

STRENGTHENING GOVERNANCE TO COMBAT CORRUPTION:

Presentation by Sue Ingram, Principal Governance Adviser, AusAID at the International Alert Series Forum on *The Business of Aid – creating partnerships, combating corruption* 19 June 2007

My presentation today has a simple message: corruption is a consequence of poor governance. And, as a corollary, if we are to combat corruption, we need to strengthen governance.

Corruption comes at a huge economic and social cost – a cost felt most acutely by the world's poor. The World Bank estimates that each year around \$US1trillion is paid in bribes worldwideⁱ. This is equivalent to ten times the total amount of development assistance provided each year. And even this huge amount - \$US1trillion – could be an underestimate as it does not capture some of the more elusive transactions, such as budget leakages and asset theft within the public sector.

Corruption sharpens income inequalityⁱⁱ, and impacts disproportionately on the poor. In many countries corruption represents a regressive tax on household incomes. Compared with higher income groups, lower income families pay a much larger share of their incomes in bribes to access public services, and their overall access is reducedⁱⁱⁱ. In concrete terms, it means a poor family is asked by a health worker to pay for medicines that are meant to be provided free of charge. Or it means that a parent is asked to pay a fee to a teacher to enrol a child in what should be free education. Or it means that an aid worker is asked to pay a toll to use a road to reach a poor village.

Corrupt transactions often siphon off funds that would otherwise find their way into public revenues and hence, hopefully, into services for citizens. For example, when a foreign company pays a bribe to a public official to provide a tax exemption, that is revenue foregone to the national budget. The official has profited through the cash payment. The company has profited through a massive tax saving. But the country – the citizens – are that much poorer. And it is their assets and their resources – often non-replaceable ones – that are being sold off for a song.

Corrupt transactions also undermine the essential infrastructure for economic and social development and, at times, put lives at risk: the bridge that washes away in the first wet season because the supervising engineer was paid off to ignore the use of sub-standard materials; the airport runway that cracks within weeks of being laid; the ferry that sinks because an official was bribed to register it when it was unseaworthy.

How then to tackle corruption? An important part of the answer is by improving governance. Let me quote from a recent DfID report on *Governance, Development and Democratic Politics*

Corruption is best viewed as an outcome of weak governance because it is more likely to occur when state capability, accountability and responsiveness are weak at the local and national level. While the symptoms of corruption must be tackled, so must the underlying causes. An exclusive focus on tackling the symptoms of corruption – through high-profile investigations, for example – has caused some countries to emphasise simplistic (and largely failed) anti-corruption initiatives while neglecting the need to strengthen national governance systems.^{iv}

Governance really is the key: to tackling corruption and improving economic development. Better governance delivers a very large *development dividend*¹. World Bank research suggests that countries which tackle corruption and improve the rule of law can increase their national incomes by as much as fourfold. Among countries from various regions, those that ranked highly for their control of corruption also had strong average annual growth in their gross domestic product. Those countries with the poorest records on controlling corruption on the other hand experienced negative growth.

Why is it, then, that poor governance creates the conditions for corruption to flourish? Fundamentally, the business of government is about taking decisions – decisions about how to exercise the powers held by government. Some of these decisions involve the direct expenditure of public funds, but many more involve matters which directly affect the interests of particular citizens. These decisions include, for example, whether to grant or to refuse a permit or licence, whether to authorise or to refuse a benefit, whether to award a contract, and whether to attach conditions to a decision.

All these decisions involve the exercise of Ministerial or administrative discretion. Where governance is good, there will be a sound framework of legislation, procedure and systems to guide the exercise of the decision-maker's discretion. This ensures that decision-making is predictable and transparent. Where governance is poor, on the other hand, and there is no clear and observed framework for the exercise of discretion, decision-making is arbitrary and the reasons for the decision are hidden.

Let me illustrate this with a simple example: the grant of a driver's licence. Where governance is good, there will be established and publicly known criteria for the grant of a licence. For example, the applicant must be at least 18 years of age, have good eyesight, and demonstrate ability to drive. These criteria will be contained in legislation, and there will be written procedures to guide decision-makers. Officials granting licences will have been trained in the application of the procedures, there will be some sort of appeal mechanism for people who believe they have been improperly refused a licence and some sort of audit mechanism to establish whether licences have been improperly granted. Where governance is weak these mechanisms will not be in place, making it very easy for officials to grant licences in return for a bribe, whether the applicant is qualified to drive or not.

Let me shift now to a real example, to show how governance, corruption and economic development fit together. The example I am using describes the collection of public revenue from logging, and it comes from Solomon Islands – not because this country is necessarily worse than many others, but because I have just returned from two years living there, working in partnership with the government to strengthen the machinery of government.

Logging is a major source of revenue for the Solomon Islands Government, with revenue from export duties currently accounting for 13-15 percent of total national budget revenue. It is also an area that – in Solomon Islands as elsewhere – is very vulnerable to corrupt transactions. Indeed, the quantum shift in the scale of corruption in Solomon Islands is attributed to the opening up of the islands to foreign logging interests in the mid 80s. An audit of the Department of Forestry, tabled in Parliament in 2006, estimated that \$SB30m in revenue was lost to the budget through the grant of export duty exemptions in 2004, equivalent to six percent of the total national budget at that time. A further \$SB7m was lost through uncollected royalty payments, the improper payment of royalties and unlawful ex

gratia payments. A lot of money was moving around, but it was not finding its way into consolidated revenue.

This could happen because the mechanisms for ensuring the oversight of executive and administrative action had broken down almost completely in the decades since independence. To quote from a 2004 Report by Transparency International examining the National Integrity Systems of the Solomon Islands

In assessing the issue of corruption in the Solomons, it is clear that the national integrity system has been comprehensively ineffective in maintaining standards of public propriety and accountability.^{vi}

By the time of the Transparency report, the Office of the Auditor-General had almost ceased to function. Its 29 staff at independence in 1978 had been reduced to two, and only a handful of audit reports had been completed or considered by Parliament since the mid 80s. As the Auditor-General himself wrote in October 2005:

The absence of an effective audit function with government over such a protracted period of time has led to an unchecked and ultimately disastrous breakdown in public accountability – an environment that (was) typified by poor financial management practices and weak controls, which resulted in significant losses in revenue and conducive to fraud and corruption.^{vii}

This situation has been turned around in the last few years, with a major injection of support to the Office of the Auditor-General and other elements of the national integrity system from the Regional Assistance Mission to Solomon Islands and a boost in running costs from the Solomon Islands Government. The staffing level of the Office of the Auditor-General is back up to 29, ten special audits into revenue sensitive areas of government have been completed and tabled in Parliament and the backlog in the completion and audit of national accounts is reducing. The local media has given extensive coverage to the findings of the audit reports. The Public Accounts Committee of Parliament has been revitalised and is examining all audit reports and calling officials to testify. Recommendations in the audit reports are being followed up by departments. The law and justice system has been significantly strengthened and is investigating and prosecuting corrupt conduct in office: 46 people, including former Parliamentarians and Ministers, have been charged with corruption related offences. And – a great example of the value of transparency – the special audit reports are publicly available on the Auditor-General's website. All these steps help to reduce the opportunities for officials to act corruptly and get away with it.

Weak systems facilitate corruption, and the corrupt official, acting alone, can take advantage of them. But corruption is more often transactional; it involves two parties: the official, and the beneficiary of the official's action. Individuals can play along with corruption because they stand to gain from it. But they also play along with it when they lack the capacity or the will to stand up to it.

Business can be a perpetrator of corruption, but it is also the victim, and business can be an important ally in efforts to combat corruption. The Extractive Industries Transparency Initiative, which was kicked off in 2002, is an important example of a partnership between government and business to fight corruption. The initiative promotes better governance of resource revenues in resource-rich developing countries. It encourages governments, companies, donors and NGOs to work together to promote transparency in money flows. This is done through the audit and publication of company payments to governments, and government receipts from companies in the area of oil, gas and mineral extraction. A multi-

donor trust fund administered by the World Bank provides funding and technical assistance to support the initiative. Since its launch, 27 governments in several regions have signed up to the initiative, and most have begun implementation. In our region, Mongolia and Timor-Leste have signed on. Australia is a contributor to the trust fund, and a number of major Australian resource sector companies are participating in it.

Improving governance and tackling corruption are key objectives for Australian development assistance. At the Millennium Summit in 2005, the Prime Minister announced that the Australian aid program would be doubled to around \$4B by 2010, but also linked the increase to ensuring aid effectiveness. "With aid", he said, "comes a reciprocal responsibility on recipient governments to tackle corruption, strengthen governance and promote institutional reform".

Early this year the Minister for Foreign Affairs, Alexander Downer, released a major new aid policy on anti-corruption: *Tackling Corruption for Growth and Development*. The policy focuses on three mutually reinforcing strategies:

- Building constituencies for anti-corruption reform;
- Reducing opportunities for corruption; and
- Changing the incentives for corrupt behaviour.

What does this mean in concrete terms?

Building constituencies for anti-corruption reform: A systematic assault on corruption needs local champions for change and needs to be driven from within a society. It cannot be imposed from outside. High quality political leadership, urged on by an active and informed civil society, is critical to success. The private sector is also an important player, as are industry representatives and trade unions. How then can the aid program assist in building constituencies committed to fighting corruption? Formal and informal education is an important element: training the young men and women who will be the future politicians, public servants, business people and community leaders. Supporting gender equity across the political, executive and managerial levels of government contributes to lowering tolerance for corruption. Strengthening institutions and groups that support good leadership is also important, as are initiatives that encourage public office holders to model ethical work practices and behaviour. And for citizens to demand good governance, they first need information. Collection and analysis of data about the character and costs of corruption, civic education and promotion of media freedom are valuable tools.

Reducing opportunities for corruption: As I've already outlined, poor governance provides greater scope for corrupt behaviour and weak political institutions and processes can facilitate the capture of decision-making by a shadow state within the state. Improved machinery for decision-making, greater scrutiny of decision-making by the elements of the national integrity system, higher standards of accountability of elected representatives to their constituents, and more competitive markets will all help to reduce the opportunities for corrupt dealings.

Much can be done through the aid program to create these conditions: by strengthening electoral systems to achieve fairer and more representative elections; by strengthening the representative and oversight roles of national Parliaments; by supporting the operation of national accountability institutions such as Auditors-General and Ombudsmen; by supporting the development of appropriate legislation, procedures and systems for executive and administrative decision-making; and by supporting efforts to improve business competition and transparency.

Changing incentives for corrupt behaviour: An effective incentive structure will help to build a culture of accountability in government. This means making it riskier and less rewarding to engage in corrupt conduct. But just as importantly it means creating the conditions that allow officials to function professionally and with integrity. There are many examples of effective approaches to changing the incentives around corrupt conduct. These include: improving public financial management processes within finance ministries and line agencies to build a robust audit trail; strengthening the technical capacity of the law and justice system to investigate and prosecute corrupt conduct; improving human resource management and development, including support for merit-based employment practices and implementation of and training in codes of conduct; and offering significant organisational incentives for significant improvements in governance.

Corrupt systems will not change spontaneously, where self-interest is well served by the status quo. This is why it is so important to build up a demand for good governance, to shift the incentives and force change from within. This is where civil society has such a powerful role to play, and where the NGO community can work to good effect with its partners in countries where corruption is widespread. Just getting information out about corrupt practices and individuals, and building an understanding that government is there to serve the people, begins to change the discourse. As I said at the outset, governance is the key. By working to strengthen governance, we erode the conditions that corruption feeds on.

ⁱ Kaufmann, Daniel “Myths and Realities of Governance and Corruption” in World Economic Forum *Global Competitiveness Report 2005-2006*, Palgrave Macmillan, ISBN: 1-4039-9844-2 p83

ⁱⁱ Ibid p85

ⁱⁱⁱ Ibid p85

^{iv} Department for International Development *Governance, Development and Democratic Politics: DFID’s work in building more effective states*, May 2007, p43

^v Kaufman op cit, p83

^{vi} Transparency International *NIS Country Study Report on Solomon Islands*, 2004, p4

^{vii} Fatai, F.A., Auditor-General of Solomon Islands *Audit Report – Department of Forestry, Environment and Conservation 2005* (<http://www.oag.gov.sb/Forestry/Audit%20Report%20DFEC%20Combined.pdf>)