

New Empirical Frontiers in Fighting Corruption and Improving Governance – selected issues

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<http://www.worldbank.org/wbi/governance>

Brief Background Comments and Empirics
Prepared for presentation at the OSCE Economic Forum 2001

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[Note: This brief paper should be reviewed in conjunction with the graphical powerpoint presentation to be given at the conference, available as a separate companion ppt file in the above referred website. Please contact us at governancewbi@worldbank.org if there are any problems accessing to the powerpoint presentation which contains empirics and graphics (and also for comments and feedback). Please also note that the views and errors are the author's responsibility, and the data is the outcome of various research efforts and also outside sources. The presentation of such data and views here do not necessarily reflect official views of the World Bank or its board of executive directors. A similar version to the comments contained below appear in the January/February Issue of the WorldPaper (<http://www.worldpaper.com>)]

What is the Issue?

Governance and corruption are notions heard often enough nowadays. Yet they are frequently left undefined, within writings long in exhortations and short in empirical evidence. What's lost is a clear strategy for combating corruption or improving governance. We have to admit upfront that we still lack many answers in this complex field, but recent empirical evidence and emerging lessons of success and failure offer some insights.

Defining the problem

What is corruption and what are its causes and consequences? What is governance, and when is it good? What strategies lower corruption and strengthen governance?

Corruption. Corruption is commonly defined as the abuse of public office for private gain. However, governance is a broader concept: we define it as the exercise of authority through formal and informal traditions and institutions for the common good.

Governance. Governance encompasses the process of selecting, monitoring, and replacing governments. It includes the capacity to formulate and implement sound policies, and it assumes a respect for citizens.

Unbundling Governance. From this framework, we have unbundled governance into *six* components, and developed worldwide measures for each. These are: i) ***voice and accountability***, which includes civil liberties and freedom of the press, ii) ***political stability***; iii) ***government effectiveness***, which includes the quality of policymaking and public service delivery, iv) ***quality of regulations***; v) ***rule of law***, which includes protection of property rights and an independent judiciary, and, vi) ***control of corruption***. It is noteworthy that controlling corruption emerges as just *one* of these closely intertwined elements of governance.

We have analyzed hundreds of cross-country governance indicators more than 160 countries and mapped the data to the six components of governance. (The detailed analysis and data is found at <http://www.worldbank.org/wbi/governance/datasets.htm> See also Chapter 6 in recently released World Bank book “The Quality of Growth”, as well as IMF’s Finance & Development, June 2000 issue).

Towards a meaningful empirical classification which accounts for margins of error. The analysis groups countries into three broad categories — ***red light*** for those with weak corruption control, ***green light*** for those with good governance, and ***yellow*** for those in between. From this analysis, as many as 40 countries emerge as having an acute governance crisis.

The Evidence. The evidence suggests that a capable state, with good and transparent government institutions is associated with higher income growth and national wealth, as well as measurable social progress. The experience of industrializing countries such as Botswana, Chile, Costa Rica, Estonia, Poland, and Slovenia supports this linkage, as does evidence over the past 20 years from economies like Singapore and Spain.

Moreover, the evidence challenges the argument that only rich countries can afford the luxury of good governance. Instead, it suggests strongly that better governance leads to better development outcomes. If Russia controlled corruption as well as the Czech Republic, or Indonesia as well as Korea, the improvements would about triple per capita incomes, while reducing infant mortality by a similar magnitude and improving literacy by about 20 percentage points in the long run. If Tajikistan were to acquire Chilean levels of government effectiveness, the resulting improvements would amount to twice those just catalogued.

Corruption and misgovernance are devastating for the poor, who routinely receive fewer social services, such as health and education, and have fewer resources to supply the bribes and payoffs that can be routinely demanded. Corrupt regimes often prefer defense contracts over rural health clinics and schools; a policy bias that worsens income distribution and diverts resources from the countryside to the cities. To gain access to public services, poor households in Ecuador must spend three times more in bribes as a share of their incomes than higher-income households.

Who benefits from bribery?

Recent evidence shows that a firm engaging in petty bribery (for example, for licenses or red tape) generally *doesn't* benefit. Nor does the business community or society more generally. Indeed, the costs of such corruption for overall business development are large. Grand corruption poses somewhat different problems. A survey of enterprises shows that in those economies in transition from communism where grand corruption is more prevalent, the growth and investment rate of enterprises are much smaller, and the security of property rights is seriously impaired. At the same time, for a number of countries in the former Soviet Union, the survey finds that firms that purchased parliamentary laws, presidential decrees, and influence in central banks *do* themselves benefit in the short run, though grand corruption imposes a particularly pernicious social cost on enterprise development. (For details on the research on State Capture and Grand Corruption, see: <http://www.worldbank.org/wbi/governance/pubs/seizestate.htm>)

Causes of Corruption

Empirical studies of the causes of corruption are fairly new, but evidence suggests that it is a symptom of deep institutional weaknesses.

Corruption rises with fewer and more fragile political rights, which include democratic elections, a legislature, and opposition parties, and weak civil liberties, which include rights to free and independent media and freedom of assembly and speech. Increasing evidence links the empowerment of civil society with effective strategies in addressing corruption. The enterprise survey evidence from transition economies suggests that the capture of the state policies and laws by corporate interests is associated with the absence of full civil liberties. The worldwide empirical evidence also suggests that the inclusion of women, whether measured in terms of parliamentary representation or social rights, goes along with a stronger civil society. Devolution, such as fiscal decentralization, may also help control corruption. In addition, evidence points to a significant correlation between corruption and a weak rule of law.

Corruption is higher in countries with a high degree of state ownership in the economy, excessive business regulation and taxes, arbitrary application of regulations, and trade restrictions. Monopolized economies tend to have more corruption.

Civil service professionalism, which includes training, hiring, and promotion systems, is also associated with less corruption. Contrary to conventional wisdom, the evidence is often ambiguous that low civil service pay causes corrupt behavior. Better public sector salaries on their own may not explain a significant reduction in corruption. For example, Ecuadorian public sector agencies that offer better pay to employees do not have a lower incidence of corruption.

The need for a Multifaceted Anticorruption Strategy which tackles the fundamentals, incentives and prevention.

Given what is known about the main determinants of good governance and corruption, what kinds of programs may have an impact? Improving governance requires a system of checks and balances in society that restrains arbitrary action and bureaucratic harassment

by politicians and bureaucrats, promotes voice and participation by the population, reduces incentives for the corporate elite to engage in “state capture,” and fosters the rule of law. Furthermore, research on state capture underscores the need for placing checks and balances on the “elite” corporate sector through promoting a competitive market economy and an active civil society. A meritocratic and service-oriented public administration is another salient feature of the strategy.

A chart synthesizing the strategy of key reforms for improving governance and combating corruption is included in the set of figures in the companion powerpoint slide presentation. However, how to combine and sequence these reforms to achieve the greatest impact on corruption is a particularly daunting challenge, as is the task of detailing and adapting a strategy to each country-specific reality. For instance, a country that has been subject to state capture by the corporate elite will require a different strategy than a country where the main source of misgovernance originates in the bureaucracy.

Details and Priorities in a multi-faceted strategy will vary from country to country.

Entry and Competition. Strategies to fight corruption must involve increasing entry and competition. In some transition and developing countries, a source of grand corruption is the concentration of economic power in monopolies that then wield political influence on the government for private benefits. The problem is particularly acute in countries rich in natural resources, where monopolies in oil, gas, and aluminum, for instance, create considerable economic and political power that leads to various forms of corruption: nonpayment of taxes, nontransparent offshore accounts, purchasing licenses and permits, and purchasing votes and decrees that restrict entry and competition. Demonopolization, deregulation, facilitation of entry and exit (through liquidation of assets and effective bankruptcy procedures), and promotion of competition are vital.

Political Leadership Accountability. To increase accountability of political leaders, some countries are pushing greater public disclosure and transparency. In several countries this has entailed the following:

- Public disclosure of votes in parliament
- Repeal of unconditional parliamentary immunity
- Public disclosure of sources and amounts of political party financing
- Public disclosure of incomes and assets of senior public officials and their key dependents
- Regulations against conflicts of interest for public officials
- Protection of personal and employment security for public officials who reveal abuse of public office by others (whistleblower statutes).

Professionalization of the civil service. A more professional civil service is another crucial element. Recruiting and promoting on merit, as opposed to political patronage or ideological affiliation, is positively associated with both government effectiveness and control of corruption. Reforms in this area have included creating independent, professional institutions with checks and balances (for example, a civil service recruitment commission) and introducing a comprehensive performance management

system with pay and promotion linked to performance, an approach that has yielded positive results in Malaysia and Thailand. In addition, allowances and non-cash benefits often need to be simplified, monetized, and made transparent. Wholesale salary increases are seldom a panacea.

The Budget, Public Expenditures and Procurement. Countries have found that it is crucial to establish basic systems of accountability in the allocation and use of public expenditures. To accomplish this there must be: a comprehensive budget and a consultative budget process, transparency in the use of public expenditures; competitive public procurement, and an independent external audit. The budget must first have comprehensive coverage of a government's activities. Many countries face problems of budgetary transparency, where major areas of budget expenditure do not pass through the treasury system, and there is substantial recourse to extra-budgetary funds. Several countries in transition, such as Hungary and Latvia, have made progress in addressing these problems with comprehensive treasury reform programs.

Transparent and competitive public procurement is key to clean government. Competitive bidding of major contracts, maximizing the scope of public oversight and scrutiny. The information technology revolution is proving to be a catalyst. The World Bank has also taken an active role in aggressively pursuing firms engaged in mis-procurement in projects; for instance, de-listed firms that have been barred from bidding in Bank-funded projects for having engaged in corrupt procurement are publicly available on the Bank's Web site. Finally, independent external audits, such as those established by several transition and emerging economies, such as the Czech Republic and Poland, have strengthened government spending enormously.

The Power of Empirics: In-depth Governance Diagnostic Surveys. Within countries, surveys can help empower civil society while providing valuable diagnostics on governance. New survey instruments can collect detailed information on behavior in even the most dysfunctional government agencies and on the delivery of specific services. Countries such as Albania, Bolivia, and Latvia have progressed from using diagnostics to taking concrete action. Bolivia is emphasizing civil service and procurement reforms. Latvia has given priority to tax and customs reforms.

In other countries, similar governance improvement efforts are taking place at the *municipal* level. For instance, in a number of Ukrainian cities specific actions to improve the effectiveness of local government in delivering public services are being carried out following diagnostic surveys. Pioneered in Bangalore, India, in the early 1990s, the now well-known citizen "report card" user surveys allow citizens to evaluate the quality of local government services. In Campo Elias, Venezuela, thanks to the leadership of the mayor, a courageous woman who believes in the power of governance data to inform and mobilize for action, the reported incidence of corruption has been halved.

The importance of Civil Liberties and Voice. Evidence from more than 1,500 World Bank-financed projects suggests that civil liberties and citizen participation are important factors for development outcomes. We found consistently large effects of civil liberties on project rates of return. Depending on the measure of civil liberties used, if a country

were to improve its civil liberties from the worst to the best, the economic rate of return of projects could increase by as much as 22.5 percentage points.

Governments and citizen groups can elicit voice through surveys and data collection in more systematic ways. Client surveys can cast light on citizens' experiences with government services and identify suggestions for performance improvement. Follow-up surveys can be used to ensure accountability and ensure that improvements are in the desired direction. Generating data and disseminating them widely are potent instruments to mobilize civil society and apply pressure on political structures. For example, simple comparative charts illustrating findings on corruption can help mobilize and give voice to previously silent and disparate citizenry groups.

Civil society oversight and participation over the decision-making and functioning of the public sector has been a crucial counterweight and instrument to combating corruption and improving governance. This involves making the state transparent to the public and empowering the citizenry to play an active role.

Conclusions

Governance is more than fighting corruption. Improving governance should be seen as a process integrating three vital components: (a) knowledge, with rigorous data and empirical analysis, including in-country diagnostics and dissemination, utilizing the latest information technology tools; (b) leadership in the political, civil society and international arena; and (c) collective action via systematic participatory and consensus-building approaches with key stakeholders in society (for which the technology revolution is also assisting). No two countries arrive at the same strategy, but to maximize the prospects of success, any country serious about improving governance must involve all key stakeholders, guarantee a flow of information to them, and lock in the commitment of the leadership.

Further background papers and data on these issues can be found at:
<http://www.worldbank.org/wbi/governance>

New Frontiers in Governance and Anti-Corruption
The 'Power of Data' and Collective Action

Daniel Kaufmann, The World Bank Institute

<http://www.worldbank.org/wbi/governance>

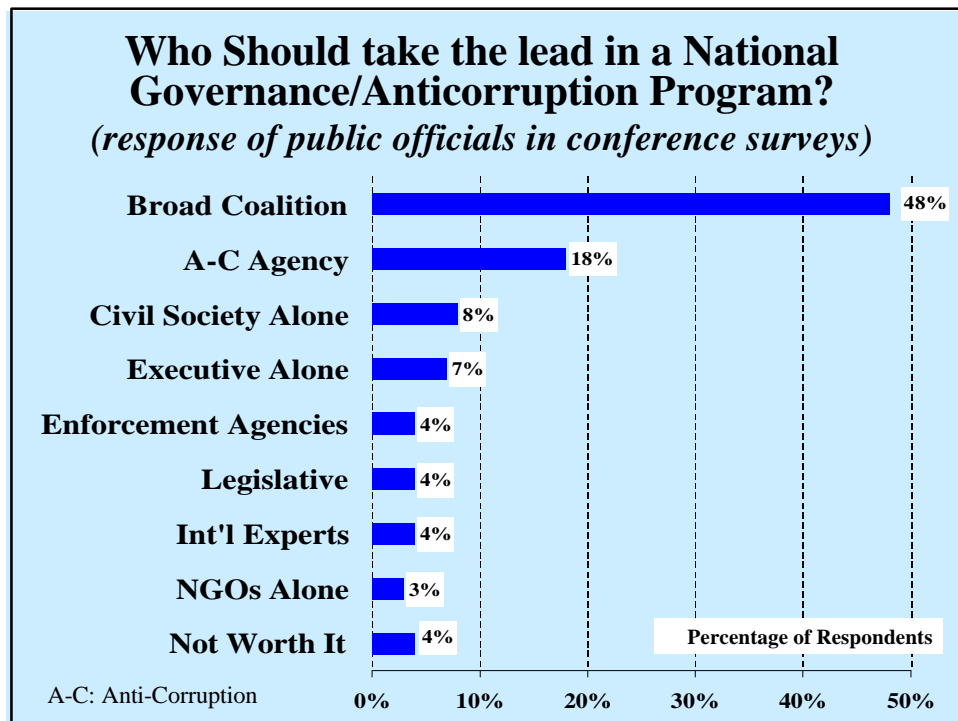
OSCE Economic Forum 2001

Brussels, January 30-31st

Governance: 9 Key Issues + 1 Challenge

- **Focus on Corruption equating poor governance**
- **Government 'drives' Anti-Corruption (A-C) program**
- **Paramount: A-C Agencies / Commissions / Ethics Off.**
- **Judiciary/Legal Enforcement Institutions are *the* key**
- **Strict Enforcement of Rules: civil service/bureaucracy**
- **High Pay in public service for combating corruption**
- **Focus: Bureaucratic bribery in developing countries**
- **Focus on problem within Governments**
- **Data on Governance/Corruption not that useful**

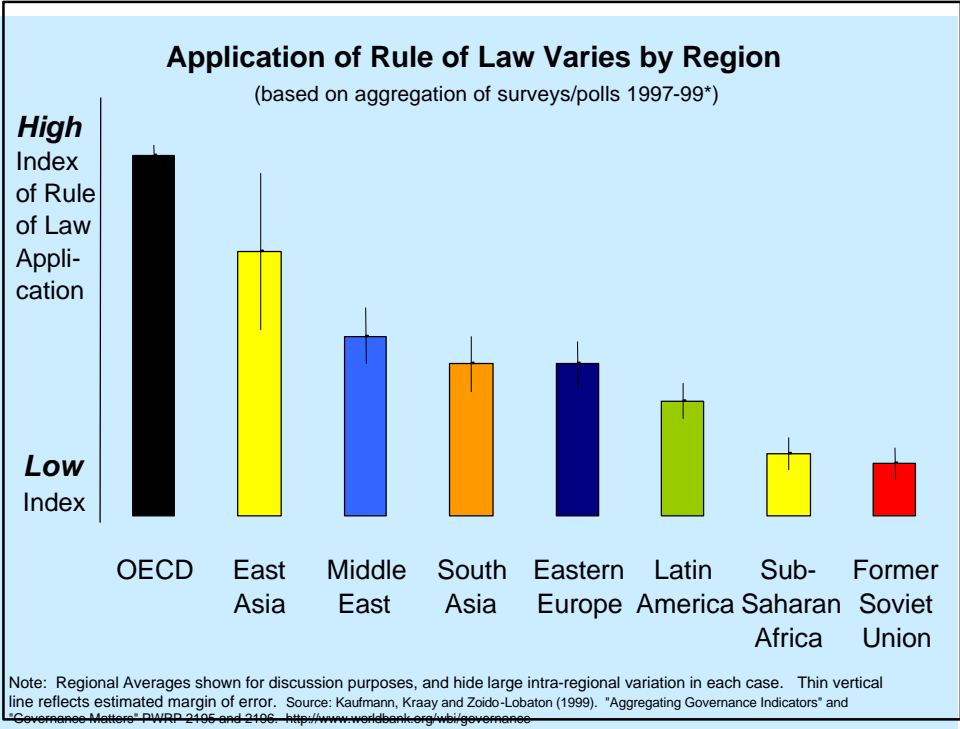
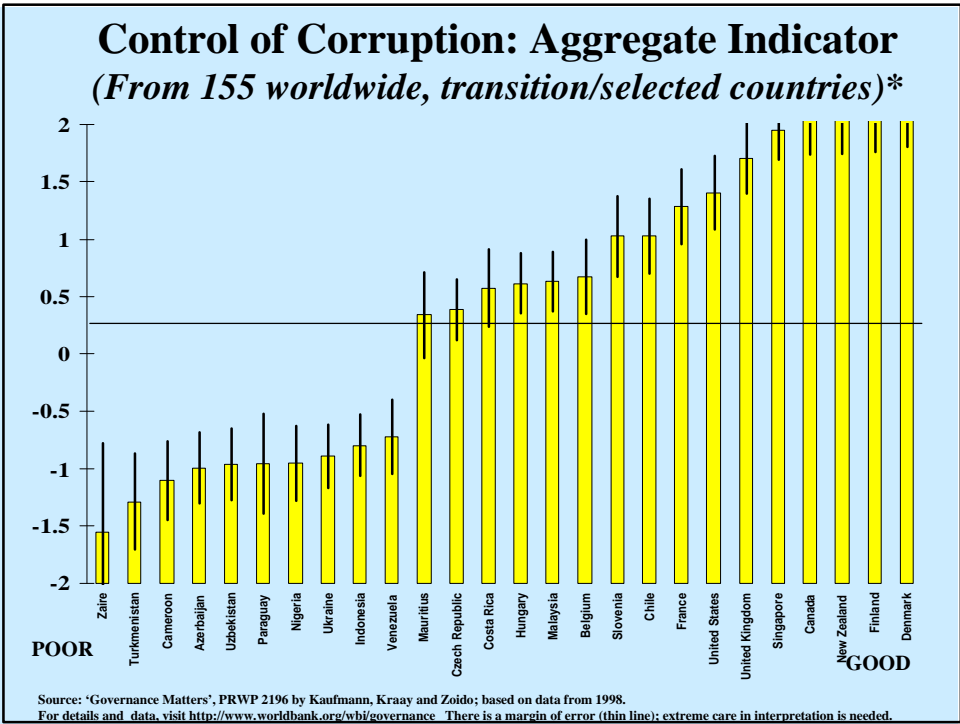
Challenge: The 9 Key Issues above contain myths



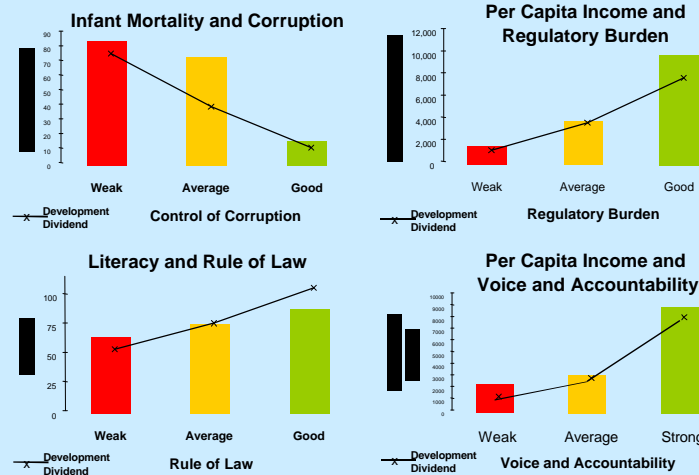
Broad Perspective -- and Unbundling: Assessing Overall Governance with Data *[based on over 300 variables; 160 countries]*

- **Control of Corruption (or Graft)**
- **Application of the Rule of Law**
- **Quality of Regulatory Framework**
- **Government Effectiveness**
- **Voice, Civil Liberties and Accountability**
- **Political Stability & lack of Violence/Crime**

Full definition on governance, and access and details on data: <http://www.worldbank.org/wbi/governance>

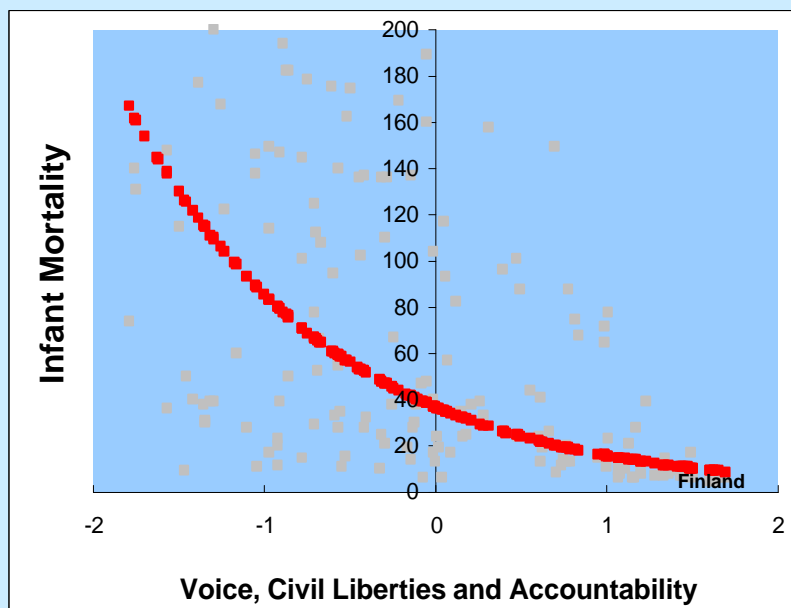


The 'Dividend' of Good Governance



Note: The bars depict the simple correlation between good governance and development outcomes. The line depicts the predicted value when taking into account the causality effects ("Development Dividend") from improved governance to better development outcomes. For data and methodological details visit <http://www.worldbank.org/wbi/governance>.

Voice, Accountability and Civil Liberties Matter for Development



Source: KIZ 1999

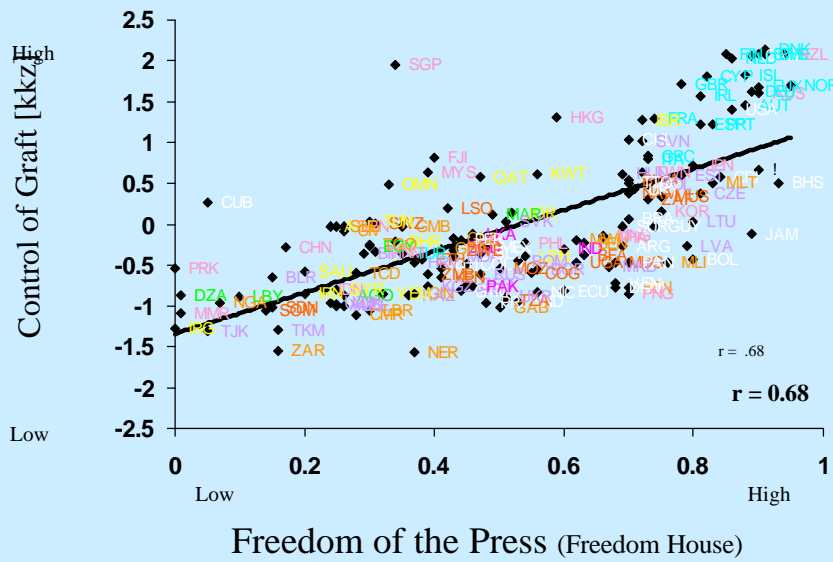
Corruption is associated with absence of Civil Liberties



Based on averages of data from 160 countries.

Civil Liberties

Control of Graft and Freedom of the Press

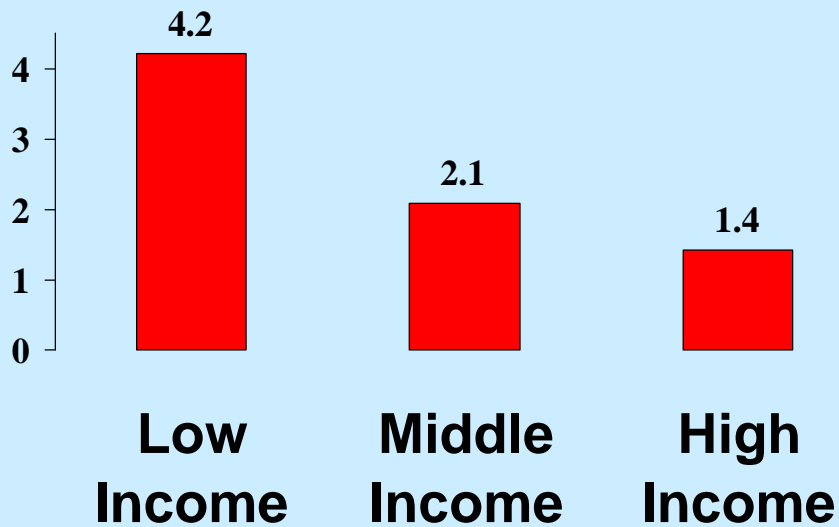


Salient Features of New Governance Diagnostic Tools

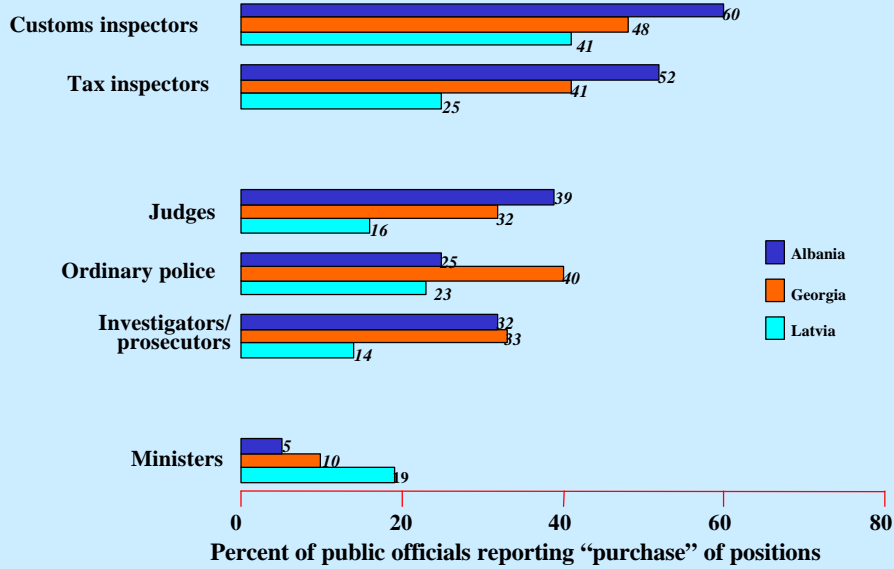
- *Multi-pronged surveys of: households, firms and public officials [‘triangulation’]*
- *Experiential questions (vs. ‘opinions’/generic)*
- *Specially designed and tested closed questions*
- *Conceptual framework: Incentive Structure behind Governance; focus on development*
- *Rigorous technical requirements in implementation*
- *Local Institution Implements, with WB Collaboration*
- *Recognizing Multidimensionality of Governance*
- *Focus on Service Delivery: Input for Action and Change*

Lower Income Households ‘Pay’ Disproportionally

Bribe/Total Income ratio % (A Latin American Country)

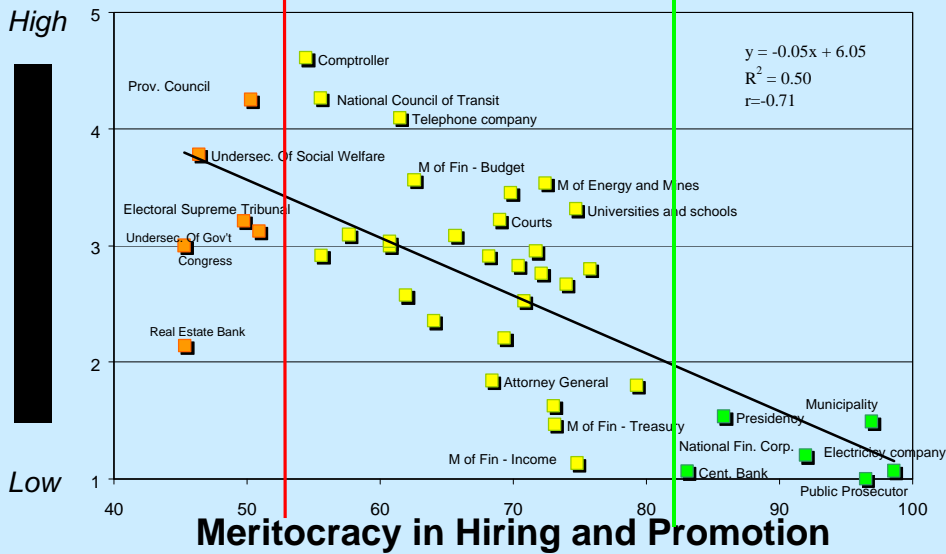


Which Public Sector Jobs Are “Sold”?

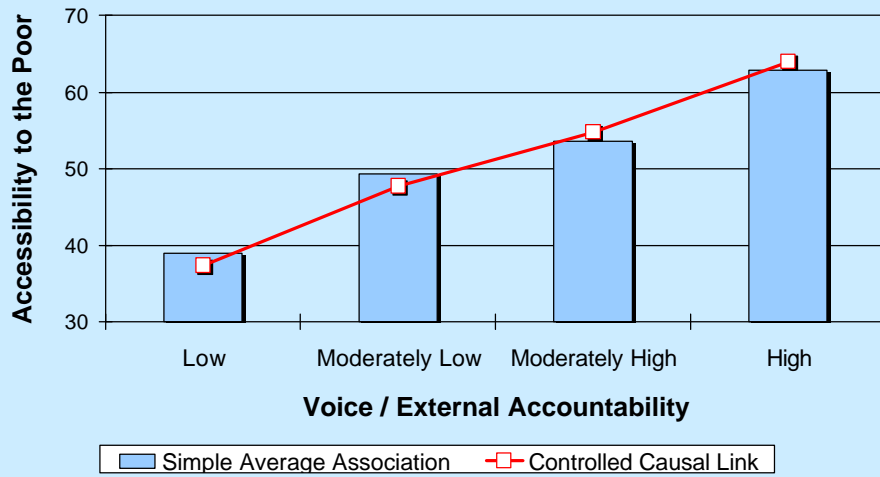


Source: Diagnostics 1998

Public Officials Survey: Meritocracy in the Public Service Can Help Reduce Corruption

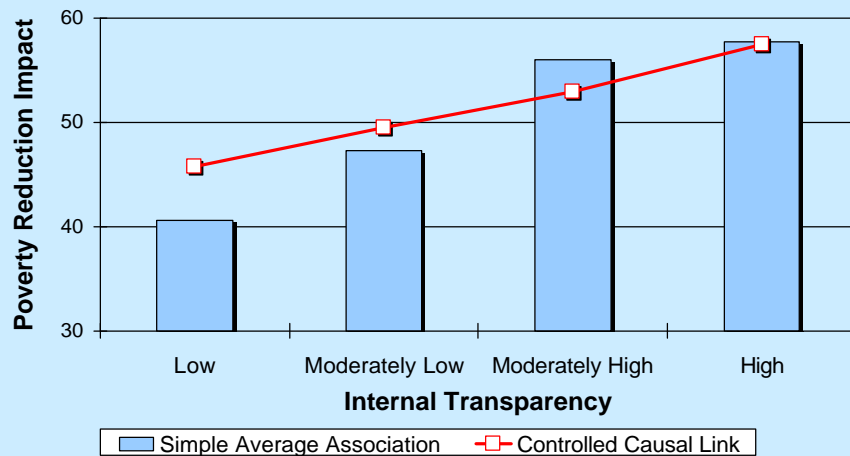


Citizen Voice Improves Accessibility of Public Services to the Poor in Bolivia



Based on Bolivia Public Officials Survey. The sample of institutions includes 44 national, departmental, and municipal agencies which are a priori anticipated to be accessible to the poor

Transparency within Government Agencies Increases Their Poverty Reduction Impact in Bolivia



Based on Bolivia Public Officials Survey. The sample of institutions includes 50 national, departmental, and municipal agencies which are a priori anticipated to have a major impact on poverty reduction.

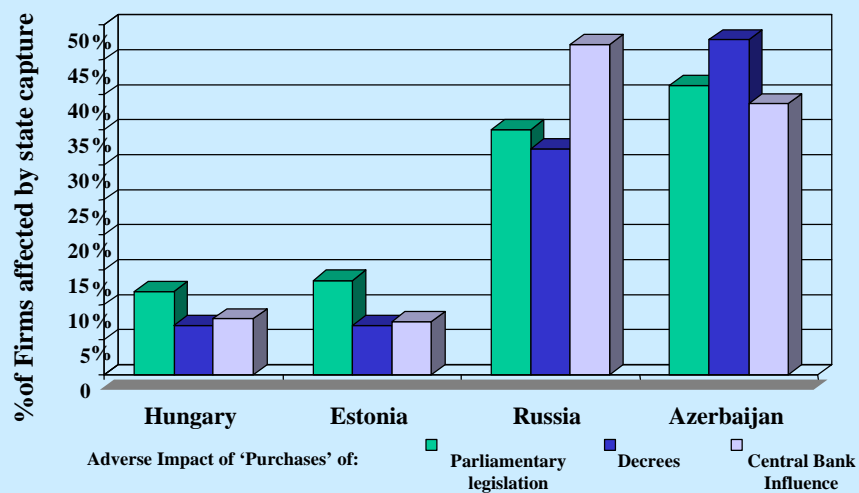
Extent of State Capture in Transition

Country	Parliamentary legislation (% of firms)	Presidential decrees (% of firms)	Central Bank (% of firms)	Criminal Courts (% of firms)	Party finance (% of firms)	Capture index (% of firms)	Capture Classification
Albania	12	7	8	22	25	16	Low
Armenia	10	7	14	5	1	7	Low
Azerbaijan	41	48	39	44	35	41	High
Belarus	9	5	25	0	4	8	Low
Bulgaria	28	26	28	28	42	28	High
Croatia	18	24	30	29	30	27	High
Czech Rep	18	11	12	9	6	11	Low
Estonia	14	7	8	8	17	10	Low
Georgia	29	24	32	18	21	24	High
Hungary	12	7	8	5	4	7	Low
Kazakhstan	13	10	19	14	6	12	Low
Kyrgyzstan	18	16	59	26	27	29	High
Latvia	40	49	8	21	35	30	High
Lithuania	15	7	9	11	13	11	Low
Moldova	43	30	40	33	42	37	High
Poland	13	10	6	12	10	12	Low
Romania	22	20	26	14	27	21	High
Russia	35	32	47	24	24	32	High
Slovakia	20	12	37	29	20	24	High
Slovenia	8	5	4	6	11	7	Low
Ukraine	44	37	37	21	29	32	High
Uzbekistan	5	4	8	5	4	6	Low
Overall	24	21	25	18	20	22	

State Capture Prevails in some countries

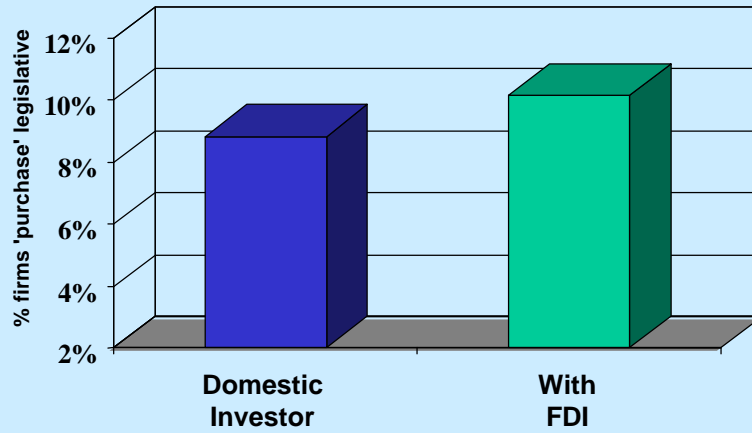
The 'Capture Economy' vs. the Market Economy

Source: Hellman, Jones and Kaufmann 2000 (BEEPS in Transition)



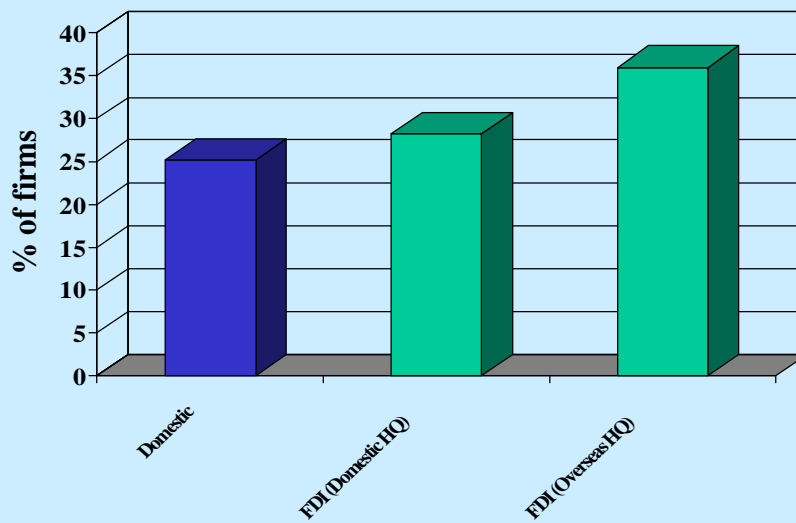
• **Transnational Corporate Responsibility Matters as Well:**

% of firms that 'Purchase' Legislation and Decrees in Transition Economies

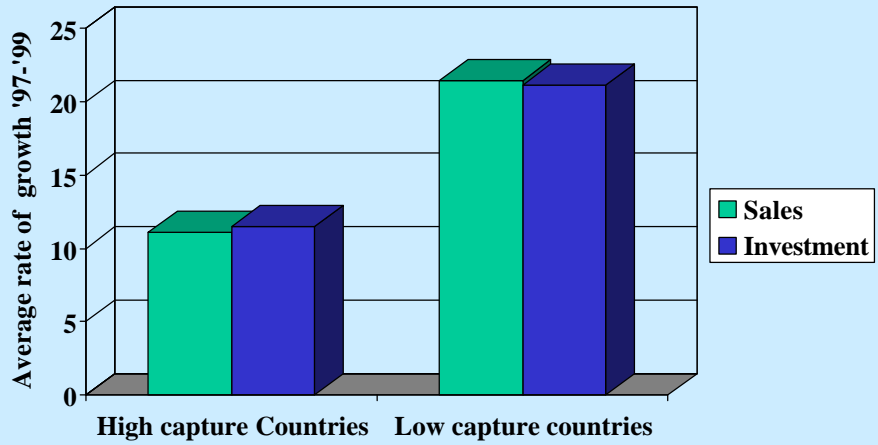


Note: For transition economies, average of 20 countries.
Source: Hellman, Jones and Kaufmann, 2000 (www.worldbank.org/wbi/governance)

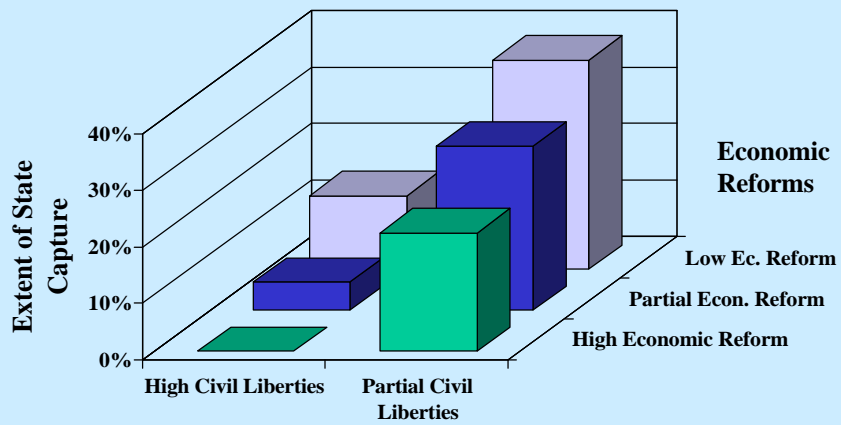
**% Firms that pay public procurement kickbacks
(of those that trade with the state)**



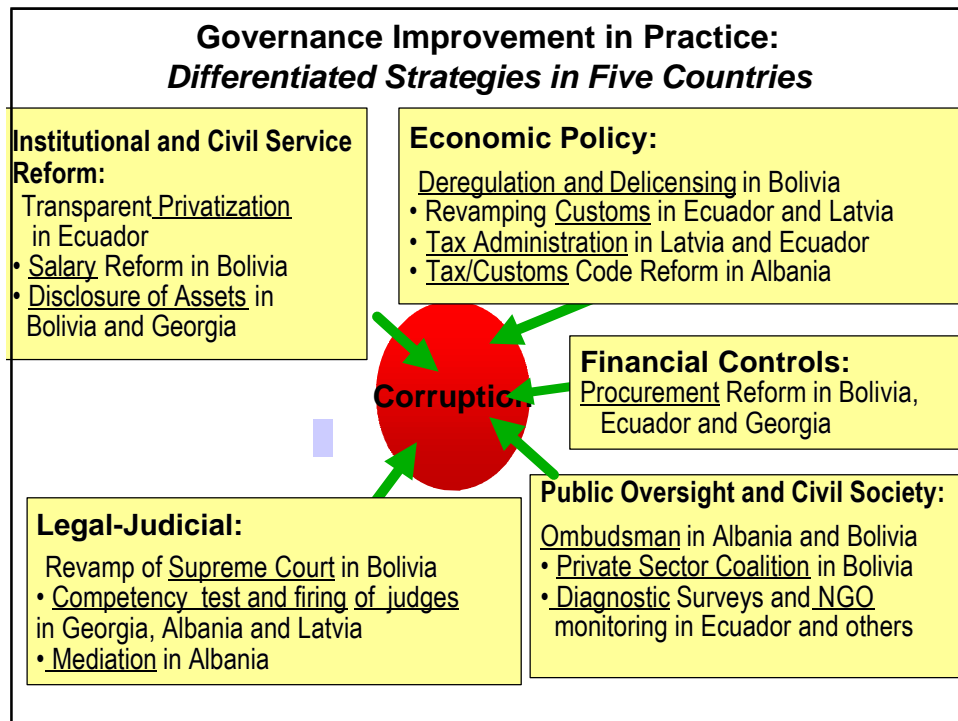
**Enormous Social/Economic costs of state capture:
 Much lower growth in sales and investment in economy
 (and also weaker property rights protection)**



**State Capture exists where partial Civil Liberties
 and slow Economic Reforms**



Degree of Civil Liberties in Transition Economies



Summing Up...

- **Broadening Framework: Governance for Growth**
- **Addressing State Capture and Grand Corruption**
- **Political vs. Economic Independence of key agencies**
- **Voice & Civil Society: Participation/Collective Action**
- **Role of Competitive Private Sector/Business Associations**
- **Addressing Fundamentals/Systemic Factors [vs. Symptoms]: imperative of Institutional Reform**
- **New empirical diagnostic tools & dissemination:**

The Power of Info.data

<http://www.worldbank.org/wbi/governance>

Broader Framework in Quality of Growth: Summing Up

- Growth is paramount for poverty alleviation and welfare improvement...
- ...But not if short term, K-int. and volatile growth
- And there are also other important welfare components: Civil Liberties, Human K, etc.
- Governance and Voice components are also important inputs for quality growth
- Rich countries can help quality growth process in emerging economies: governance and aid
- We are still learning: power of data

Visit: <http://www.worldbank.org/wbi/governance>

National Governance: Challenges in Integrating Anti-Corruption Into Institutional Change

A simple Formula synthesizing Governance/Anticorruption:

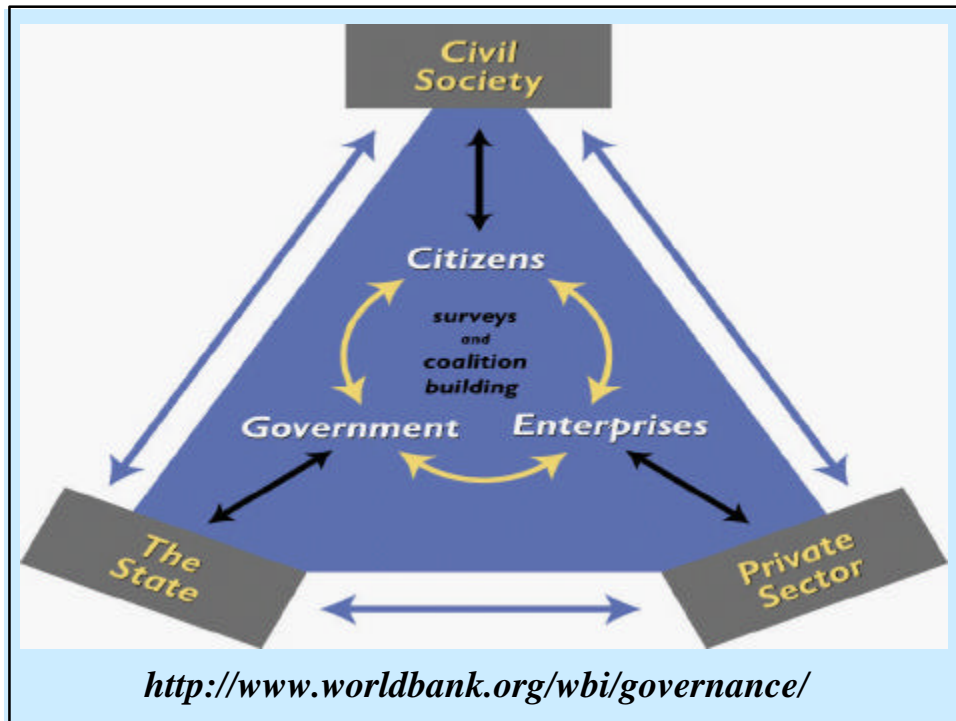
$$***IG and AC = KI + LE + CA***$$

Improving Governance and Anti-Corruption =

= Knowledge/Info.Data + ...

...+ Leadership (incl. Political) + ...

... + Collective Action (change)



Data Presented for Analysis and informing Policy Advice, not for Precise Rankings

The data contained in this presentation originates from various enterprise surveys (as well as outside expert rating agencies) and are subject to a margin of error. The purpose is therefore not to present precise comparative rankings across countries, but instead to illustrate characteristics of governmental and corporate performance in order to assist in drawing implications for action. No ranking of countries is intended in presenting results from these external sources by either the presenter of this work, the World Bank or its Board of Directors.

Further details and data, visit: <http://www.worldbank.org/wbi/governance>