❑ ANTI-CORRUPTION: UNSHACKLING ECONOMIC DEVELOPMENT

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Corruption saps a country's economy by hampering tax collection, wasting resources, deterring private investment, discouraging entrepreneurship and undermining the enforcement of important regulations, says Peter Richardson, an adviser to Transparency International (TI) and former director of Transparency International USA, the U.S. chapter of the nongovernmental organization dedicated to combating corruption. He says it also disproportionately harms the poor because it skews economic planning against investments in social services.

"The Millennium Challenge Account (MCA) eligibility requirement of a demonstrated commitment to limit corruption and promote good governance can be a major step toward changing the incentive system for development assistance," says Nancy Zucker Boswell, TI-USA's managing director. "It will send an important signal that there will be added costs to not addressing corruption – ineligibility for MCA assistance." Boswell and Richardson argue that the policy changes should start with preventive measures such as reforming civil service, where needed, and ensuring transparency of all laws and regulations. They add that countries need to implement a criminal law system where there are "independent prosecutors to bring cases and a competent and independent judiciary to impose sentences."

There is a global consensus that corruption in government and business inhibits economic growth and can perpetuate poverty. Because financial resources are fungible and corruption drains them, economic assistance to countries that have not demonstrated a commitment to reducing corruption is unlikely to lead to sustainable development. This conclusion has led bilateral and multilateral development assistance agencies to reconsider the criteria for aid recipients and to move toward a greater emphasis on good governance.

According to the legislation transmitted recently by the Bush administration to Congress, to merit help from the proposed Millennium Challenge Account (MCA) countries must show by their actions that they are serious about reducing corruption. Such a "demonstrated commitment" is necessary to establish that countries have the requisite determination to spur their own economic development and poverty reduction and to ensure that the intended benefits of such economic assistance will not be dissipated.

CORRUPTION IMPAIRS DEVELOPMENT

Efforts to quantify the economic loss due to corruption are necessarily speculative, but numerous independent estimates have been made. In an estimate by the World Bank, which the Organization for Economic Cooperation and Development (OECD) considers conservative, the annual cost of corruption was calculated at more than $80 billion worldwide – more than the total of all economic assistance. Research at the International Monetary Fund has indicated that corruption can reduce a country's growth rate by 0.5 percentage point per year. A former senior World Bank procurement expert estimates that corruption commonly adds 25 percent to the cost of large government contracts.

Large bribes sap a country's economy, and small bribes – for example, "facilitation" payments to speed up routine government actions – disproportionately harm the poor. Corruption tends to bias country economic planning against the social sectors, which tend to be most beneficial to the very poor, and in favor of large capital-intensive projects, which present more opportunities for large corrupt "rake-offs."

It also undermines economic development and poverty reduction in numerous, diverse, and often immeasurable ways. For example, where corruption is pervasive it deters the best people from entering government service, making corruption self-sustaining; and it provides an incentive for those who have joined the civil service to pursue personal enrichment rather than the public good. This reduces respect for the law, can facilitate crime, and generates cynicism, which feeds the expectation that extortion is inevitable and bribery necessary. Equally important, corruption undermines the enforcement of important regulations, such as building safety codes and environmental protections, and provides an incentive for the proliferation of unnecessary regulatory requirements, each of which creates opportunities to extort bribes.

Tax collection becomes more difficult in highly corrupt environments, making higher tax rates a necessity to obtain required revenue. This can create an incentive for capital flight.

Pervasive corruption can erode political stability, deterring private foreign and domestic investment. Even where stability is not a factor, the high likelihood of extortion discourages such investment.

While correlation does not necessarily indicate causation, it is significant that quantitative analyses have shown that corruption correlates positively with policy distortion and the time business must spend with government officials. It correlates negatively with merit-based recruitment in civil service, civil service wages, predictability of the judiciary, foreign direct investment, the ratio of gross investment to gross domestic product (GDP), women's rights, investment in education, and national environmental performance.

Corruption is not the sole cause of countries' persistent poverty. Poor natural resource endowments, poor economic management, poor education systems, inadequate infrastructure, poor incentives for farmers and businesses, poor administration, and the shortage of savings and capital for investment (to name a few) often contribute. But large-scale corruption invariably impairs development.

WHAT CAN BE DONE ABOUT IT?

While it is unlikely to be totally eliminated, large-scale or pervasive corruption is not inevitable in any country. Movements over time in country rankings on the *Transparency International Corruption Perception Index*, which ranks countries in terms of the degree to which corruption is perceived to exist among public officials and politicians, illustrate that corruption can be tackled.

Given the scope of the problem, a holistic approach and a long-term perspective to anti-corruption reform are essential. Making such an approach operational requires leaders with the political will and a broad mandate from civil society, including the private sector. The participation of all these stakeholders – government, civil society, and the private sector – is essential.
Within many countries, these groups have worked in coalition to list major weaknesses and gaps in the country's "integrity system." They have set priorities, identified targets of opportunity, built sustained political pressure, and monitored the progress of reform.

Diverse conditions, which exist from one country to another, make it impossible to prescribe a universally applicable menu of necessary reforms or any standard sequence for introducing them. Nevertheless, the most urgent reform starts with instituting preventive measures. They are usually more cost effective and less divisive than focusing solely on criminal laws, detection, and prosecution, although the measures anchored in criminal laws can have a long-term deterrent effect when done with persistence and on a large scale.

The most critical preventive measure is for the public sector to undertake to publish in a prompt and accessible manner all laws, regulations, administrative and judicial decisions, procurement, campaign finance, and other routine information. It should provide opportunities for public participation and transparency in the decision-making process before actions are taken.

Preventive measures should also include instituting codes of conduct and conflict-of-interest standards for public officials, with training to promote compliance and sanctions for non-compliance. Higher-ranking officials should publicly disclose their assets on a periodic basis in order to minimize opportunities for illicit enrichment. Whistleblowers and the media must be protected from reprisal so they can play a responsible role.

Beyond the preventive measures, there is a role for criminal law provided there are independent prosecutors to bring cases and a competent and independent judiciary to impose sentences. It is this area that citizens find particularly problematic, given the prevalence of impunity, weak institutional oversight, and lack of respect for the rule of law. The practical effectiveness of recent multilateral conventions that prescribe preventive and criminal measures, including the InterAmerican Convention Against Corruption and the Council of Europe Criminal Law Convention on Corruption, will depend on how these issues are addressed.

Additional public sector reforms often needed will also include: civil service reform, particularly providing compensation that permits a reasonable standard of living; regulatory reform to reduce the number of approvals required and the scope for official discretion in granting them; and strict rules, broad publication and public oversight to promote transparency and accountability in public-sector procurement.

No anti-corruption strategy will be successful without the participation of the private sector. Domestic and multinational corporations should adopt and apply codes of conduct and procedures to promote ethical conduct and to monitor compliance with laws and regulations, including those prohibiting domestic and transnational bribery. Since the entry into force of the OECD Convention on Bribery of Foreign Public Officials, there are criminal prohibitions on transnational bribery. While enforcement of these and related domestic laws will be the prerequisite to changing corporate behavior, corporations are well advised to institute programs that include training, procedures for reporting illegal or unethical behavior, and strong monitoring and enforcement mechanisms. Companies should establish and maintain an effective system of internal controls, books, and records that accurately reflect their transactions and disposition of assets. As a general matter, all professionals, such as accountants, auditors and attorneys, should have and enforce standards and codes of ethics and an effective accreditation process.

Obviously, carrying out such an ambitious range of reforms can be complex and will require a long-term commitment. It will require technical and financial capacity and, above all, political will. The public plays a key role in keeping the subject high on the political agenda. Rankings, such as the annual *Transparency International Corruption Perception Index,* which builds pressure for reform, and "service delivery surveys," which gauge the incidence of bribery in individual government agencies, enable reform efforts to be directed to the areas of greatest need. Other useful surveys include those that assess agency budgetary inputs in relation to outputs and "Big Mac" surveys, which compare the cost of similar items such as aspirins in various public hospitals to identify unjustified divergence.

Bilateral and multilateral development assistance agencies, in designing their assistance strategies, must also play a key role. Mainstreaming anti-corruption into country assistance strategies will help reformers. The institution of systems for investigating allegations of corruption in procurement and for debarring firms found to have engaged in corruption is another step forward. Multilateral development banks could do more, including adding as a condition for bidding a requirement that bidders have anti-bribery codes of conduct and compliance programs.

CONCLUSION

The MCA eligibility requirement for a demonstrated commitment to limit corruption and promote good governance will be a major step towards changing the incentive system for development assistance. It will add to the already enormous costs of corruption for those who fail to meet these criteria. Donors must consider how the needs of these countries will be addressed. In those that do meet the requirement, MCA assistance can help promote reform because it requires governments, businesses, and civil society to work together in a constructive partnership. In so doing, it has the potential to improve the prospects for economic development and the productive use of assistance. Realizing this potential will require field-based assessments of the state of corruption in a country and the effectiveness of MCA projects, and careful attention to auditing and accountability to ensure that funds are used as intended. This will be a huge challenge but one that promises to have a profound impact on future assistance strategies and their success in combating corruption. ❏

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