreational events (9.5%)<sup>97</sup>. There were typically a number of reasons for donating, the most common relating to religious beliefs, humanitarian needs and promoting a local organization. The Islamic tradition of individuals donating a certain percentage of savings to worthy causes ('Zakat') appears to be a key driver behind these charitable contributions. Religious organizations and orphanages collect from homes, particularly during festive seasons, while public appeals are used by social welfare organizations. Development NGOs that are the focus of this report do not appear to feature prominently among the list of local contributions. Part of this is due to the fact that apart from national emergencies, development NGOs do not actively seek local contributions.

**The new provision for tax deductions for charitable contributions introduced in the 2005 Budget may increase resources going to development NGOs.** This new provision that permits deductions for "philanthropic and educational institutions" ought to increase the flow of funds to the non-profit sector as a whole. NGOs will need to submit a written application to the National Bureau of Revenue (NBR) describing their activities and NBR will then decide whether contributions to NGO in question will give rise to tax deductions. It will be important to monitor this process carefully as this process involves considerable discretion of what constitutes an eligible philanthropic or educational institution.

**The certification process for tax deductions could be devolved to an independent professional body.** Lessons may be drawn from the Pakistan Centre for Philanthropy's (PCP) certification program (see Box 4.3) and from the Philippine Council for NGO Certification. Organizations receive a 'seal of good housekeeping' according to whether they meet defined standards of organizational effectiveness, based on independent evaluation of their internal governance, financial management and program delivery. In both countries the Ministry of Finance has devolved certification for tax purposes to these bodies – the advantage for the Government is that it avoids stretching existing capacity within the ministry and they do not have to deal with complaints from non-profits that are not certified. Certification bodies are discussed in greater detail in chapter 4 in the context of proposed improvements in the legal and regulatory framework for NGOs.

**The expatriate Bangladeshi community is a potentially large source of private donation.** The bulk of remittance transfers to Bangladesh (around \$3.4 billion in 2003/04) are from relatively poor migrant workers who remit funds to sustain their families. However there is a smaller group of relatively wealthy Bangladeshis who can be tapped for charitable contributions to NGOs. In order to facilitate this transfer, NGOs could explore obtaining non-profit status in the United States and Europe, or could establish tax exempt foundations, so that income tax deductions can be obtained for contributions. This is likely to be a resource-intensive process that at least initially only

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<sup>97</sup> Ahmad and Jahan (2002)

the larger NGOs could explore. The Government could also facilitate this resource transfer by ensuring that the laws related to Anti-Money Laundering are widely known and applied in a streamlined manner. NGOs will also need to make greater efforts at publicizing their activities to target expatriate communities, as well as take steps to improve corporate governance, in order to encourage these private charitable contributions.

### 3. 2. Internally generated funds

#### 3.2.1 Micro-finance interest income

**Micro-credit surpluses are being generated with low cost operations:** As micro-finance scaled up in the 1990s, there was a growing emphasis on financial sustainability as individual branches became profitable within a few years. Financial analysis of NGOs of various sizes<sup>98</sup> suggests that many generate surpluses from their microfinance operations (table 3.2). All the NGOs surveyed had positive adjusted returns on assets, with most at about 3.5% and ASA much higher at 10.5%. There have been consistent efficiency gains for all sizes of NGOs over the past five years, as the number of borrowers and total portfolio per credit officer have been steadily increasing, for all sizes of NGOs (see Annex table 3.3). ASA is known worldwide for being an industry leader in cost-efficiency and all the NGOs surveyed show high levels of efficiency when compared to programs in other countries. High population densities are a significant contributing factors to this, though NGOs have also worked hard to develop low cost, efficient, decentralized management systems (see chapter Five).

**Table 3.2: Profitability of NGO MFIs, 2001-4**

NGO or category	Indicator	2001 (%)	2002 (%)	2003 (%)	2004 (%)
Very Small NGOs	Adjusted financial self-sufficiency	168	122	119	121
	Adjusted return on equity	n.a.	3.8	3.4	4.0
Small NGOs	Adjusted financial self-sufficiency	128	113	122	127
	Adjusted return on assets	n.a.	1.7	3.4	4.8
Medium NGOs	Adjusted financial self-sufficiency	144	122	122	119
	Adjusted return on assets	n.a.	3.5	3.6	3.2
ASA	Adjusted financial self-sufficiency	113	169	173	n.a.
	Adjusted return on assets	n.a.	10	10.5	n.a.
BRAC	Adjusted financial self-sufficiency	107	111	118	n.a.
	Adjusted return on assets	n.a.	2.3	3.4	n.a.

Note: Financial self-sufficiency is defined as total annual income/(total operating + financial expenses)\*100. The adjustments made to calculate these ratios were made to adjust the cost of funds borrowed from PKSF to to commercial market rates of borrowing (i.e. from 4% for smaller NGOs and 7.5% for ASA and BRAC in 2004, for example, to 10%, the average lending rate of nationalized commercial banks to NGOs), and adding an opportunity cost of capital equivalent to the annual rate of inflation.

<sup>98</sup> These included BRAC (3.8 million active borrowers) and ASA (2.5 million active borrowers) of the large NGOs; two medium NGO MFIs with between 50,000 and 500,000 active borrowers by June 2004 (Jagoroni Chakra and TMSS); eight small NGO MFIs with between 10,000 and 50,000 active borrowers by June 2004; and 4 very small NGO MFIs, with fewer than 10,000 active clients by June 2004.

### Box 3.2. Linking NGOs to commercial bank financing

There has been relatively little use of commercial bank funds by NGOs as the contribution of other cheaper and more easily accessible sources (e.g. member savings, retained earnings and loans from PKSF) have been sufficient for micro-finance growth. However this source has the potential to become more important in the future as NGOs seek to diversify funding sources.

The Swiss Development Corporation (SDC) has been a pioneer in trying to increase access to and use of commercial bank funding by NGOs in Bangladesh. The first project was a challenge fund with Sonali Bank, the largest Nationalized Commercial Bank (NCB). Loans to about ten NGOs at 10% interest were guaranteed by SDC, with independent ratings of the NGO MFIs being a prerequisite, collateral was required in the form of personal guarantees of the NGO directors. Sonali Bank continued this program on its own after the SDC project was completed and now has 10 to 15 NGO partners, though it has dispensed with the requirement for independent credit ratings. More recently SDC has partnered with Pubali Bank - a fund of Taka 75 million was formed to lend to NGOs, with SDC contributing one-third of this amount. SDC charges 3% for its loan and in turn Pubali Bank lends to NGOs at 10%, with NGOs required to have an independent credit rating done before applying. Initial demand from NGOs has been so high that SDC is considering increasing its contribution. In one case where the amount of the loan to a single MFI was very large, Pubali Bank required collateral in the form of a lien on property owned by the NGO, but in most cases only the personal guarantee of the directors is required. Basic Bank has had access to capacity building support from SDC along with support to pay for credit ratings done for NGOs that qualify to apply for funding, but no direct support for their loan fund. It has 25 to 30 NGO partners to which it charges 9% from a Taka 20 million fund.

The Credit and Development Forum (CDF) funds about 40 very small NGOs, through a facility funded by two NCBs. The NGOs are charged 12% for these funds, the banks get 10% and CDF gets 2% to administer the program. The NCB facility of Taka 50 million has currently disbursed Taka 20 million, and is guaranteed by the personal guarantee of CDF's Directors. CDF claims that there is considerable NGO demand for larger amounts of funding, something it cannot provide, at least for now. One reason for the willingness of these very small NGOs to use commercial bank funds is that while they aspire to become partners of PKSF, they have not yet been able to qualify.

A recent decision by PKSF that its partners may not charge clients more than 12.5% has spurred the partner organizations to make renewed efforts to diversify their funding sources, including the use of bank funds, primarily to reduce their dependency on PKSF funding over time. Even so, there are still constraints to be overcome, primarily the relatively high cost, the difficulties of working with banks to meet their requirements and the fact that some NGOs do not have a legal status that allows them to directly borrow from banks. It appears, though, that bank rates might decline in future, and if this can be coupled with banks becoming more knowledgeable about microfinance and more convinced that this is good business, as has happened in some other countries, opportunities to link NGO MFIs with commercial banks will increase.

**There is a trade-off between reducing interest rates and access for the poorest:** Micro-credit profits are used to finance lending to groups and geographical areas that are under-served as

well as build the equity bases of these institutions. There is scope for reducing interest rates but this could be at the cost of serving poorer clients as currently part of the spreads are used to cross-subsidize small loans. BRAC's average loan size is around 40% lower than ASA's<sup>99</sup> and reflects the fact that a higher proportion of loans currently go to the poorest (see Annex table 3.4). A few NGOs use micro-finance profits to cross-subsidize their social programs e.g. TMSS though the majority appear to only cross-subsidize the poorest borrowers within their micro-finance program. Moreover, it is important to put the criticism of NGO interest rates in context – the real alternative for poor households are not commercial banks, but the village moneylender where rates average around 120% per annum.

**Interest income is projected to grow with micro-credit expansion provided portfolio quality remains unaffected.** Annex table 3.4 shows that there has been rapid growth in client numbers in recent years and there is also clear evidence that the market for mainstream micro-credit is not saturated. Chapter Two illustrates the geographical areas where there is relatively little coverage and shows that currently around 37% of households access micro-credit. Given that around 50% of households are poor and another 10% of current micro-credit borrowers are part of the vulnerable non-poor group, there is a clear scope for market growth even allowing for a sizeable number who may not wish to borrow. However, it is critical that portfolio quality is maintained at currently high levels as risks grow with larger loans and in older branches. The lessons from the temporary fall in portfolio quality at the Grameen Bank in the late nineties, which resulted in a restructuring of the portfolio, need to be taken into account as growth takes place.

**Recent initiatives by some NGOs to securitize their portfolios and borrow from commercial banks indicate a growing integration with the formal financial system.** The interest in finding alternative sources of funds grew after PKSF capped the interest rate at which its partner organizations could lend to clients in mid 2004. There are still significant problems to be overcome in accessing commercial funds, such as the type of collateral to offer, but this source of loan portfolio funds will grow if the costs of borrowing from banks decline and if steps are taken to help commercial banks overcome their reluctance to lend to NGOs (see Box 3.2).

**Social investment funds, have not yet played much of a role in the financing of the microfinance sector in Bangladesh, in contrast to their rapidly growing use in Eastern Europe.** Equity investments in NGOs will be facilitated if an appropriate regulatory framework to set up micro-finance banks is established or if more NGOs register under the Companies Act. CARE is considering setting up a social investment fund that will combine commercial investments with the use of grant funded technical assistance, a model employed by at least two of the recently established international social investment funds. BURO Tangail is one of the few NGOs in Bangladesh to actively seek out international investment funds. However these types of transaction need to address foreign exchange controls that limit how much can be repatriated for loan repayments.

**It is likely that independent credit ratings will be required for NGOs wishing to access commercial funds.** Credit ratings are one more level of transparency that give comfort to investors - PKSF could also make use of published performance indicators and credit ratings as part of its NGO assessment process. The assessments and credit ratings that have been done to date in Bangladesh were carried out by M-CRIL, an international specialized microfinance rating agency, but

<sup>99</sup> BRAC's average loan size in 2003 was 6100 taka compared to ASA's at 8500 taka



it would be useful to establish a local rating organization. This could happen by linking an experienced international rating agency with a local organization that wants to become a rating agency or with an existing rating agency that rates regulated financial sector institutions and wishes to develop a capability in microfinance.

### 3.2.2 NGO managed commercial enterprises

**A number of NGOs run a variety of business operations.** The scale and type of operations vary considerably and Annex table 3.5 provides examples of some of the different segments in which NGOs operate. Broadly there are three types of business (i) those that have grown as an extension of credit operations and the needs of poor micro-entrepreneurs (e.g. Gano Kallyan Trusts hatcheries to produce day-old chicks for poor poultry rearers) (ii) those that link rural

#### **Box 3.3 Moving out of poverty using micro-credit and a mobile phone**

Grameen Telecom introduced mobile phone services in rural areas in 1997 and began an innovative business initiative with Grameen Bank borrowers. The Village Phone Program (VPP) selects, trains and provides credit to Grameen members who purchase a phone using the loan and provide mobile phone services in the village for a fee. Village Phone members are charged a lower rate by Grameen Telecom and the difference between the user fee and this negotiated rate is the per cal profit.

Jharna Begum, now one of 125,000 phone ladies operating around the country, has been a member of GB's *Shonarong Tongibari* branch for the last thirteen years. She first joined GB to provide some financial support to her father. She was in great financial hardship when she married Habibur Rahman, a hired hand in a rickshaw workshop. Her husband's meager earnings were barely enough to provide for their two children and they were struggling to make ends meet. Over the years, Jharna took a number of general loans from GB. Eventually they were able to set up a rickshaw garage in their house and start a confectionary.

Jharna's economic situation improved significantly when she took a 12,000 taka loan from the Grameen Bank to purchase a cell phone under the new VPP. She conducts her cellular phone business from a rented shop in the village bazaar from 9:30 in the morning to 9:00 at night.

With an additional monthly income of Tk5,000-Tk6,000 coming from the mobile phone business, Jharna is now saving every month, something she was not able to do before she bought the cell phone. She makes a regular monthly deposit of Tk800 in her savings account with GB and has also opened a separate savings account for her husband. In stark contrast to her struggling days, she is now the proud owner of a plot of land which she purchased from her savings for Tk40,000. She has also bought a refrigerator for the confectionary and some furniture for the house. The village phone business has helped her acquire the bakery premises for her husband.

According to Jharna Begum, the village phone business has significantly improved her life. Becoming a village phone operator has not only raised her earnings but has also enhanced her socio-economic status in the community. The local elites of the village now visit her household regularly. When asked about her future plans, Jharna said her primary goal was now to educate her son and daughter and further expand her business, starting with buying her own mobile phone shop.

with urban consumers (e.g. Grameen Phone that created a market for rural mobile telephone users – see Box 3.3) and (iii) businesses set up without a direct poverty reduction element, but which generate revenues for the NGO's development programs.

**There is considerable debate about the legitimacy of NGOs operating private sector businesses.** The dominant view is that NGOs should be required to separate all their for profit businesses from their development work, that they should not be allowed to use subsidized capital to enter or operate businesses and that NGOs should pay taxes on their for-profit segments at the same rate as other businesses. There are also concerns that NGOs may be drifting from their core mission of poverty reduction as management resources are diverted to overseeing commercial activities. There are also contradictory views of NGOs regarding pricing of inputs and outputs – some arguing that NGOs 'entrap' their members into adverse pricing relationships – others that NGOs unfairly subsidize markets by paying artificially high prices<sup>100</sup>.

**On the other hand the potential that NGOs have to stimulate rural growth is also recognized.** The clear benefits of NGOs providing poor rural producers with input, output and marketing linkages are obvious. Large NGOs in particular have a nationwide network and there are private sector actors who are interested in tapping into partnerships through sub-contracting arrangements or as part of their corporate social responsibility mandate. Donors also see the potential of NGOs to act as facilitators for rural market development and private sector linkages, and commercial ventures as a means of reducing dependence on donor financing. It is common practice in many countries for NGOs to operate business ventures to generate revenues (see Box 3.4).

**NGO businesses are registered under a variety of forms that have significant effects on their objectives, independence and operational freedom.** Box 3.5 below gives examples of different types of NGO business registration. Project Support Enterprises typically are not separately registered and generally form an integral part of an NGO, although they may operate as 'profit centres' within the overall institutional structure. Their accounts are not generally separated from the overall NGO<sup>101</sup>. The second category (not- for profit businesses) form the next tier where businesses are accorded separate registration and hence attain a level of independence but the aims of these businesses may not be explicitly profit-oriented. The governance of these types of businesses is also closer to that of the sponsoring NGO. The final tier is characterised by separate incorporation as a 'for profit' under the Companies Act, with shareholders and a Board. These businesses are still generally majority owned by the NGO, but in the case of financial institutions, a requisite number of external shareholders and minimum share capital are stipulated. The most developed type of NGO business is a publicly limited company floated on a stock exchange. The GKT hatchery is an interesting example where micro-credit clients savings were converted into equity and these members own the majority shares of the business.

**The profitability of NGO businesses appears mixed.** An analysis of commercial enterprise financial data for the past several years suggests that agro-based businesses typically exhibit low profitability with returns on assets negative in some years and averaging around 1.5% (Annex table 3.6). Returns for handicrafts, a traditional market for NGO businesses, also exhibited a mixed picture: returns on assets varied from 0.62% for TMSS in 2003-4 to 5.62% for BRAC.

<sup>100</sup> McKennie et al 2003, Alamgir 2004

<sup>101</sup> Some larger NGOs do provide segmental reporting on Project Support Enterprises, such as BRAC.

### Box 3.4 NGO linked commercial ventures in other countries

The 'endowment model' is an integral part of NGO financing strategies worldwide. NGOs are increasingly trying to raise funds from internal sources to cover basic operating costs in addition to approaching external donors for its program costs. Examples include:

- Organizacao de Ajuda Fraternal, a center for street children in Brazil, covers all of its annual expenses from the sale of furniture and hospital equipment, while simultaneously providing job training and income for its constituents.
- Ekocenter, a coordinating body for environmental NGOs in Yugoslavia, is using publishing and an organic wine project to generate income.
- Child Relief and You (CRY), in India, generate nearly 50 percent of its annual income through the sale of greeting cards, paper products and children's toys in India and the US.
- FUNREDES, in the Dominican Republic, covers over 70 percent of its operational expenses by offering internet and website design services to for-profit companies.
- The environmental NGO, Adonis, also in the Czech Republic, has started a for-profit tourist office to attract eco-tourists to the region.
- In Georgia 55 out of 291 randomly selected NGOs were involved in commercial activities.

Examples of laws governing NGO commercial activities in various countries are:

**Switzerland** – The legal principles governing the establishment and functioning of non-profit associations are found in Articles 60 to 79 of the Swiss Civil Code. The Articles stipulate that while the aim of the association must be non-profit, this does not imply that the association must refrain from generating profit. However, any profit made cannot be distributed to members and must be used by the NGO in order to achieve its aims.

**Bulgaria** - Numerous Bulgarian NGOs have already launched strategies to initiate commercial activities. According to the Bulgarian NGO law, NGOs (as separate legal entities) may conduct economic activity, provided it complies with specific legal criteria:

- The economic activity must be supplementary, meaning that the volume of the for-profit activity must not exceed the amount of basic non-profit activity.
- The economic activity must be relevant to the basic mission of the NGO, e.g. the business activity must be a means for achieving organizational goals.
- The revenue generated by the economic activity must be reinvested, i.e. used for achieving the objectives set forth in the statutes or the incorporation act of the NGOs.
- The scope of the economic activity must be defined in the statutes of the NGO.

**Central Asian Union (Kazakhstan, Kyrgyzstan and Uzbekistan)** – Commercial activity has emerged as an increasingly important source of revenue for NGOs in these countries. Under the Public Associations Laws and the CAU Civil Codes, a non-profit organization has the right to carry out business activity only insofar as such activity furthers the purposes for which the non-profit organization was created and corresponds to such purposes.

From the data available it is also clear that BRAC and Grameen commercial ventures operate very much in a league of their own in terms of scale and market power. They have higher levels of commercial expertise and market share than the bulk of smaller NGOs, which operate less professional, and generally have more capital constrained enterprises. While a larger sample is

required to make firm conclusions it appears that a large set of NGO businesses are managed with limited capacity and variable profitability.

**There are a number of factors that explain widely different returns to NGO businesses.** First few but the large NGOs can afford to allocate specialist staff to operate businesses in a professional manner, and therefore there are concerns of businesses diverting management resources away from poverty reducing activities. Second the continued operation of efficient businesses depends on the organisational strength of the NGO to act in a commercial manner. This is by no means assured, especially in smaller NGOs where much is focused on a few talented individuals, who oversee operations. Third many of these businesses, especially in the handicraft sector remain relatively undercapitalised, due to frequent cash transfers to social activities. This may result in low levels of reinvestment, resulting in low levels of business growth. From the existing evidence, a tentative conclusion can be drawn that suggests NGO businesses that are separately incorporated from an NGO's social activities perform better. Separation seems to allow greater specialisation, more strategic business planning and improved governance.

**There is no evidence of NGOs taking advantage of members through the pricing of inputs or outputs.** Recent work on examining the extent to which NGO members are 'trapped' into adverse pricing relationships compared prices that NGOs offered their members for outputs, and prices charged for inputs<sup>102</sup>, with private sector vendors of products of similar characteristics. The study conclusively argues that NGOs offer fair prices that do not overly distort markets and another study shows that BRAC's Program Support Enterprises often set a price floor even when market conditions change to protect poor producers. The market distortion through this subsidy is justified on equity grounds given the organization's overall poverty reduction mandate.

**Looking forward NGOs ought to be more systematic about market entry and exit.** The rationale for starting a commercial venture typically varies between the correction of a market failure in order to benefit the poor or the opportunity to earn profits to subsidise social programmes. The best success stories in Bangladesh stem from NGOs taking innovative steps in areas where the private sector were too risk averse to enter (e.g. rural telecoms). If the objective is to create new markets then once new private sector players have entered the market, NGOs could look to divest in that market segment and reinvest in new 'frontier' markets that benefit the poor. This role is more akin to a 'social venture capitalist'. However if the objective is to generate revenues for the social part of the NGO then clearly remaining in profitable markets makes most sense.

**In short NGO run commercial enterprises can generate significant rewards, but there are considerable risks involved.** The analysis here indicates that there are varying financial returns to NGO run businesses. The type of return is likely to be a function of the capacity of the NGO to employ professionals to run these operations. Hence small NGOs in particular ought to think carefully prior to setting up such ventures due to the fact that the capacity to run businesses profitably is likely to be weaker. At the same time there have been clear examples of NGOs entering markets that benefited the poor and acted as a catalyst for private sector entry. This social venture capital role ought to be encouraged particularly given the comparative advantage NGOs have in linking rural producers with the wider market. We also argue that NGOs should to the extent possible register their businesses as independent entities. This will provide greater transparency to these ventures and will create a more level playing field with the private sector. Moreover any funds

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<sup>102</sup> Louis Berger 2004

**Box 3.5: A typology of NGO Business' and their legal status**

**Project Support Enterprises:** *registered under the Social Welfare Act.* Parent NGOs are normally registered under this Act (TMSS, JC, BRAC). A number of business activities have been undertaken as programs or projects of the main NGOs, i.e. the businesses do not have any separate legal identities. Typically separate books of accounts are maintained and financial reports are prepared according to the type of business. Examples of such businesses are all businesses of JC and TMSS, program support enterprises of BRAC such as seed production and processing, tissue culture, poultry businesses.

**Not for Profit Businesses:** *registered under the Companies Act 1994:* The 'not-for-profit' company is also widely used as a legal arrangement where the Companies Act 1994 (section 27 and 28) is used to create a company limited by guarantee. Examples of such organizations are Grameen Shakti, Grameen Telecom, Grameen Mothsha Foundation, Grameen Uddog and Grameen Shamogree.

**For Profit companies** *registered under the Companies Act 1994:* The Companies Act 1994 has been used to create private limited companies. Most are majority owned by the NGO, sometimes as joint venture companies with private sector participation such as BRAC Industries Ltd., BRAC Concord Ltd., BRAC Concord Lands Ltd.

**Banking institutions:** *registered under The Banking Act 2001:* has been used to create BRAC Bank.

**Public limited Companies:** GKT used the Companies act 1994 to float its poultry hatchery to establish it as Public Limited Company; BRAC Bank plans to do so in the near future. These companies are overseen by the Securities and Exchange Commission, and the reporting requirements thereof.

which are then used for the NGOs development activities ought to be recorded clearly in the financial records and could then qualify for tax exemptions. Clarifying these tax incentives is likely to encourage other private sector entities to channel resources for development activities.

**A common theme that emerges from this discussion on financing NGOs** – is that there is a need for regulatory reform and financial accountability improvements. We find that fiduciary weaknesses within several NGOs and the lack of a system that distinguishes reliable NGOs from 'fly-by night' entities are constraining external assistance to a proven service delivery model. The potential to access commercial sources of financing for micro-finance programs is also partly impeded by the lack of a modern regulatory framework overseeing this growing sector and the lack of a rating agency or certification body. Profits from commercial ventures cause resentment among the private sector and Government due to the lack of clarity with tax laws and the use of profits. As such there is a clear need to strengthen the regulations, the regulators and financial accountability requirements for the modern NGO sector – issues that we turn to next.



# Chapter Four: The Regulatory Framework and Financial Accountability Issues

**The weaknesses in the regulatory framework for the NGO sector in Bangladesh has not got in the way of, and has perhaps contributed to, the growth of the industry.** As discussed in earlier chapters a laissez-faire regulatory stance, an outdated legal framework and the lack of capacity of various regulatory agencies has provided considerable flexibility for NGOs to undertake new activities, expand their programs and diversify their funding sources, including entering into commercial ventures.

**Relative to the size of the sector and in spite of the regulatory weaknesses there have been few incidents of scandal or debacle in the NGO sector.** Several reasons can be cited for this. First, one must give credit to inherent altruism – which has been the basis for groups of people to come together for a greater goal and which sustains the sector. Peer pressure amidst NGOs is an important one and the role of apex bodies in training, harmonizing rules and ensuring indirect compliance with legal requirements is related to this. The donor community oversight and the training provided to the NGOs too have contributed to the relative lack of scandals. Nevertheless, one must not dismiss the fact that lack of capacity to enforce and lack of resources to investigate complaints by implementing agencies could also lead to an under-reporting of actual problems.

**There is a growing focus on NGO financial accountability, corporate governance and the regulatory framework.** NGOs in Bangladesh are increasingly being subjected to questions from government, political parties, the business community, beneficiaries, donors and the public. These include charges of tax avoidance, taking advantage of not-for-profit status to start businesses, collecting saving deposits without legal authority, involvement in politics, and the emergence of ‘fly-by-night NGOs’ among others.<sup>103</sup> Strengthening NGO governance, developing a certification system to screen out dubious NGOs and modernizing the regulatory framework is, therefore, all the more important if the sector is to effectively counter such attacks.

## 4.1 An overview of the laws affecting NGOs

**The legal framework for NGOs has not gone through any substantive reform in recent times.** This is surprising given the size of the sector described in chapters one and two. The earliest and one of the most important laws dates back to 1861 and the most recent relevant regulation was issued by the NGO Affairs Bureau (NGOAB), in 1982<sup>104</sup>. Invariably, the legal framework is outdated, obsolete and in some cases not in sync with modern NGO regulatory concepts.

**There are a plethora of laws and government agencies dealing with NGOs in Bangladesh.** There are twelve laws under which NGOs are registered and regulated<sup>105</sup>. The most

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<sup>103</sup> Khan, M. M. (2003)

<sup>104</sup> The only other development on the regulatory front is the introduction of the Hindu Religious Welfare Trust Ordinance of 1983, Christian Religious Welfare Trust Ordinance of 1983 and Buddhist Religious Welfare Trust Ordinance of 1983.

<sup>105</sup> The Societies Registration Act 1861, The Trust Act 1882, The Companies Act 1994, The Cooperative Societies Ordinance 1964, Charitable Endowments Act 1890, Wakf Ordinance 1962, Voluntary Social Welfare Agencies (Regulation and Control) Ordinance

important ones for the registration and operation of the development NGOs examined in this report are the Societies Registration Act 1861, Trusts Act 1882, Voluntary Social Welfare Agencies (Regulation and Control) Ordinance 1961, The Foreign Donation (Voluntary Activities) Regulation Ordinance 1982 and the Companies Act 1994. These are implemented by four Government agencies - the Social Welfare Ministry, the NGO Affairs Bureau (NGOAB), the Ministry of Commerce, and the Ministry of Women and Children.

**The Societies Registration Act of 1860 is one law that is used to register NGOs.** The Registrar of Joint Stock Companies (RJSC) in the Ministry of Commerce is responsible for registering any society formed for any “literary, science, or charitable purpose”.<sup>106</sup> Around 4900 Societies were registered under this Act including several large development NGOs. This Act is one of the most lenient with respect to fiduciary requirements. Other than filing the annual list of the governing body with the Registrar and receiving prior consent of the Government in case of dissolution, there is no other formal requirement that NGOs have to abide by. Crucially, the Act does not even specify whether the Society is expected to maintain accounts and audits although in practice the RJSC will likely not register the Society, without provision for accounts and audits in the Society’s governing rules.

**The Trusts Act of 1882 is another law providing the legal basis for the formation of NGOs.** A Trust can be established “for any lawful purpose,” whether private or public and can be created by any person competent to form a contract. No government registration is required and the trustee is legal owner of the property and personally liable for breach of trust.

**The Companies Act of 1913 (amended 1994) provides legal status to not-for-profit companies.** Not-for-profit companies can be registered with limited liability provided that the company applies any income for promoting its objectives and prohibits the payment of any dividends to its members. As with the Societies Act, the Registrar of Joint Stock Companies (RJSC) is the implementing agency. The Act provides the most rigorous legal framework for NGOs with clear directives on its fiduciary obligations. These include holding of annual general meetings, maintenance of accounts, and appointment of a registered chartered accountant as an auditor. Non compliance of directives may result in fines or imprisonment. The number of NGOs registered under this law is significantly lower than other laws possibly due to a combination of a lack of awareness of this option as well as its more rigorous legal requirements.

**A large number of NGOs are registered under the Voluntary Social Welfare Agencies (Registration and Control Ordinance), 1961.** This mandates registration for any formal or informal organization formed to render welfare services to children, youth and women, social work, or co-ordination of social welfare agencies. The reasons for its extensive use by NGOs includes (i) social welfare department officials are accessible at the union level making it easier for local organizations; (ii) organizations must register under this Ordinance to receive financial support from the Social Welfare Ministry; and (iii) under the Foreign Donations (Voluntary Activities) Regulation

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1961, The Foreign Donations (Voluntary Activities) Regulation Ordinance 1978, The Foreign Donation (Voluntary Activities) Regulation Ordinance 1982, Hindu Religious Welfare Trust Ordinance of 1983, Christian Religious Welfare Trust Ordinance of 1983 and Buddhist Religious Welfare Trust Ordinance of 1983.

<sup>106</sup> These include literature, fine arts, education, libraries, museums, etc. Environment, human rights, and historic preservation qualify only under a modern, progressive concept of “charitable” and there are no provisions for social or sporting clubs, self-help groups, contemplative societies, etc.



Ordinance 1978, a local organization receiving foreign funding for channeling to other organizations can do so only if those organizations are registered under this ordinance.

The purpose of this ordinance was to control voluntary organizations and hence it gives extensive powers to the government with respect to NGOs. The Ordinance is administered by the Social Welfare Department of the Ministry of Social Welfare and it has broad discretion to suspend or dissolve an NGO without recourse to judicial appeal. For example, if after making an enquiry the Ministry is satisfied that a registered NGO has failed to comply with the provisions of the ordinance or any other irregularities, then it may suspend the governing body and appoint in its place an administrator or caretaker body. Box 4.1. describes the suspension of Gano Shahajjo Sangstha's (GSS) activities - the seventh largest NGO at the time - in 1999. Though the governing body may appeal to the central government, the final decision, following the appeal, shall be final and shall not be called in question in any court. Curiously, the Ministry of Women's Affairs registers and oversees NGOs dealing with women, even though it has not been empowered under the Social Welfare Ordinance.

**The Foreign Donations (Voluntary Activities) Regulation Ordinance of 1977 (amended 1982) oversees donor flows to NGOs.** This Ordinance requires that any organization carrying out voluntary activity using foreign donations is registered with the NGO Affairs Bureau (NGOAB). Each foreign grant must be approved and monitored by the NGOAB. The Foreign Contributions (Regulation) Ordinance of 1982 (FCR) expands the scope of the law to all contributions to NGOs from abroad. While the NGOAB has not actively used the powers under the 1978 and 1982 Ordinances to take action against violating NGOs in the past, it has recently started to do so with one legal case already instituted and two more in process.

#### **Box 4.1 The suspension and re-birth of a large NGO: the case of Gono Shahajya Shongstha**

In 1999 the Government of Bangladesh took over the administration of a large NGO after investigations revealed misuse of foreign donations and gender discrimination. This was the first time the government stepped in and took over the running of a big NGO in Bangladesh.

Gono Shahajyo Shaungstha (GSS), set up in 1983, focused on village education programs and engaged in social mobilization and advocacy. By 1999, GSS, with funding primarily from the EU, DFID, CIDA and DANIDA, was one of the largest NGOs in Bangladesh. At that time, GSS's education program was reaching 200,000 poor children in 750 primary schools across the country. The allegations against GSS and its Executive Body, brought on primarily by GSS staff members, led to an investigation carried out by the NGO Bureau and a High Court Order for the dissolution of the Executive Body in 1999. These allegations centered around the mis-use of funds relating to the development of its new headquarters office and gender discrimination. The management of GSS was transferred to the Ministry of Social Welfare, which in turn appointed a three-member Caretaker Body for its supervision. The High Court Order was contested in court by the previous Executive Body, which claimed that allegations against GSS were politically driven. During the four and a half year legal battle over GSS, ongoing GSS programs closed and about 6,400 employees, including 4,000 teachers, were made redundant.

In September 2003, the High Court cleared GSS of all the charges and the management and administration together with GSS's assets and liabilities were handed over by the Caretaker Body to a new Executive Committee that was formed. GSS started operating again in 2004 following its registration with the NGO Affairs Bureau. Since then, BRAC, under a project that sub-contracts smaller NGOs to implement education programmes, has given a US \$0.5 million grant to GSS's education program for a period of three years beginning January 2004. Currently 350 schools are operating with approximately 50,000 students enrolled.

**The taxation regime for NGOs in Bangladesh is unclear.** The 1984 Income Tax Ordinance, as amended through July 2004, stipulates that income used for “charitable” purposes are exempt from taxes. Thus the way the law is written, NGOs would not be required to pay tax on income from all sources, including income from commercial activities. However the Finance Acts of 1998 and 1999 made NGOs subject to tax on their income, though the Income Tax Manual does not reflect these changes. At the same time micro-credit surpluses are exempt as long as the NGO is registered with the NGO Affairs Bureau. There are other exemptions too<sup>107</sup>.

**The term ‘charitable purpose’ is further complicated by the increasing numbers of NGOs in Bangladesh that are undertaking commercial activities to fund their development programs.** It is not clear whether the organization should still be exempt from tax on the surpluses generated by these operations. NGOs remain confused about the taxation regime and BRAC is currently in litigation with the National Bureau of Revenue regarding these issues.

**The 2005 Budget has made donations to NGOs in Bangladesh tax deductible in principle.** Prior to 1992/93, the Income Tax Act provided for 100 percent deduction of the amount contributed to charities. However rampant tax abuse resulted in this being withdrawn except if the beneficiaries were certain health facilities, registered organizations benefiting persons with disability, and the Aga Khan Development Network. These clearly were an ad-hoc list of exemptions and the 2005 Budget has widened this list to cover all philanthropic and educational institutions approved by the Government. As discussed in section 3.1.3. the implementation of this ‘approval’ process could be delegated to an independent certification agency.

**Another grey area in the legal framework for NGOs in Bangladesh is the definition of political activities and to what extent an NGO can be involved in political activities.** Political activities, broadly defined, comprise a range of activities from public education to electioneering. “Electioneering” which is supporting or opposing candidates for office and campaign funding fall at the extreme end of the spectrum of political activities and are clearly the most controversial form of ‘political activity’.

**Another shortcoming is the absence of modern and appropriate procedures for censure and appeals.** The Societies Act, for instance, has no provisions for fines, penalties, or involuntary dissolution. The Director of Social Welfare (DSW) may “suspend the governing body” of a NGO if it has committed any irregularity with funds, any mal-administration in the conduct of its affairs, or has failed to comply with the provisions of the Ordinance. No NGO can be dissolved on its own motion though. The DSW may recommend that the Government dissolve a NGO because it has violated its constitution, the Ordinance, or rules made there under, or acted “in a manner prejudicial to the interest of the public”. Before recommending dissolution, the DSW need only give the NGO such opportunity to be heard “as it thinks fit”. An NGO ordered to be dissolved has 30 days to appeal to the Government, but there is no right to appeal to a court. Any person who contravenes the Ordinance or any rule there under or makes a false statement to the DSW can be fined or imprisoned for up to six months. Where an offence is committed by an NGO,

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<sup>107</sup> Income from “house property” held under trust or other legal obligation wholly for religious or charitable purposes are exempt but this does not apply to NGOs registered with the NGOAB. Another interesting feature is that there is tax exemption for income that is not applied to charitable or religious purposes during income year but is accumulated or set aside for such purposes for not more than 10 years, provided the taxpayer notifies the Deputy Commissioner of Taxes and invests the money in Government securities or with the Post Office Savings Bank.

every director or officer of it is deemed guilty of that offence unless he proves that the offence was committed without his knowledge or consent.

Under the Foreign Donations Ordinance, for “reason to be recorded in writing,” NGOAB can inspect or, acting under the Code of Criminal Procedure, seize accounts and other documents after providing a reasonable opportunity to be heard. NGOAB can cancel the registration of an organization or stop any activities for a failure to submit required declarations, wilful submission of false declarations, or any other contravention of the Ordinance. Anyone who receives or uses a foreign donation in contravention of the Ordinance or any rules there under is liable for a fine of double the amount of the donation or imprisonment for up to three years.

**Other than an appeal to court for relief against actions of various implementing agencies, there is no internal or quasi judicial forum for appeal or interim relief.** Any appeal against the NGOAB has to be filed in court. The court process takes its due course and in the interim, irreversible damage can happen to the NGO as donor sources dry up and programs wind down eroding the NGOs image in the community. The foregoing also increases the incidence of rent seeking in some cases. Having an appeal mechanism within either the implementing agencies or a joint appeal venue prior to court appeal will help to establish a transparent, cost effective and accessible relief to aggrieved NGOs.

#### 4.2: Implementing Agencies

**The NGO Affairs Bureau was conceived as a one-stop shop for NGOs.** The rationale for setting up NGOAB<sup>108</sup> in 1991 was a large backlog of projects pending Government approval under the then-existing system, which required multiple levels of government review. Though NGOAB was conceived as a one-stop shop for NGOs administering foreign funds, it could never be one in reality. This is because all NGOs have to first establish themselves under the various Acts discussed above that are administered by other agencies and registration with NGOAB also requires the approval of the Home Ministry, a line ministry and recently approval from local Government. NGOs are now required to get clearance certificates from concerned local government officials prior to applying for clearance of subsequent funding for that project. The certificates are not always easy to obtain and some NGOs reported being forced to pay rent-seekers for these.

**NGOAB is regarded as the primary regulator as most development NGOs were supported by foreign funds in the 1990s.** NGOAB undertakes a diverse set of functions. The main ones are NGO registration; approval of project proposals; releasing funds and monitoring NGO projects<sup>109</sup>. Prior to registration by NGOAB an NGO must be approved by the Home Ministry and at least one line ministry – in practice both these steps take longer than their stipulated time. The NGOAB has the same number of staff in 2005 as in early 1990’s, and yet the number of registered NGOs has tripled<sup>110</sup>. There are about 1200 NGOs currently receiving foreign funds

<sup>108</sup> World Bank’s 1996 study, Pursuing Common Goals.

<sup>109</sup> Other subsidiary, but time-consuming functions, includes receiving information on foreign travel by NGO personnel; approval of expatriate consultants and all other matters relating to NGOs receiving foreign funds.

<sup>110</sup> The Bureau started operations with 66 staff positions with an additional post created in 1998. There are a total of 15 officer-level staff members including the Director General and Directors. Five officers are involved in field level work that entails examining projects and providing fund clearance. One officer is responsible for liaising with different ministries and international agencies and another for NGO registration and renewal. A total of 1882 organizations had registered with the Bureau till August 2004. Of these, 1100-1200 were estimated to be receiving foreign funding. Around 100 new NGOs are registered every year while the number of renewals ranges from 300-500.

though almost 1900 are registered with the NGO Affairs Bureau. At present, around 150-250 projects are inspected annually following complaints registered with the Bureau.

**Accounting and audit requirements exist but the NGO Bureau seldom assesses the quality of these audits:** As per these ordinances, organizations registered with the NGOAB are expected to provide annual reports and audits with regard to the projects funded. Unless these are accepted and approved by NGOAB, subsequent applications for additional fund clearance for the same project will not be released. The amended 1978 ordinance states that only one bank account can be maintained for receiving foreign funding. Accounts are to be maintained following NGOAB guidelines and books of accounts must be audited by a chartered accountant selected from a list of audit firms eligible to audit NGOs. This list is not particularly selective as around half of the 264 registered auditing firms are authorized to conduct audits by the NGOAB.

**Department of Social Welfare (DSW) registers and deals with the NGOs whose purpose is to render welfare services as defined in the Voluntary Social Welfare Agencies (Registration and Control Ordinance) 1961 Act.** There are a staggering 45,536 organizations registered with the DSW as of late 2004, though only a small share are active NGOs. In practice the DSW is only able to fulfill its registration mandate. It is unable to carry out its monitoring function except on an occasional basis when investigations are launched following disputes within an NGO's governing board or complaints from the public. A survey of 83 NGOs carried out in 2005 reported frequent delays and problems with registration. The DSW also provides limited funds to NGOs to implement various social welfare programs, with a maximum grant amount of 100,000 taka. However the monitoring and auditing of these grants is weak.

**The Registrar of Joint Stock Companies (RJSC) carries out registration functions under both the Societies Act 1861 and the Companies Act 1994.** Around two thirds of the 100,000 odd registered entities are companies and only around five percent are Societies. A review of 2004 records show that around 84 Societies were being registered a month but the current recording system makes it effectively impossible to determine the stock and flow of non profit companies. There are a few professional staff in the RJSC and there is no clear separation of staff for dealing with Societies or Companies. The Registrar's office neither has the funds nor the manpower to effectively follow up on registered organizations. They can ask for information and clarifications, but rarely are investigations or charges drawn. The absence of computerized systems makes it difficult to verify different information such as how many or which organizations have submitted audited financial reports, which Societies have provided the annual list of governing body members, or even the number of not-for-profit companies.

### 4.3 Corporate Governance and Financial Accountability

**The legislative framework relating to internal governance, including accounting, disclosure and transparency, for NGOs are rudimentary.** As discussed earlier, the Societies Act includes a requirement for an annual meeting but does not require the submission of annual accounts or audits. The Trust Act requires clear accounts to be maintained but there are no requirements for external audit. The Companies Act is the only law that contains any fiduciary responsibility rules and not for profit companies face extensive book-keeping, audit and report-filing requirements. However, as discussed earlier the RJSC is unable to enforce these requirements.

Interestingly, the Administrator of Waqfs and other religious trusts also requires the submission of audited accounts.

Not only are the laws inadequate in this area but there are notable differences in the regulatory requirement of the various laws. Some of these refer only to the maintenance of accounts and books but do not give any specific guideline as to what accounting method to follow. NGOAB states double entry accounting while the Companies Act suggests the use of accrual basis. The accounting requirements in the Companies Act lack clarity and at times are incompatible with International Accounting Standards (IAS).

**There are risks with the current structure and composition of NGO Boards.** Most NGOs in Bangladesh are still first generation institutions. They face the same corporate governance problems associated with the for-profit sector in Bangladesh as they tend to be founder dominated and are typically governed by friends and/or family.<sup>111</sup> The founder will typically head management as well as hold important Board positions such as the Chair or Secretary. These dual roles have the risk of creating conflicts of interest and compromises organizational accountability.

Board and general members typically do not have term limits. Some of the more established Dhaka based civil society personalities (e.g. NGO professionals, social workers, academics, activists) tend to be represented on numerous NGO Boards. While these individuals are perceived to bring a level of respect and accountability for a particular organization, it also raises doubts as to whether they can effectively govern that many institutions. When Board elections are held, they appear to take place on a consensus basis with members tending to rotate posts, limiting the scope for new members. NGO Boards, therefore, tend to remain static and perhaps less prone to challenging decisions of the founder. This lack of understanding on the roles and responsibilities of Board members may in turn plague succession planning and continuity of organizations following the absence of the founder or other key individuals.

**Financial delegation authority and payment procedures vary considerably across NGOs:** Smaller NGOs tend to have Board members as signatories to the organization accounts. In the case of large organizations, the Board delegates authority at different levels. Certain NGOs set up purchase committees and submission of comparative quotations depending on the amounts involved – these vary from anything above Taka 5000 in one NGO to above Taka 100,000 for another.

**Accounting capacity in most NGOs appears reasonable though the use of technology is sporadic.** The demand for accounts related information can be very large due to the multiplicity of funding sources, projects and areas of operation. Most organizations higher qualified personnel in the head accountant's post and for larger organizations, trained accountants were recruited at the regional or area offices to oversee the accounts of multiple branches. Large national NGOs like BRAC and Proshika have to a large extent computerized down to the branch level while ASA is automated centrally. The smaller organizations were more likely to have full manual systems due to resource constraints. PKSf has recently started rolling out an accounting software program for their partner organizations.

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<sup>111</sup> Saifullah, A. K. M. and Mawla. A. Q. M. G. (2003)

**Donor financial reporting requirements are questionable.** Smaller NGOs with different donors supporting separate projects had to devote comparatively more time and resources in meeting multiple reporting requirements. Another common donor practice that raises transaction costs is their insistence on NGOs opening separate accounts for their funded projects. Discussions with NGO accountants indicate that standardizing donor financial reporting formats would significantly reduce their workload. The perception of a sample of NGO accountants is that donors use a range of lax accounting principles for their reporting requirements. These include dependence on cash basis accounting, disregarding trial balance as a tool for verifying double entry system of accounting, and a propensity to focus only on their funded projects as opposed to consolidated accounts and audits.

**PKSF is credited for introducing some standardization of financial management practices.** PKSF have instituted certain International Accounting Standards (IAS) for financial reporting and as a result PKSF funded NGOs are fairly uniform in their financial reporting, audits and presentations. PKSF partners previously operated on a cash basis but have gradually moved towards accrual basis of accounting. Their experience demonstrates that adequate capacity building and training can lead to NGOs attaining satisfactory accounting standards. PKSF recently reduced the number of audit firms eligible for auditing partner organizations, to maintain quality.

In short, financial management practices of NGOs have been shaped by donor requirements, absence of a coherent and uniform accounting standard within the regulations, and lack of awareness on the benefits of adopting sound accounting practices based on International Accounting Standards (IAS). As a result, there is no standard basis of accounting with NGOs following a range of systems - cash, accrual, modified accrual, hybrid and so forth. The Bangladesh Accounting Standards (BAS) are normally not applied and differences in presentation, disclosures, terminology and accounting policies exist.

**Internal audit practices vary significantly by size of NGO.** Some of the smaller organizations did not have internal audit teams or an internal auditor, while larger institutions with multiple branches did. The internal audit team in BRAC reports directly to the Executive Director and is the largest among NGOs with 100 auditors employed. The Grameen Bank's internal audit team is required to check whether targeting criteria for borrower identification has been followed by visiting a sample of client households.

#### **Box 4.2: Microfinance Transparency Award**

In 2004 CGAP announced a Financial Transparency Award for microfinance institutions. The announcement states that “Transparency is essential if the microfinance industry is to reach scale. Investors, donors and, most importantly, domestic savers, will only place their funds where they can reliably assess risk and return on the basis of standardized and comparable information. In a further effort to promote transparency, the award aims to highlight financial reporting disclosure and encourage microfinance institutions to adopt International Financial Reporting Standards (IAS1 on Disclosure) and the industry-specific CGAP Disclosure Guidelines for Financial Reporting by Microfinance Institutions. Compliance will indicate that an MFI's financial statements contain the information necessary to fully understand performance.” This level of disclosure is also a prerequisite to calculating ratios about performance that allow MFIs to track their performance accurately over time and also compare it with what other MFIs are doing. Information about the award is available at [www.cgap.org/fintransaward/index.shtml](http://www.cgap.org/fintransaward/index.shtml).

**While annual external audits are common, their quality varies significantly.** Analysis of a range of audit reports shows that the quality and comprehensives are mixed at best. Many NGOs have separate audit reports for different projects without a consolidated one for the entire organization. Donors are partly responsible due to their focus on the specific project that they finance. The auditor to be appointed and audit fee are approved in the annual general meeting – however fees are such that audit firms often cannot afford to spend quality staff time on NGO audits.

**Public access to audit reports is limited and undermines accountability:** An extensive web-search failed to find any NGO, other than BRAC, who posted their audit report on the organization's website. While the laws under which NGOs are registered do not require public disclosure of audit reports, doing so voluntarily would improve public accountability and transparency.

#### 4.4 Improving the institutional framework for NGO regulation

**Human resource development, computerization and improvement in procedures need to underlie any regulatory reform in the NGO sector.** Training efforts so far have concentrated on building the capacity of NGOs and there has been less focus on training regulatory agencies. This needs to be rectified. An appropriate data collection mechanism needs to be introduced to help in devising plans for the oversight and development of the sector. The use of complaints from the public, or deviation in use of funds from approved purposes as the triggers for investigation by the regulatory bodies also need to be revisited.

**An Independent NGO Commission that assumes the functions currently performed by the DSW, NGOAB and Women Affairs Department is an option that could be considered.** The Commission's aims would be to maintain an effective framework within which non profit organizations can operate and work with NGOs to encourage good practice. The Commission ought to be empowered to deal with the incorporation or establishment of NGOs, apex bodies and licensed certification bodies. There are precedents for independent regulatory bodies in Bangladesh, in telecoms and energy, as well as organizations like the Charities Commission in the UK (see Annex 4.1).

**The proposed Commission would need to build upon the lessons of other independent commissions.** Lessons from regulatory bodies in energy and telecoms, as well as the recent experience with setting up the Anti-Corruption Commission, need to be absorbed prior to setting up a similar body for NGO oversight. The Commission ought to report directly to Parliament in order to ensure its autonomy and the Commission's Board ought to be composed of Commissioners selected from both the public and private sector. The Commission need to be adequately funded and must be able to retain its fee and fine income. Donors could provide the initial seed capital for the Commission in order to get it off the ground. It is crucial that the Commission is able to determine its staffing and salary structure independently. Furthermore, it ought to comply with international good practices on governance and disclosure.

**The proposed NGO commission can encourage uniformity in accounting standards.** Uniform standard(s) of accounting (e.g. uniformity in NGO accounting principles, reporting and presentation of NGO financial statements / audit reports etc) need to be introduced for the sector

with contradictory systems phased out. These standards do not necessarily have to be new ones as there are international standards that can be applied to the local context<sup>112</sup>. The lead for this undertaking should be taken by the proposed NGO Commission in consultation with accounting bodies such as the ICAB, NGOs and donors. The Securities and Exchange Commission (SEC) is the country's only regulatory body that is working to enforce accounting standards for listed companies<sup>113</sup>. The NGO regulatory body could play a similar role for the NGO sector and in particular encourage donor harmonization of financial management requirements.

**Certification bodies can reduce the regulatory burden of the proposed NGO Commission.** The proposed NGO Commission will need to use its scarce resources to deal with big NGOs and apex bodies, concentrate on overall policy issues and capacity building of the sector. Thus it is necessary for the Commission to be assisted by Certification Bodies that are private sector owned corporate entities with sector specific expertise who can be licensed to certify and sanction medium, small and very small NGOs. This delegated legal authority is superior to membership based Self Regulatory Organizations, such as ADAB or FNB, as experience has shown that they have problems enforcing rules. Certification Bodies can rate NGOs and provide references to donors and the public for a fee. A seal of approval from a certification agency can be used by the Ministry of Finance to determine the list of NGOs to whom donations are tax exempt. They can also help in facilitating NGOs' work and relations with relevant ministries and regulatory authorities. The NGO Commission can also be the first level appeal avenue for complaints against certification bodies. Box 4.3. discusses the experience of a certification body in Pakistan.

#### Box 4.3. NGO Certification in Pakistan

The Pakistan Centre for Philanthropy's (PCP) non-profit organizations certification program is the first initiative of its kind in the South Asia Region, although it is based on other similar initiatives, particularly one in the Philippines. The objective is to facilitate non-profit organizations of all kinds, to diversify their resource base and expand their programs, while at the same time demonstrating their commitment to "best practices" in governance and management. Certification is a "seal of good housekeeping" for organizations that meet defined standards of organizational effectiveness based on an independent evaluation of governance, financial management and program delivery. PCP staff spend two to three weeks reviewing NGO documents and examining the operations of NGOs before deciding whether or not to recommend them to the Certification Panel that is made up of a majority of private sector representatives along with two government officials. The process is voluntary and does not come under the control of any government ministry, and organizations that do not qualify the first time but would like to try again are offered help to create and implement an improvement plan. Certification is recognized by the authorities and NGOs that are certified also obtain not-for-profit tax exempt status from the Central Board of Revenue, something that must be renewed every second year. While the certification process is primarily aimed at improving NGO performance and transparency so that donors, can better judge which NGOs are reliable, it has the added effect of creating a general sense of credibility about NGOs, thus improving the reputation of the NGO sector. Although the process only began last year and is entirely voluntary, it has already attracted the better NGOs since no one wants to be left behind. More information can be found on the PCP's website at [www.pcp.org.pk](http://www.pcp.org.pk).

<sup>112</sup> The background paper for this chapter - Khan (2005) - has a detailed review of the applicability of International Accounting Standards for NGOs in Bangladesh

<sup>113</sup> Non-complying audits are referred to the ICAB for action. They allow 60 days for ICAB to look into the matter and if steps taken are unsatisfactory, they have the authority to directly contact the auditor and can de-list them from auditing other listed companies for up to 5 years.



The proposed Commission would also require powers to deal with troubled NGOs including dissolution through proper process; due process for sanctions and installation of appropriate appeal procedures for all NGOs, apex bodies and Certification Bodies. The law needs to also introduce conflict resolution mechanisms that would involve NGOs in disputes with other NGOs, donors, Government and clients.

**The proposed certification system would be voluntary and focused more on creating incentives for better corporate governance and on using moral suasion rather than legal enforcement.** In order to increase incentives for certification, donors could request certification prior to releasing funds above a certain threshold. Certification Bodies can finance themselves from public donations and fees from NGOs certified by them. The Certification Bodies ought to be required to report to the Commission periodically on its activities and compliance; refer non compliance of Commission regulations to the Commission for action and refer conflicts that cannot be resolved at its level to Commission. A Certification Body's license can be revoked if there are deficiencies in its practices.

#### 4.5 Improving the laws relating to NGOs

**The focus of regulation ought to be shifted to fostering better governance and accountability in the NGO sector, rather than the micro-management of foreign funds.** All relevant laws and regulations related to the NGO sector need to be harmonized and streamlined towards a uniform regulatory framework to avoid duplication, overlapping, and contradictory requirements. This does not necessarily mean that existing laws/regulations need to be repealed and replaced with a new all encompassing one. Instead, the existing laws can be modified by incorporating standardized requirements such as the Board structure, holding of annual general meetings, financial reporting, accountability to regulatory agencies and so forth. The framework needs to move away from the stereotyped welfare approach to one reflecting the present day scope of development activities. Arbitrary powers of the State that allow for interfering with NGO structures (e.g. dissolving/suspending the governing body and replacing it with an administrator) need to be removed and the right to legal appeal against government actions needs to be instituted. Finally, the process of registration needs to be simplified and the steps made publicly available.

**In undertaking the legal reforms, a number of key principles need to be ensured.** Generally broad discretion should be given to NGOs to structure their organization in a way that suits their individual goals and purposes. NGO activities in Bangladesh span a number of activities and it is important that the law is not written with a particular group in mind, but allow for flexibility in application. It is important to have tiered regulation based on size and activities of NGOs. All penalty provisions should be structured so as to provide a gradation of sanctions, with fines and other intermediate sanctions being applicable before the ultimate penalty of board suspension or dissolution can be used. Administrative discretion should be reduced, reasons for imposition of penalties should be spelled out more clearly, and judicial appeals should possible to contest any adverse ruling or penalty.

**In consolidating the laws for the formation of NGOs, it important to merge the definitions of “social welfare agency” and “organization involved in voluntary activity” into a single, new definition of “Public Benefit Organization” (PBO).** They can be defined as

organizations organized and operated exclusively for public benefit purposes (e.g. education, poverty, health, environment, art, science, etc.). In this context, the definition of an organization as a PBO ought to be based on its purposes and activities without regard to whether its funding is foreign or domestic. Certification as a PBO ought to be a condition for receiving significant tax and other benefits (e.g., foreign grant eligibility, tax exemption, deductible donations).

**Apart from direct electioneering, banning NGOs from the wide range of activities that could possibly be defined ‘political’ would not be appropriate in a country that is democratic.** As a general principle a broad range of political activities ought to be permitted except for the funding or support in favor or against candidates for public office. These restrictions reflect a balance between the guaranteed rights to freedom of speech, expression, and press and laws regulating elections, political parties, and campaign funding. NGOs in other countries are generally prohibited from electioneering and campaign funding, and limits are often placed on direct and grass-roots lobbying too.

**An appropriate set of regulations are necessary for micro-credit NGOs.** The micro-credit sector in Bangladesh lacks the regulatory framework that an industry of its size merits. As discussed in chapter two, the ‘laissez-faire’ regulatory framework contributed to the growth of the sector. However, now that the sector is past its infancy, and close to \$500 million dollars of savings have been mobilized from poor households, it is necessary to modernize the laws governing micro-credit activities. Currently only the Grameen Bank has a special law to govern its activities as it is registered as a specialized bank. A multi-stakeholder committee is spearheading the task of coming up with a legal framework for NGOs involved in micro-finance. While this process does not have the mandate to propose reforms of existing legislation and institutions overseeing the whole NGO sector, it may well be the case that in practice this new law will cover a large number of key lacunae in the legislation governing the overall sector.

**Modern procedures for dealing with distressed NGOs and the mergers and exit of NGOs need to be developed.** An enabling legal framework that permits the merger of NGOs help smaller NGOs to continue their mission by joining forces with bigger ones. In the long run, economies of scale could help to improve governance, accountability and disclosure of the smaller and medium size NGOs. This will also help in the oversight of the sector. Similarly, a legal mechanism for managing distressed NGOs, and winding up of NGOs, will help to improve the development of the sector. Except in the case of trusts, where the court steps in to appoint trustees, and the Companies Act that empowers the court to intervene in the management and winding up of NGOs registered under the Act, there are no such powers in other legislation governing NGOs to manage the absence of management and ultimate winding up. This lacuna needs to be addressed.

**The Societies Act ought to be replaced based on the current state of the sector and in line with applicable international good practices.** The new law amongst other things would need to include issues such as – (i) categorization of different types of NGO (ii) regulatory exemptions of small NGOs that are not engaged in micro-finance, with an option to bringing them under regulation when certain triggers go off, (iii) permitted and prohibited activities of NGOs, (iv) internal governance requirements (v) audit and accounting requirements, (vi) tax treatment, (vii) appeals, sanctions and penalties that are commensurate with offences and (viii) transition provisions for exiting societies.

**In addition to the Societies Act other laws would need to be repealed and amended - the following are suggestive changes.** (i) The Trust Act 1882 could be amended to update it on duties of trustees, failure to comply with fiduciary duties, incorporating case law developments and bringing it under the purview of the Commission (ii) The Companies Act 1994 could be amended in line with main NGO law. (iii) The Wakf Ordinance 1962 and other religious trust laws ought to be reviewed to modernize and improve governance (iv) the Voluntary Social Welfare Agencies (Regulation and Control) Ordinance 1961, The Foreign Donation (Voluntary Activities) Regulation Ordinance (1982) can be repealed.

**Bangladesh needs to review its tax regime for NGOs and clarify the scope and applicability of exemption.** In view of international good practices, income in the form of donations, grants, membership dues and micro-credit income of NGOs ought to be exempted from tax. However passive investment income and income from active trade or business must be taxed, in order to create a level playing field with other private sector competitors. Deductions for donations to NGOs have recently been re-introduced in the 2005 Budget.

The Income Tax Ordinance 1984 has made it mandatory for all NGOs working in Bangladesh to submit income tax returns. However, many small and medium sized NGOs, assume that their not-for-profit nature exempts them from this requirement. Moreover, whether the income of NGOs is exempted from tax or not is decided only after submission of their returns. This problem is further compounded by the opaque rules and procedures regarding taxation and tax exemptions for not-for-profits as discussed earlier. Hence, the tax laws related to not-for-profits need to be simplified and compiled as a separate section with focus on providing greater incentives for local resource mobilization for the sector. There also needs to be greater awareness and enforcement of NGOs filing their income tax returns.

#### **4.6 Improving corporate governance and financial accountability practices within NGOs**

Based on our earlier analysis we suggest a number of broad areas where corporate governance and financial accountability of NGOs can be improved – suggested legislative and regulatory improvements related to strengthening financial accountability have been covered above. These improvements are in many respects applicable to the corporate sector as well, and reflect the weaknesses that exist in both the for profit and not for profit sectors.

**Board composition:** Boards and general bodies should ideally be constituted with a diverse group of individuals bringing different skills and expertise. The size of the Board is an important consideration for effective decision-making since smaller boards may lack sufficient debate while large boards can be unwieldy and ineffectual.<sup>114</sup> There should be term limits on Board members to allow for rotation, and close relatives and friends should be avoided or phased out.<sup>115</sup> Management and Board should ideally be separated so that the Chair (Board) and the Executive Director (Management) posts should not overlap. Board members should be oriented on their roles and

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<sup>114</sup> BEI (2004)

<sup>115</sup> For organizations such as privately funded family foundations or family trusts, the issue of family/friends membership or term limits may not be appropriate. If, however, such organizations become dependent or start attracting public funding, then there is a stronger case to be made for the above restrictions.

responsibilities and understand the consequences of their decisions.<sup>116</sup> Involvement of beneficiaries in Boards and/or in management and policy decision making process can be beneficial in better understanding the needs of the clients that NGOs purport to serve. This would also enable them to be more accountable to their constituents.

**Internal financial management policies:** NGOs should develop management and financial policies, service rules, reporting and documentation guidelines from an early stage of their development. Financial policies should provide details on accounting convention, depreciation, revenue recognition, taxation, recognition of government grants, loan provision, accounting for expenses and so forth. Procurement policies and roles and responsibilities of audit committees and internal audit teams need to be detailed. There should be budget allocation for capacity building of employees including accounts staff. All of these guidelines must be available and communicated to all staff. NGOs should invest in automating their accounting systems as the benefits of computerization include increased efficiency, easier information sharing, and a reduction in duplication, errors and fraud.

**Capacity building:** Building the capacity of the NGO sector in accounting and auditing is essential. PKSFs experience of training their partners will be of use to apex bodies like FNB that are planning to run similar programs. It is advised that resources be allocated for hiring accounting professionals or that bodies such as ICAB are involved in this process to ensure due diligence in designing the training programs. Lastly, the ICAB or other similar institution will need to play a more active role in developing trained professionals for effectively serving the not-for-profit sector.

**Annual audits and financial transparency:** Public misconceptions about NGOs would be limited if there were a consistent set of disclosure requirements and in general greater information on NGO programs, funding and expenditures. The laws under which NGOs are registered do not require public disclosure – nevertheless ensuring uniform public access to NGO audit reports would be an important part of strengthening public accountability. In cases of NGOs handling public savings deposits, financing from the Bangladesh government, or receiving benefits such as tax deductions of citizen's donations, public access to audit reports should be mandatory. This could be in the form of posting the audit reports on the organization's website, making copies freely available in the head and branch offices, making copies available at public libraries and so forth.

**A next step could be to establish a committee with a mandate to modernizing legislation governing NGOs.** The members of the Committee need to be carefully selected from a pool of experienced professionals who are have the necessary experience and understand the NGO sector well. This high level committee could be tasked with building upon the analysis in this chapter by undertaking a detailed review of the relevant laws and proposing new legislation and amendments to existing laws. The committee could also draft a law that establishes the proposed NGO commission. One option could be that this committee be the same as the one charged with developing the micro-finance laws as this committee includes Government and industry representatives, though its composition would need to be broadened to include non micro-credit practitioners.

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<sup>116</sup> For example, PKSF loan conditions require that three Board members act as guarantors. Failure to repay may result in the seizure of their assets, even if they are registered with limited liability.

**There are risks involved with amending the regulatory framework.** The main risk is that over-regulation or poorly designed regulation stifles the NGO sector. As the regulatory framework is modernized the first principle should be enhancing the space given to NGOs to innovate and scale up their activities. Regulations should be ‘facilitative’, and excessive or poorly designed regulation must be avoided at all costs. These risks can be mitigated if changes are done in a fully consultative manner, as suggested above, and various options are explored with adequate time and resources provided to evaluate these choices. A second risk concerns the proposed independent NGO Commission. Independent regulatory commissions in Bangladesh have thus far had a mixed track record, with difficulties in recruitment, funding and mandates. Lessons from these experiences need to be absorbed prior to setting up a new institution.



## Chapter Five: Scaling Up Through a Strategic Compact

Despite the striking progress made on many fronts, there remain large development challenges and unmet needs in Bangladesh. For instance while infant mortality has declined, neo-natal mortality is proving stubbornly hard to bring down. While strides in school enrolment and gender parity in primary has been achieved, drop-out rates among the poor at the early stages of secondary school remain high<sup>117</sup>. Micro-credit has reached vast numbers of poor households nationwide and yet there remain significant pockets of the country with limited access to financial services, particularly ones targeted to the poorest. While female empowerment indicators have undoubtedly improved due to in part to NGO activity, there remain significant social challenges confronting women in both the domestic and public sphere.

Hence there is a clear need for the provision of improved services to the poor and a need to promote access to existing services. Chapter two has illustrated that NGOs are playing a significant role in service delivery and advocacy and that these interventions are generally well-targeted and have had a positive impact on their clients. However, the wider ‘macro’ impact has been curtailed by the relatively ‘micro’ nature of some of these activities. For instance the growth and employment impact of NGO loans has been limited by the small size of loans. Another example is that the NGO impact on neo-natal mortality is constrained by the relative lack of specialized post-delivery care. That said an unchecked future expansion of NGO services across the board may not necessarily prove the best means of ensuring pro-poor service delivery for a number of reasons. First this relates to questions of whether this will limit the capacity of Government to deliver these services in the long run and whether it will weaken the accountability relationship between provider and client. Second, advocating an expansion in NGO services, leads to questions relating to the capacity of NGOs to deliver quality services retaining their focus on the needs of the poor. Third and related to this are issues of how best any growth in NGO programs ought to be managed, particularly in light of the weaknesses in financial accountability and traditional contracting mechanisms discussed in earlier chapters. This chapter examines these issues, by drawing on the findings from the earlier chapters. We focus on each issue in turn in order to answer the key question that this chapter poses: ‘Is further NGO growth desirable, is it possible and how is it best managed?’

### 5.1 Does further NGO growth make sense from a public policy standpoint?

The draft Bangladesh Poverty Reduction Strategy Paper<sup>118</sup>, articulates the role of NGOs primarily in the context of improving service delivery. The issue is whether the status quo size and type of services that are currently being provided are at an ‘optimal’ level or is there a case for a change in scale or mix of activities? How does this relate to the role of central and local Government? In certain cases is it better for NGOs to be facilitators of better service provision by the public or for-profit private sector, rather than direct providers of services. Given the broad nature of these questions, we break this discussion down along the lines of chapter two, which focused on the key activities delivered by NGOs, and we then draw some general conclusions.

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<sup>117</sup> World Bank 2003

<sup>118</sup> Government of Bangladesh 2004

In micro-finance, the role of the Government in our view, ought to be in strengthening the regulation and supervision of the sector. We argue that in line with best practice, the Government or dominant funding agencies such as PKSF, should not attempt to set final borrower interest rates and ought to leave that decision to each individual NGO. Given the questionable sustainability of Government micro-finance programs and the clear comparative advantage of NGOs in micro-finance we argue that Government ought to move away from the direct provision of micro-credit. Once an appropriate regulatory framework is established the larger NGOs could convert into specialized micro-credit banks.

The analysis in chapters two and three point in a number of strategic directions for micro-credit NGOs:

- (i) Micro-credit programs ought to focus on targeting geographical areas, particularly in north-west Bangladesh, where access to credit is limited. Carefully designed subsidies may be required to generate the incentives to set up micro-credit branches in areas where operating costs are likely to be higher than the norm.
- (ii) The micro-credit industry ought to scale up successful experiments that provide micro-credit to the poorest. There will remain a group of extremely poor households who do not wish to borrow to sustain their livelihoods for whom non-credit interventions are more appropriate. However, there remain a significant share of households for whom adapting the current micro-credit model, and perhaps combining micro-credit with other services, will lead to welfare gains.
- (iii) NGOs that provide micro-credit ought to continue with their judicious entry into providing larger loans. Many NGOs have already ventured into this market, though with a few exceptions, the number of larger borrowers is still relatively small. While there is a temptation to upscale these programs rapidly from a public policy standpoint, given the potential growth-generating impact, we argue that the current cautious expansion strategy is the right one. Providing larger loans has its benefits but it also involves considerable risks, as there are a limited number of former micro-credit borrowers who want to ‘graduate’ into this market and new wealthier clients do not have a credit history with the lender and are less likely to be socially pressured into repaying.

Turning to the education sector, there is currently a very different mix of Government and NGO provision when compared to the micro-credit sector. In contrast to micro-credit, where the market is dominated by the NGO sector, students in NGO schools make up less than ten percent of primary enrolment (as chapter 2 shows, these are largely poor children). This figure has been by and large constant over the past decade. We show in chapter two that learning outcomes in NGO schools are superior to Government primary schools, and that the transition rate, of NGO students, to Government secondary schools are high. Based on these facts, we argue that in order to achieve Bangladesh’s Millennium Development Goals (MDG) in education, an expansion of NGO primary schools is warranted. The PRSP states that “*access is low for ethnic and linguistic minorities and people living in char-land, lowland, baor and coastal areas where there is a disproportionate concentration of the extremely poor*” (page 114). NGO schools could focus on these groups and in reaching the large numbers of poor students who do not enroll, or who drop-out of schools. In areas where both Government and NGO primary schools exist a voucher system could be piloted to provide consumer choice and



strengthen the short route to accountability between provider and client. This expansion in NGO schools could be done by transferring poorly performing Government primary schools to NGOs (for which there are precedents) or by financing the construction of new schools – we turn to financing and contracting issues later in the chapter. Another approach is for Government or community management of schools with NGOs acting as facilitators to ensure targeting and teaching quality – the recent Reaching Out of School Children (ROSC) project targets the enrolment of 500,000 poor children with money going to communities who can contract NGOs to help in running schools.

### **Box 5.1 The transition from NGO to community management**

While the prevalent NGO model is one of direct service provision, there are also notable examples of NGOs building the capacity of communities to manage their own resources.

The Rangpur Dinajpur Rural Service (RDRS), a prominent NGO operating in northwestern Bangladesh, has set up a unique federated group structure. At the lowest tier, Primary Groups comprised of around twenty poor individuals are set up and are provided a range of services directly by RDRS. Following an evaluation of the effectiveness and initiative levels, these Primary Groups may be allowed to transform into the second tier. The members can then join other Groups from their own or nearby villages to form a Union level Federation. RDRS has consistently promoted the emergence of these apex bodies or umbrella organizations, and has encouraged them to gradually take over management tasks from RDRS. The Union Federations (UF) represent the interest of primary groups, provide support services and act as vehicles for carrying forward development activities by and for the poor. At present there are two hundred and sixty active UFs, each run by an elected office holder and made up of elected representatives. The federations are required to have written constitutions, hold regular Committee and Annual General Meetings, plan and budget their activities and carry out annual audits.

Federations which have proven to be successful and sustainable can move up one step further and graduate as autonomous bodies no longer reliant on RDRS for resources and support. With encouragement from RDRS, one hundred federations have registered separately with the government's Social Welfare Department and are recognized as independent NGOs. This has given them legal recognition for their development work as well as the right to receive resources, cooperation and advice from the Social Welfare Department. This recognition also generates enthusiasm, interest and confidence among the members. Increased interaction with the government means there is a greater opportunity for the voices of the poor to be heard on a wide range of issues.

Community management of schools, and related educational facilities, is another way of strengthening the links between the provider and client. In the adult literacy and continuing education program, BRAC has established over 800 learning centers (libraries with IT facilities) on the premises of Government secondary schools or at the center of a union (the smallest administrative unit). In order to assess the communities interest in this facility BRAC requires a community contribution and the formation of a committee that will oversee the centers. Within two years, a learning center is transformed into a registered autonomous trust – as of early 2004, almost 80% of learning centers had been transferred from BRAC to the community by setting up these trusts.

At the same time, the Government's intention of creating space for NGOs and local communities in pre-primary schooling in the draft PRSP, calls for a strategic shift into these areas

for NGOs. Whether this shift comes at the expense of, or in addition to, a growth in NGO primary programs will depend on the NGOs preferences and financing options. Finally, with respect to post-primary education, NGOs could provide financial incentives for NGO trained primary graduates to remain in secondary schools and also leverage the experience gained in primary provision to disseminate best practices in community involvement, personnel management and teaching methods. The PRSP also clearly articulates the role of NGOs in raising literacy levels by providing and supporting continuing education programs. Experience from Nepal and other countries illustrate the merits of community management of schools and educational facilities. As we look ahead the role of NGOs in supporting school management committees and community involvement can pave the way for handing over educational assets to communities, thereby strengthening accountability mechanisms (see Box 5.1).

In the health sector the discussion in chapter two highlighted the very different ways that health services are delivered by Government, NGOs and private providers. The main strength of the NGO system is the vast numbers of village-based community health workers. These workers are important as the achievement of health outcomes is crucially dependent on individual households, particularly females within them, being conscious of a number of health and hygiene issues. Apart from awareness-raising, these workers are critical intermediaries between Government and private facility based services and poor clients. In assessing the role of NGOs in primary health care and nutrition services the draft PRSP states “*These initiatives require further scaling up and lessons from these experiences may be replicated in other areas of concern.*” (page 128). While reviewing the fact that the immunization program expanded from less than 1 percent of the population in 1981 to 60 percent in 2000, the draft PRSP points out that “*the immunization programme in Bangladesh is by and large a success story largely because of the collaborative effort with NGOs*” (pg 122).

Looking ahead, the appropriate role of Government, NGOs and the private sector in health ought to be shaped by efficiency and equity arguments as well as by the on-going and emerging needs in the sector. For instance, health indicators show that infant mortality, and more specifically neo-natal mortality which constitutes about two-thirds of infant deaths, remains a key problem. Critical interventions to address this problem include ensuring access to Emergency Obstetric Care, increasing skilled attendance at birth and improving awareness of post-natal care. As the PRSP suggests vouchers could be issued redeemable at both private and Government clinics to increase the use of modern facilities while NGOs could raise awareness of post-natal care, improve the skill levels of their community health workers so that they are better equipped to help during home deliveries, as well as act as facilitators by referring pregnant women to specialized care.

Malnutrition remains stubbornly high in Bangladesh with 45 percent of children under five stunted and 48 percent underweight (GOB 2004). Interventions that play to the strengths of community based health workers, such as promotion of breast feeding, growth monitoring and prevention, some nutritional supplementation and awareness of better nutritional practices ought to be scaled up by NGOs in partnership with Government along the lines of the National Nutrition Programme.

Another area where there is a clear public good and comparative advantage of scaling up NGO activity is in the area of non-communicable diseases. The large network of community health workers will be able to promote mass awareness of HIV/AIDS, malaria and tuberculosis detection and cure. The success of the Directly Observed Therapy programme, and the fact that currently NGOs are operating in over half of the country’s sub-districts registering cure rates that are higher

than those achieved by Government health complexes suggests that this type of program ought to be contracted out to NGOs to implement on an even wider scale.

In short there are existing health programmes (e.g. tuberculosis, nutrition, family planning and immunization) where there is an argument for even further scaling up of NGO activity as also argued by the PRSP. However, there are also emerging areas, such as in addressing the factors related to neo-natal mortality, where NGOs can at best play a facilitating role in ensuring access to specialized emergency obstetric care can only be provided by either the Government or the private sector.

Turning to advocacy and social programs, the discussion in chapter two illustrates the difficulty in measuring the impact, let alone the cost-effectiveness of these programs. Nonetheless whatever limited evidence there is suggests that awareness of issues such as corruption, violence against women, land rights and so on have improved due to the work of advocacy NGOs. Moreover on a more local level, advocacy for pro-poor access to services and efforts to promote the poor in decision-making bodies have also to an extent been successful. RDRS's model of encouraging communities to federate and directly network with local Government officials to access resources is another model of facilitating pro-poor advocacy (see Box 5.1). The PRSP endorses the active involvement of NGOs in improving governance, specifically in promoting social awareness against corruption, in promoting legal literacy among the poor and improving information flows. We argue that all these activities constitute an integral part of a well-functioning democracy and that the one area where NGOs ought to stay away from is involvement in partisan politics.

The discussion above provides illustrative areas where NGOs could consider focusing their activities over the medium term, either as direct providers or as facilitators of Government, private sector or community provision. As part of this process, there are also areas where NGOs could consider exiting, or limiting their activities, in order to maintain the focus on areas where their comparative advantage is greatest. These decisions will vary from one NGO to another and are internal management decisions that need to be made periodically.

We now turn to the capacity of NGOs to implement this strategy of a focused scaling-up by assessing NGO leadership, incentives, capacity building programs and organizational norms.

## 5.2 Is further NGO growth possible?

Size matters in the evaluation of NGO performance in Bangladesh as the scale of service delivery which has to date marked Bangladeshi NGOs is unprecedented. In the late 1980s, "*scale was the stick that NGOs were most often beaten with ... they could never be more than small exemplars of good practice and innovation*"<sup>119</sup>. By the 1990s, at least, this could not have fairly applied to NGOs in Bangladesh. This was a group of organizations whose impact lay significantly in the sheer numbers of poor people they reached. This section focuses on what has been learned about the organizational factors underlying success in the implementation of NGO programs, whether these provide a basis for further growth and how best any further scaling up ought to be financed.

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<sup>119</sup> Smillie and Hailey (2001)

5.2.1 *Management, incentives and systems*

**Concerns about domination of the sector by the founding generation of NGO leaders may have been overstated.** Leaders of the prominent NGOs are in most cases the original founders of the organization, and are convincing advocates of their organizational philosophy. Where the original founders are no longer the leaders, they are likely to have recently been replaced and/or retain a managerial or governing presence in the organization. Charismatic leadership was vital in the development of NGOs, and undoubtedly contributed to the expansionary phase in a number of ways. Particularly in the early days, leadership skills helped in inspiring staff to believe in the possibility of change, providing the organization with a sense of collective purpose, and the basis for motivation of individual staff members<sup>120</sup>. Second the ability of NGO leaders to attract the support of donors and other important audiences, such as Government officials<sup>121</sup>, has also been vital.

Concerns are frequently voiced about the over-domination of the big Bangladeshi NGOs by their founder-leaders<sup>122</sup>. A recent study raised fears that this domination meant that Bangladeshi NGOs were facing difficulties in the transition between leaders, and some NGOs have already floundered in the handover from founder to second-line leaders<sup>123</sup>. It is evident that many NGOs will face turbulent times as they are forced to rely more on the soundness of their formal management structures and processes than on a single individuals leadership. However, comparative analysis of management practices in South Asian NGOs shows that the link between strong, personality-driven modes of leadership in Bangladeshi NGOs and undesirably authoritarian forms of management are highly exaggerated<sup>124</sup>. The study acknowledge the existence of hierarchies in South Asian NGOs, but find that leaders in successful NGOs are characterized by their ability to listen to others below them in the management hierarchy, and to respond to what they hear; they are skilled at managing multi-functional teams and at delegating to decentralized operations. Patterns of NGO growth also suggest that qualities of charismatic leadership are less likely to be vital to future expansion given that the organizational capacity to replicate with an NGO branch manager - a 'franchise-holder' - may be more significant than the capacity to innovate.<sup>125</sup>

**NGO salaries and incentives cannot compete with the far greater attractions of public sector employment.** While it is a common perception that NGO staff enjoy higher salaries and better perks than Government staff, there is little evidence to support such a claim. The situation with respect to doctors is illustrative. A study of public sector medical professionals found that the average total income was found to be US\$460 per month, with more than half of respondents earning more than their Government salary in private earnings<sup>126</sup>. By contrast, the consolidated salary of a doctor in the NGO sector ranges from US\$180 - US\$300 including an allowance for not engaging in private practice. The story with teachers is similar. NGO primary school teachers receive on average \$20 per month compared to an average of \$45 (with an additional

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<sup>120</sup> See Siddiqi (2001)

<sup>121</sup> NGO leaders needed to be able to present convincing visions and new ideas about how to 'do' pro-poor development in ways that appealed to donors who may have sought radical champions of the poor, but who also needed to be able to rely on formal reporting procedures and accounting (see Sanyal 1991; Stiles 2002). In the early years it was also vital that the same individuals could transmit their vision and organizational goals to senior Government officials for approval or support (see Yunus with Jolis 1998: 168-70).

<sup>122</sup> See White 1999; Smillie and Hailey 2001

<sup>123</sup> Siddiqi 2001

<sup>124</sup> Smillie and Hailey (op.cit)

<sup>125</sup> See subsequent section on the franchising system

<sup>126</sup> Cited in World Bank 2003

75 percent in allowances and benefits) for equivalent teachers in the Government primary system. Cross-country analysis of public sector performance suggests that the wider the gap between the highest and lowest paid employee ('salary decompression ratio') the greater the incentives for better performance. The 10:1 ratio for public sector employees is similar to most NGOs – a recent survey of 62 NGOs<sup>127</sup> showed that around 60% had a compression ratio that varied between 8:1 to 10:1 and only 15% of NGOs had a ratio greater than 10:1. NGOs report high staff turnover levels, with staff leaving to enter public sector employment, which remains attractive in large part because of the prestige associated with it, the scope for additional earnings and security of employment.

**NGO management of health sector human resources presents some difficult challenges – as well as promising prospects.** A health facility survey conducted in 2004 (AHI 2004), found that while most NGO medical staff (doctors, nurses and midwives) were 'happy' with their jobs and found the workload acceptable, about half were dissatisfied with their salaries and benefit levels. More than two-thirds of NGO health center medical professionals also felt the potential for career development and promotion in their organization were poor. Not surprisingly, medical staff turnover rates in NGOs are high, mainly as a result of poor promotion prospects and the lure of public sector employment. At the same time, the success of individual campaigns - child immunization, tuberculosis, ORT, for example - that have involved NGO frontline community health workers suggests there may be lessons about how to structure incentives to improve performance among public sector medical professionals (see Box 5.2)

**There is little evidence to support the assumption that NGO staff performance is linked to their higher levels of altruism.** Research on women working in NGO rural branches and Government credit programs explicitly rejects the notion. Fieldworkers perceived their work as 'just a job', and that altruism and progressive motivations played a very small role in decisions to work in rural development.<sup>128</sup> First generation NGO workers are more likely to have been inspired by commitment to altruistic or progressive goals. Unemployment rates among secondary school and university graduates – the groups from whom the majority of NGO staff are drawn – are such that the motivations for entering NGO employment may very well reflect the lack of alternatives, instead of or in addition to, altruism.<sup>129</sup>

**Direct participation – or the perception of being directly involved - in organizational decision-making may help keep commitment high.** In Nijera Kori, for example, salary levels and benefits are known to be lower than in other NGOs. However, staff motivation is enhanced because they acquire a sense of 'belonging' to the organization and a stake in organizational goals through frequent face-to-face meetings and systematic information flows up and down the system, which ensure staff are informed of and contribute to the direction of programs.<sup>130</sup> NGO micro-finance staff are encouraged to feel their work is 'special' by NGO efforts to share messages about the success, household impact and wider importance of micro-finance.

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<sup>127</sup> This survey was conducted as background work for the Irish et al (2005) study

<sup>128</sup> Goetz 2001

<sup>129</sup> The Labor Force Survey (1999-2000) reported unemployment among those 'SSC/HSC' at 11.5 per cent; and with 'degree and above' at 7.8 per cent. Unemployment figures are generally believed to understate the situation (ibid).

<sup>130</sup> Kabeer 2003

**Close monitoring of employee performance and the ability to dismiss employees for poor performance offers the most convincing explanation of NGO employees' superior performance.** Regular and systematic monitoring appears to help explain why NGO school teachers are more likely to be present compared to better paid Government primary teachers. School supervisors visit regularly and they in turn are monitored by higher-level staff. Monitoring of employee performance is facilitated by systems which highlight poor performance. This is clearest in the micro-finance sector, with its simple and uniform accounting practices: poor performance will quickly show up through higher default rates. Campus-style living arrangements also lead to 'peer monitoring' amongst staff, with the immediate supervisor (the branch manager) also sharing the same facilities<sup>131</sup>. Finally the ability to dismiss employees relatively easily, without having to deal with powerful unions or cumbersome dismissal procedures, is an important incentive to perform well.

**Staff training and linking pay with knowledge retention help develop staff capacity.** NGO training programs vary significantly across organizations, both in terms of delivery, scope and emphasis. Certain NGOs have their own training centers while other organizations appear to place less emphasis on formal training and more on the 'training' of young middle class graduates characteristically employed by NGOs as they experience village life through early programs of immersion or on-the-job training.<sup>132</sup> Apex bodies such as PKSF also offer a range of training courses to various levels of NGO staff. A large part of the training provided by NGOs and apex bodies is training of trainers that helps disseminate knowledge to wider groups of staff as well as to clients. There are also courses that have been designed to build the capacity of senior and mid-level management – these are critical as most NGOs prefer to have experienced former field workers in management positions with relatively few lateral entrants recruited directly from management positions elsewhere.

**Box 5.2: Managing NGO health professionals: are there lessons for the public sector?**

One reason frequently cited to help explain why NGO health programs appear to be effective is that staff – mainly Community Health Workers - are based or recruited locally, unlike Government doctors who tend to live at a distance from their workplace. However, local community membership is not always incentive enough: one study found that in the Government system, Family Welfare Visitors recruited from the local community were reluctant to leave the health facility to perform their outreach duties in villages (Chaudhury and Hammer 2003). More convincing is the argument that NGO staff performance is influenced by stricter monitoring systems and the incentive structures these put in place. Both regular and random supervisory visits by higher level staff to hear views from the community on the quality of services provided ensure that problems like absenteeism are minimized. At the same time, monthly meetings with national or regional staff provide staff in the field with opportunities to air their concerns and make suggestions to improve management and performance.

NGO health programs have also pioneered financial incentives to improve staff performance. Success in generating knowledge about the use of ORT (oral rehydration therapy) for the treatment of diarrhoeal diseases is linked to a system in which BRAC Community Health Workers were compensated on the basis of how well women had retained and used knowledge about ORT in which they had trained them. Similarly, high success rates in tuberculosis completion and recovery rates through the DOTS program have been attributed to the system by which Community Health Workers receive half of a Tk 100 bond payment when patients complete their treatment.

<sup>131</sup> Jain and Moore (2003).

<sup>132</sup> See for example, the description of Grameen Bank's training methods in chapter 21, Yunus with Jolis (1999: 160).

Finally incentives to retain the knowledge learnt matters – as Box 5.2 illustrates NGO programs have used knowledge retained by clients, and by implication knowledge retained by staff in training programs, in performance related pay schemes in the health sector.

**The staff salary bill may grow with an ageing staff and more complex programs:** Experience from the Grameen Bank is illustrative. Grameen Bank has staff costs that are higher than most NGOs, partly because Grameen follows the government benefits system and partly because it has reached a state of maturity where expansion has slowed and a higher percentage of staff have been with the organization for a long time. Grameen realized that its staff costs would continue to increase unless more staff turnover could take place and it introduced a scheme with incentives for staff to leave after ten years. This can work for mainstream microfinance since it is not difficult or expensive to induct and train a significant number of new field workers every year, though experience becomes more valuable at the middle management levels and higher. But as NGOs mature and as they add products, management costs will inevitably rise and high staff turnover at the field level might not be so desirable.

**Clearly capacity across NGOs is far from uniform though small NGOs can be a source of innovation.** Most NGOs are small and have limited managerial and staff capacity to expand on a large scale. While small NGOs are likely to be able to re-focus their activities along the lines suggested above, only large and possibly some medium sized NGOs could go to scale with new services. Small NGOs have demonstrated their ability to pilot innovative approaches – for instance nineteen small NGOs, supported by PKSF, have developed products that address the needs of the poorest in recent years. The larger NGOs that can go to scale will need to make a concerted effort to absorb the lessons from these innovations, particularly in education where BRAC's Non-Formal Education model is dominant.

**Expansion of NGO activity was based on a 'franchising system': NGOs reproduced organizational structure and program design in thousands of small units across the country.** The period of rapid growth of micro-finance programs is closely correlated with the growth of the NGO sector as a whole. This was fueled largely by a 'franchising approach': new branches simply copied the procedures and norms of existing branches<sup>133</sup>. Franchising of branches from within organizations was possible because in the early years, at least, there was a strong operational focus on a narrow, standardized range of micro-finance products offered to all clients. It was quick and easy to recruit and train staff in a simple product at a time when branches were being opened at a rapid rate. This enabled an efficient - and easily replicable - program and the performance of individual branches could easily be monitored because the narrow range of similar products could be compared using disbursement and repayment rates.<sup>134</sup>

**The focused expansion recommended for the future will also use this franchising system though the products may be more complex.** In micro-finance, scaling up financial products for the poorest will require a greater period of learning for managers and staff in branches where these programs do not exist. Similarly in poorer, more remote areas where even the basic micro-credit product is in short supply, branch managers and staff may need to provide greater flexibility to the standard savings and loan terms in order to attract clients. In health, the basic 'franchising units' are the village based community health workers. Clearly investments in building

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<sup>133</sup> Zaman 2004

<sup>134</sup> Jain and Moore 2003

their capacity are essential in order to improve their effectiveness during childbirth and post-natal situations, create awareness of communicable diseases, administer tuberculosis detection and treatment as well as carry on their more routine, and yet vital, tasks of family planning, nutritional awareness and so forth. In education, the basic unit of the ‘franchise’ is the non-formal school and in both pre-primary and primary, these programs can be scaled up using existing procedures. However the pressures to adopt a uniform model while scaling up also need to balance the risk of stifling innovative learning methods developed by small NGOs. In short while the ‘franchising system’ remains relevant for the future, human resource management will need to address issues of capacity building of field staff and building a solid management layer that will can oversee this growth and the addition of more complex products.

### 5.3 Managing a larger and more focused NGO program

Chapter Four discussed the trends and issues related to donor, Government and self-financing of NGO programs. We find that overall levels of external assistance channeled directly or via Government to NGOs have risen over the past decade particularly with new sector wide programmes in education and health and the financing of micro-credit programmes through PKSF. As we look forward issues surrounding the increasing financing of NGO programs through the Government Budget will become more important.

**Greater financing of NGO social services through the Budget has its merits as well as some risks.** For most NGOs, education, health and other social programs remain largely dependent on external subsidies – be it from resources channeled through the Budget or direct aid from donors. Financing of NGOs through Government has increased over the past few years and in our view this is a trend that ought to be supported. Transferring resources to NGOs through the Budget improves the comprehensiveness of the public expenditure framework, strengthens coordination with Government spending and in principle leads to better policy outcomes.

There are two main risks associated with increasing dependence on Government financing. The first is that there could be a potential conflict with any advocacy work that challenges prevailing Government policy. In this situation one option for multi-faceted NGOs is to limit their advocacy activities to issues that are important for the poor and are not highly controversial e.g. awareness of marriage laws, claims to Government services. A second option is for NGOs to separate their advocacy and service delivery work into two different legal entities with different financing sources. A third option is to limit the dependence on Government financing to an extent that would not jeopardize the whole program should funding be suspended<sup>135</sup>.

The second risk with increasing Government financing is the emergence of ‘fly by night’ NGOs seeking to exploit weak Government contracting processes. It is clear that Government-NGO contracting has not escaped the governance problems associated with public procurement in general. It is clear that funding of NGOs through Government ought to increase only on the condition that best practice models of contracting are replicated widely. In short models which appear to work best are when contracting is done by autonomous bodies (e.g. PKSF) or by independent third party firms and not when it is carried out directly by a Government agency.

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<sup>135</sup> Action Aid has explicit policies to limit funding from institutions whose policies and programs they could campaign against.



**Interest income and commercial borrowing can be used to finance micro-credit activities.** The micro-finance industry has now matured to the point where many NGOs can sustain a large portion of their lending activities from self-generated funds and borrowing at market rates. PKSF has an important role to play in building the capacity of NGOs to manage their micro-finance portfolio, in promoting innovations within the industry and in facilitating links to commercial sources of funding – one way of doing so would be to gradually align PKSF’s own lending rates to commercial rates without any restriction on final on-lending rates from NGOs to borrowers. However the expansion of micro-credit in remote areas or for the extreme poor may well require strategic subsidies.

**A strategic compact between Government, NGOs, donors and clients is required.** Finally we return to the World Development Report (WDR 2004) conceptual framework discussed in chapter 1. We argue that in Bangladesh, there is a need for a strategic compact between Government, NGOs, donors and clients where each party needs to strengthen its current practices and demand more from each other in order to improve the quality of NGO interventions. The strategic compact could be structured as follows.

The **Government** needs to modernize the legal and regulatory framework for NGOs while recognizing NGOs as an ally in the development process. As part of this modernization the Government needs to rationalize the number of agencies that oversee NGOs and consider establishing an independent regulatory body. It needs to be more tolerant of critical views and recognize that NGOs that engage in pro-poor advocacy activities have an important role in all democratic environments.

The Government ought to withdraw from areas where the public good rationale for its intervention is missing or from areas (e.g. direct provision of micro-credit) where NGOs have a comparative advantage. At the same time there are areas where in the long run the Government may wish to be more actively involved. These could include (i) strengthening the capacity of local Government who then choose to contract NGOs to implement services (ii) improving public expenditure and procurement systems so that aid to NGOs channeled through the Budget is recorded properly and disbursed in a transparent manner (iii) help mainstream certain NGO activities such as non-formal primary education by providing formal recognition to these schools (iv) widely disseminate lessons from successful partnerships with NGOs and also lessons on what has not worked, both with respect to implementation issues and impact.

**Donors** for their part need to be clear about the reasons they are supporting NGOs. If the main reason is to develop a broad-based civil society then support to a myriad of NGOs that focus on various constituencies appears reasonable. If on the other hand donors wish to improve service delivery and have an impact on large numbers of people then perhaps support to a handful of large NGOs is logical. While financing social sector activities donors also need to develop a clear strategy for sustainability, as has occurred in micro-finance. This strategy ought to be developed in tandem with Government where in the medium run the Budget progressively absorbs the costs of financing many of these social sector programs. In areas such as advocacy, where the conflicts of interest with Government financing are too great, donors could work with NGOs to tap the market for greater private charitable contributions.

Secondly donors need to streamline and harmonize their financial reporting requirements as current practices often create unnecessary duplication of efforts. At the same time staff in donor

agencies who interact with NGOs need to upgrade their own financial management skills in order to interpret best practice reporting formats. Donors also need to set in place systems that allow the transfer of ‘institutional memory’ during frequent staff rotations.

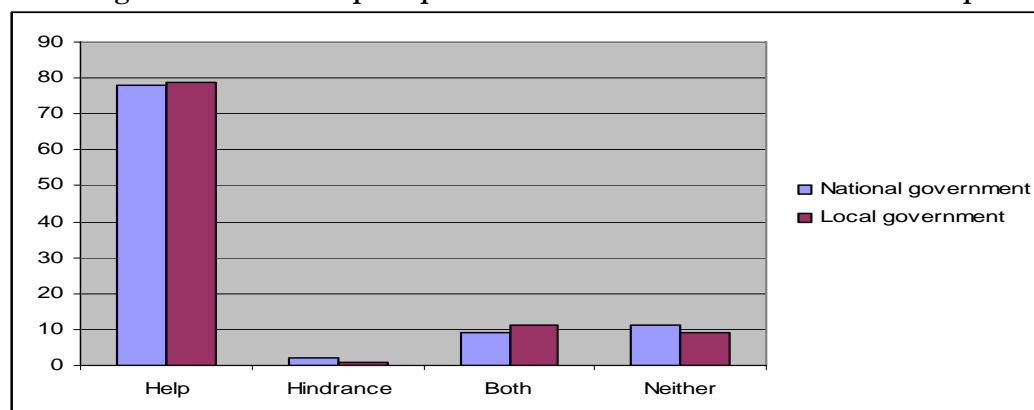
While there is a clear case for a focused expansion of NGO activity, and there are NGOs that have invested in building the capacity to do so, any discussion of greater financing requires a quid pro quo on the side of NGOs. The **NGO** part of the compact could involve the following areas (i) strengthening of financial management and corporate governance arrangements (ii) a systematic effort to provide public disclosure with respect to income sources, expenditure patterns and programme information along with a public information strategy to address misconceptions about NGOs (iii) greater efforts to align programmes with national strategies, coordinate with local and national Government officials and act as facilitators of Government, private sector and community service provision (iv) revisiting strategic directions periodically based on national development needs and internal capacity constraints and (v) developing a middle management layer to oversee more complex development programs.

**Clients** also have an important role in this proposed strategic compact. Clients can improve the quality of services provided to them by demanding better service and by monitoring service provision. Mechanisms that improve client power also need to be put in place in order for poor households to exercise these rights. For instance, vouchers can be introduced so that clients can choose between public, NGO and private providers. NGOs ought to remove any implicit or explicit barriers to clients moving from one NGO service provider to another. Monitoring mechanisms can also be set up through for instance user groups or management committees to provide systematic feedback to NGO officials and regulatory bodies.

In conclusion, this chapter argues that on the basis of the evidence presented in earlier parts of this report, there is a case for a focused scaling up of NGO activity, both as direct providers of services and facilitators of pro-poor interventions. This scaling up can build on investments in capacity and systems that have thus far been developed, though clearly this capacity is by no means uniform and will need further strengthening. We argue that the financing required for the focused scaling up can be obtained from a range of sources depending on the activity in question. We argue that the micro-finance sector has matured to point where the sector ought to move towards commercial sources of funding through linkages to the formal financial system. In the social sectors, there is a strong case for financing through the Government Budget, provided contracting procedures improve. The source of this financing could be external assistance or domestically raised revenue; while this mechanism involves some risks we argue that the benefits of greater coordination in public policy outweigh these costs. For advocacy type work, financing sources ought to be independent of Government, raised from private donations or external grants. Finally, in order to achieve these goals the report argues for a ‘strategic compact’ between Government, NGOs, donors and clients. The implicit compact would be where each actor strengthen various areas that are within their own mandate. The combined impact of these improvements will go a long way in achieving the common goal of improving services to the poor in Bangladesh and help achieve the Millennium Development Goals.

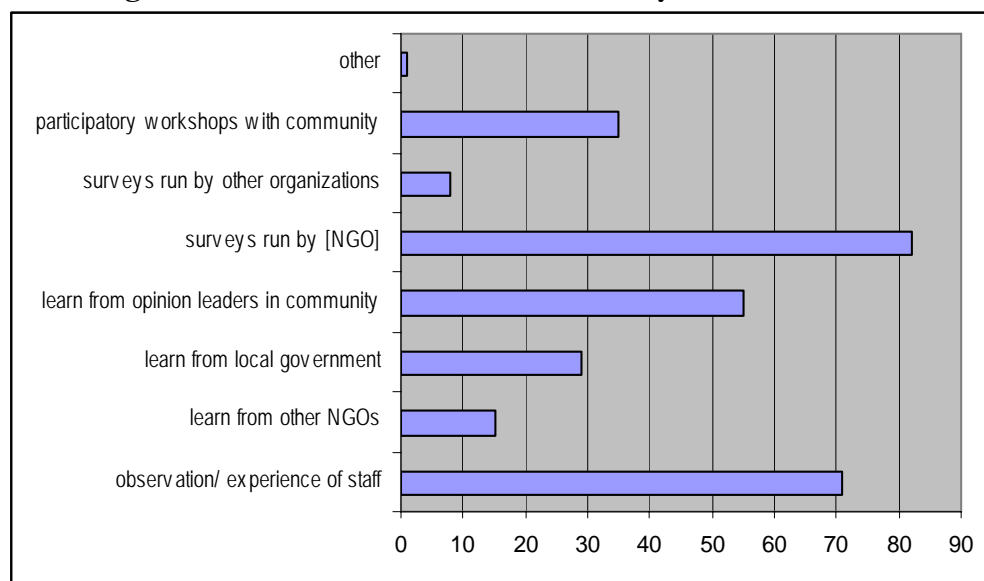
## Annexure

Annex Figure 1.1 NGO staff perception on relations with Government counterparts



Source: World Bank NGO survey (2003)

Annex Figure 2.1: How NGOs assess community needs



Source: Gauri and Galef 2004

Annex Table 2.1 Microfinance as Share of Total Private Sector Credit			
	FY02	FY03	FY04
<b>Outstanding (in billion Takas)</b>			
Banks	675.7	776.6	902.2
Non-banks	24.6	31.6	40.2
Microfinance institutions <sup>2</sup>	36.3	43.1	53
<b>Total</b>	<b>736.6</b>	<b>851.3</b>	<b>995.4</b>
<b>Microfinance as % of Private Sector Credit</b>	<b>4.9</b>	<b>5.1</b>	<b>5.3</b>

Source: Bangladesh Bank

(2/ Includes PKSF, Grameen Bank, BRAC, ASA, Proshika)

**Annex table 2.2: NGO education programs**

Education program	No. of NGOs involved	No. of centers	No. of learners			Total
			Female	Male	% Female	
Early child development	41	1,615	16,901	13,707	55%	30,608
Pre-primary education	119	9,450	163,970	110,281	60%	274,251
Primary education	559	44,372	943,120	522,776	64%	1,465,896
Adolescent education	200	4,340	77,071	33,205	70%	110,276
Adult education	251	5,701	107,922	46,738	70%	154,660
Post-literacy and continuing education	219	14,964	487,607	124,130	80%	611,737
Other education	14	1,500	33,268	4,674	88%	37,942
<b>Total</b>		<b>81,942</b>	<b>1,829,859</b>	<b>855,511</b>	<b>68%</b>	<b>2,685,370</b>

Figures are estimated by collating data from NGOs with significant education programs with information from CAMPE

Main sources: CAMPE Directory of NGOs with Education Programs (2004); BRAC Annual Report 2003

**Annex table 2.3 Donor financing of education programs of big NGOs (million taka)**

	1998-9	1999-2000*	2000-1	2001-2	2002-3	Total	US\$ million
VERC	0.7	1.8	1	1.1	0.8	5.5	0.1
FIVDB	37.5	33.5	27.2			98.3	1.6
BRAC	902.4	2,226.90	854.5	1,052.60	1,394.20	6,430.60	107.2
CAMPE	n.a.	5	7.7	35.8	47.9	96.3	1.6
PLAN	n.a.	n.a.	212.9	245.9	274	732.8	12.2
RDRS	9.8	6	4.9	n.a.	n.a.	20.6	0.3
PROSHIKA	468.3	627.4	n.a.	n.a.	n.a.	1,095.70	18.3
CMES	44.2	45.3	94.1	48.3	50.2	282.2	4.7
DAM	16.5	3.4	16.8	8.4	19.4	64.5	1.1
<b>Total</b>	<b>1,479.50</b>	<b>2,949.30</b>	<b>1,219.00</b>	<b>1,392.10</b>	<b>1,786.60</b>	<b>8,826.50</b>	<b>147.1</b>
In US\$ million	24.7	49.2	20.3	23.2	29.8	147.1	

\* The rise in funding in 1999-2000 was an anomaly as BRAC received a large infusion from its donors.

Source: NGOAB, 2004

<b>Annex Table 3.1. Estimated IDA disbursed through NGOs (1995-2004)</b>		
		<b>Mill US\$</b>
	<b>Energy (as of Dec 2004)</b>	
1	Rural Electrification & Renewable Energy Development	6.7
2	Renewable Energy Development	3.1
	<b>Energy Sub-total</b>	<b>9.8</b>
	<b>Microfinance</b>	
3	Poverty Alleviation (Microcredit I: disbursed as of Sep 2004)	131.0
4	Microfinance II (Disbursed as of Dec 2004)	149.5
5	Microfinance LIL (FSP)	1.6
	<b>Microfinance Sub-total</b>	<b>282.0</b>
	<b>Health</b>	
6	Bangladesh Integrated Nutrition Project (FY97 - FY02)	41.9
7	Health & Population Program	3.0
8	National Nutrition Program (disbursed as of Dec. 2004)	6.4
9	HIP/ AIDS Prevention (disbursed as of Dec. 2004)	2.4
	<b>Health Sub-total</b>	<b>53.7</b>
	<b>Water</b>	
10	Arsenic Mitigation Water Supply (disbursed as of Jan. 2005)	6.0
11	Water Supply Program Project	0.0
	<b>Water Sub-total</b>	<b>6.0</b>
	<b>Education</b>	
12	Female Secondary School Assistance Program (1993-2001)	5.6
13	Non-Formal Education Project (1996-2001)	7.4
14	Post-Literacy & Continuing Education (2001-2005)	13.3
	<b>Education Sub-total</b>	<b>26.3</b>
	<b>Rural Development</b>	
15	Silk Development Pilot Project (1997-2003)	10.2
16	Social Investment Program Project (2003-2005)	1.7
	<b>Rural Development Sub-total</b>	<b>11.9</b>
	<b>TOTAL IDA Disbursement through NGOs (1995-2004)</b>	<b>389.8</b>
	WB disbursement (1995-2004)	2,788.7
	IDA disbursement to NGOs as share of WB lending (%)	14.0

<b>Annex Table 3.2: Donor Financing Mechanisms</b>		
<b>Types of relationship</b>	<b>Direct from Donor</b>	<b>Funding from INGO or Large domestic NGO</b>
<b><i>Contractual</i></b>	For a specific short to medium term task	For a specific short to medium term task
<b><i>Project</i></b>	For a specific area of programming and often donors co-ordinate funding– e.g. non-formal education, water & sanitation, etc	Acting as a subcontractor to an INGO, or as part of a network (e.g. Grameen Trust, Proshika etc)
<b><i>Wholesale management (usually via a tender)</i></b>	Contractor manages (usually via a tender) a pool of money (facility) for a specific theme – smaller NGOs apply via the facility. Most are based in Bangladesh e.g. Manusher Jonno ASIRP (with GoB), & Katalyst – DFID; Health & Human Rights Funds - USAID); Canada Fund (CIDA); some HQ based (Civil Society Challenge Fund – DFID)	INGO manages a facility for donors to finance other small NGOs around an objective - e.g. Oxfam (disaster relief), Care (Income III); BRAC (microfinance), Samata (LAND network)
<b><i>Partnership Agreement</i></b>	Donors pool funds around agreed outcomes which encapsulate the entire NGO's operations (e.g. Ashroi, Proshika Phase VI, Njera Kori, Samata, Rupantar)	INGO funds a partnership with a domestic NGO across all areas of its operations (NOVIB & Proshika, Oxfam & BRAC)
<b><i>Institution Building</i></b>	Donors co-fund the entire organisation, which emerges as a different legal entity. This is usually part of the 'traditional exit' – e.g. PDBF (CIDA); Aranuk Foundation (USAID), Manusher Jonno Trust (DFID)	INGOS co-fund the entire organisation which emerges as a different legal entity – e.g. early funding of Grameen by Ford Foundation

Sources: Matsuert (2005), Sultan (2004)

<b>Annex Table 3.3: Micro-finance efficiency Indicators</b>				
	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>
Very Small NGOs	148	161	167	207
Borrowers per credit officer	570,000	573,000	633,000	811,000
Portfolio per credit officer – taka	7.6%	9.9%	9.9%	9.2%
Cost ratio*				
	190	200	209	207
Small NGOs	506,000	576,000	622,000	677,000
Borrowers per credit officer	10.5%	10.3%	9.9%	9.1%
Portfolio per credit officer				
Cost ratio	209	215	220	249
	686,000	733,000	740,000	898,000
Medium NGOs	8.8%	11.4%	10.1%	9.6%
Borrowers per credit officer				
Portfolio per credit officer	345	448	461	461
Cost ratio	1,310,000	1,700,000	1,970,000	2,110,000
	4.1%	3.4%	3.3%	3.1%
ASA				
Borrowers per credit officer	n.a.	298	364	n.a.
Portfolio per credit officer	n.a.	881,000	1,160,000	n.a.
Cost ratio	13.5%	12.6%	11.5%	n.a.
BRAC				
Borrowers per credit officer				
Portfolio per credit officer				
Cost Ratio				

\*This is the cost per 100 taka lent out and is calculated by dividing total expenses by total disbursements in a year.

Annex Table 3.4: Outreach and average loan size by NGO size				
	2001	2002	2003	2004
Very Small NGOs				
Annual Growth - clients	n.a.	37%	27%	25%
Average Loan Size - taka	6,580	6,256	6,435	7,742
Small NGOs				
Annual Growth - clients	n.a.	20%	18%	16%
Average Loan Size - taka	5,622	6,610	7,510	9,979
Medium NGOs				
Annual Growth - clients	n.a.	19%	21%	24%
Average Loan Size - taka	5,420	5,960	5,504	6,289
ASA				
Annual Growth - clients	25%	40%	8%	11%
Average Loan Size - taka	6,722	7,524	8,589	n.a.
BRAC				
Annual Growth - clients	n.a.	(5)%	15%	n.a.
Average Loan Size - taka	4,967	5,886	6,088	n.a.



Annex Table 3.5 An illustrative range of NGO businesses		
Business Sector	Businesses	Sponsor
Poultry hatchery	GKT Poultry hatchery	GKT
	BRAC Poultry hatchery	BRAC
Feed mill	BRAC poultry feed mill and marketing	BRAC
Seed production and processing	BRAC seed production and processing BRAC tissue culture (potato)	BRAC
	GKT seed processing GKT tissue culture (Potato)	GKT
Fish hatchery and fish production	BRAC fish hatchery	BRAC
	JC Fish farming	JC
	Grameen Mothsha Foundation	Grameen
	TMSS fish production	TMSS
Horticulture	BRAC horticulture and nursery and vegetable exports	BRAC
Dairy	BRAC Dairy products	BRAC
	TMSS dairy and livestock	TMSS
Handicrafts/garments/handloom	TMSS <i>Uthpaddan</i>	TMSS
	<i>Chakra</i> handicrafts	JC
	<b>Aarong</b>	BRAC
	Grameen <i>Shamogree</i>	Grameen
	Grameen <i>Uddog</i>	Grameen
Rural cell phone	Grameen Telecom	Grameen
Internet services	BRAC BD Mail	BRAC
	Citechco.net	Grameen (joint venture)
Private Banking	BRAC Bank	BRAC (joint venture)
Land development	BRAC Concord Land	BRAC (joint venture)
Housing financing	BRAC-Delta Housing Finance Corp.	BRAC (joint venture)
Private higher education	BRAC University	BRAC
Renewable energy (Solar photovoltaic systems)	Grameen Shakti	Grameen
	BRAC Solar Energy Program	BRAC
	TMSS Solar Energy Program	TMSS
Knitwear	Grameen Knitwear (in EPZ)	Grameen
Cell Phone	Grameen Phone	Grameen (joint venture with Telenor and other investors)

Source: Alamgir 2004: 10.

Annex Table 3.6: Average Profitability of four NGOs with commercial activities 2001-04

Sector	NGO	ROS (%)	ROA (%)
Agro-based products	Jagorani Chakra	9.00	n.a
	BRAC	4.17	1.51
	GKT	0.04	n.a
Handicrafts/dress making	Jagorani Chakra	21.9	n.a.
	BRAC	8.10	6.20
	TMSS	1.99	2.48
Printing	BRAC	7.12	11.29
Dairy products	BRAC	5.81	6.99
Non-agro-based businesses	BRAC	7.21	5.34
Property (House)	BRAC	24.84	0.94

### Annex 4.1: The Charities Commission for England and Wales

**Introduction:** The Charity Commission is established by law as the regulator and registrar for charities in England and Wales. The Commission is independent from the political process with powers given by the Charities Act 1993 (although it dates back to 1601), exercised by five Commissioners with different areas of expertise. Charity in Britain is defined on the basis of public benefit. Thus charities in Britain are voluntary bodies whose purpose is to benefit the community. Charity includes inter alia relief of poverty, sickness, education and community relations. The Commission has three objectives: to maintain an effective framework within which charities can operate, to work with charities to encourage good practice and to eradicate bad practice and abuse. A core function of the Commission is to determine whether an organization meets the requirements of a charity and to register it in the public Register of Charities. Charities may take a number of forms from trusts, associations to charitable companies. Although responsibility for running the charity rests with its trustees, ultimate accountability is to the High Court. The Commission's role is to act as a streamlined administrative alternative to the oversight of the High Court.

**Regulation and Accountability:** The Commission provides a framework of accountability for charities. This includes meeting requirements for registration, reporting and maintaining proper financial accounts. The Board of trustees are accountable to their members. Charities in a particular field particularly ones which have a substantial public policy interest, are often accountable to a particular specialist body. For example legal pro bono work needs to comply with the Bar requirements. The role of the Commission is to provide a framework for that accountability, co-operating with other forms of accountability. Charities are expected to be transparent because they serve the public interest. The Commission by law is not allowed to interfere in the manner in which trustees administer their charities in seeking to fulfill their purposes. The Commission gives advice, and guidance and they have the power to intervene in cases of mismanagement or misconduct.

**Registration and Monitoring:** The Commission maintains a register of charities. At registration stage the Commission is essentially concerned with determining that the body is charitable and that it is properly formed in accordance with the requirements of the law. The status of registered charity is valued, not only for the tax relief but for the credibility it brings. With registration comes accountability and monitoring responsibilities. Accountability varies according to the size of the charity, commencing with simple reporting of activities, and receipts and payment accounts for small charities, up to sophisticated reporting and accounting for large charities. The Commission sends a return to all charities but charities below the 1,000,000 pound a year threshold are only asked to provide basic details. The 5,000,000 plus charities above the 1,000,000 a year threshold must complete a more detailed return which includes financial accounts. The aim of the accountability framework is to support good management, to make it accountable to its members, beneficiaries and the public. The 1993 Act gives the Commission the power to scrutinize the activities and financial circumstances of the charity as the basis for regular supervision.

**Advice, Guidance, Investigation and Professional Support:** *The Commission's offices have Support Divisions which is responsible for the day to day relationship with charities. They are responsible inter alia for*

*providing charities with a legal service to amend or update their constitutions, giving advice and guidance on a range of legal, governance, management and financial issues.*

Each of the Commission's offices has an Investigation Division responsible for using the Commission's intervention powers where problems have arisen which cannot be dealt with on a co-operative basis by the Support Division. The Commissions' powers to intervene are where there is suspected misconduct or mismanagement or where the charity's resources need protecting. The powers include suspending trustees, freezing bank accounts, and appointing a receiver and manager to act in place of the trustees. Although the Commission does not have the power simply to de-register the charity, it has on occasion advised the dissolution of a charity, transferring its resources to a comparable charity. Beside the Registration, Support and Investigation Divisions, the Commission also has a responsibility for developing the interpretation of the law and to disseminate it to the charitable sector.

### **The Charities Bill 2004**

A new Charities Bill was published on 21 December 2004. This legislation is as a result of a strategic review of the charitable and voluntary sector. The Bill paves the way to greater empowerment of the charitable sector and a more defined role for the Charity Commission to both ensure compliance and engender accountability. The Bill essentially provides:

- greater freedom for charities to operate within a more flexible legal framework which will help them respond to changes in society
- supports trusteeship by providing simpler arrangements for obtaining relief from liability for honest mistakes, and paying trustees for providing services
- supports greater choice by establishing a new structure for charities – the Charitable Incorporated Organization which will simplify administration and reduce risk for charities which want to become companies
- provides new descriptions for charitable purposes
- makes benefit to the public a priority

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