

9. Improving Public Sector Governance: The Grand Challenge?

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That many states are failing to deliver on their most basic functions is a harsh reality. Generalizations are dangerous given the wide diversity of developing countries. But the typical developing country state today is faced with rising expectations, a growing and disparate population, and a rapidly changing international environment—all of which outstrip its ability to deliver public goods and services.

States have responded to these challenges with varying degrees of competence. At one end of the spectrum are the failed states, where governments barely exist, and where they do, provide hardly any services. At the other extreme are a handful of countries where leadership and bureaucracies are relatively competent and governments are doing well by the people. In between are weak or predatory states that “consume the surplus they extract, encourage private actors to shift from productive activities to unproductive rent seeking and fail to provide collective goods” (Evans 1995: 24); young democracies struggling with a difficult political transition, managing simultaneous political and economic liberalization with weak bureaucracies and few checks and balances; and more mature democracies where governments are doing the best they can, but face the same difficulties as the advanced countries when it comes to political corruption and abuse of office. Then there are the large, continent-size polities such as India and Brazil which are difficult to categorize, because within their national boundaries can be found the entire range of governance configurations. Peru and Pakistan have as little in common as China and Chad. But all countries now face a common challenge: how to get governance “right.”

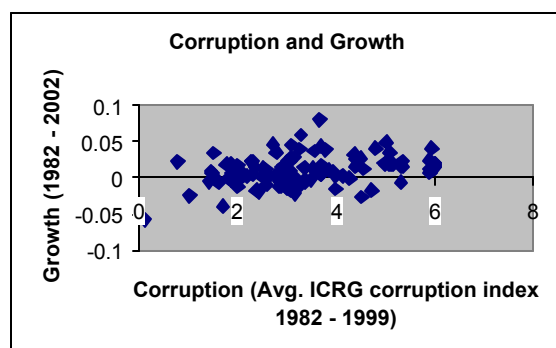
Though extensive research had been done into the causes and impact of poor governance, and in particular of corruption¹, it was not until the mid-1990s, with improvements in data and econometric techniques, that large, cross-country analyses emerged on the impact of governance institutions on investment and growth. This research has shown that corruption—which is both a symptom and cause of bad governance—discourages private investment and, more generally, that the quality of governance institutions has a significant if not predominant impact on economic growth (Mauro 1996; Keefer and Knack 1996; Wei 1996, 1997; World Bank 1997; Kaufman et al. 2000 and 2002; Rodrik et al. 2002). Further, it has provided evidence of what analytical studies have long argued and case studies have suggested: corruption distorts the allocation of resources in ways that hamper poverty alleviation—that is, corruption hurts the poor (Mauro 1998; Davoodi and Tanzi 1998; Gupta, S. et al. 2002).² Figure 9.1 summarizes the basic results of these studies.

¹ See for instance Susan Rose Ackerman (2004) and Robert Klitgaard (1988) among others. Much of the work on rent-seeking that punctuated the literature from the mid-1970s to the 1980s, for example Krueger (1976) and Bhagwati (1978), essentially tackled conceptual issues.

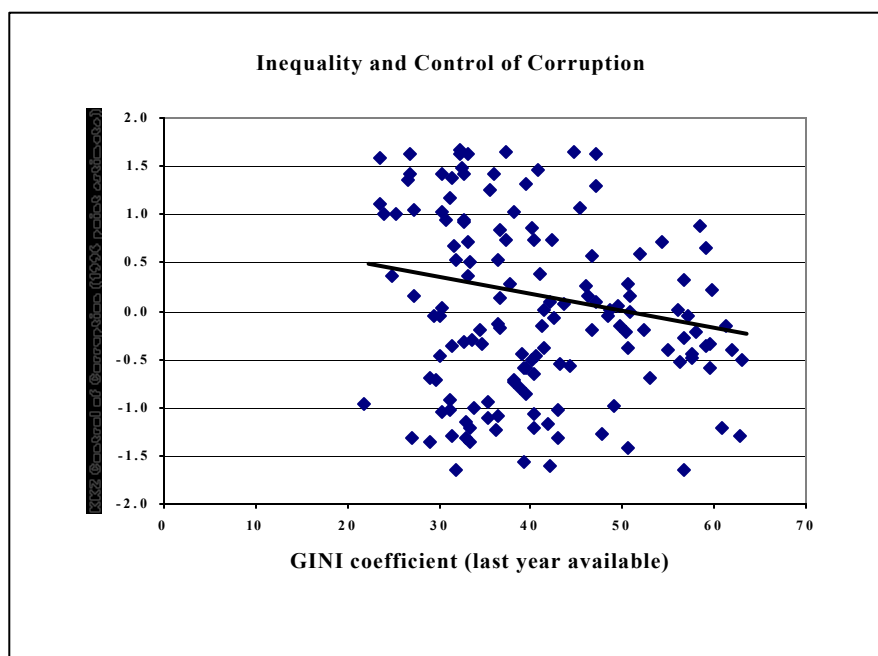
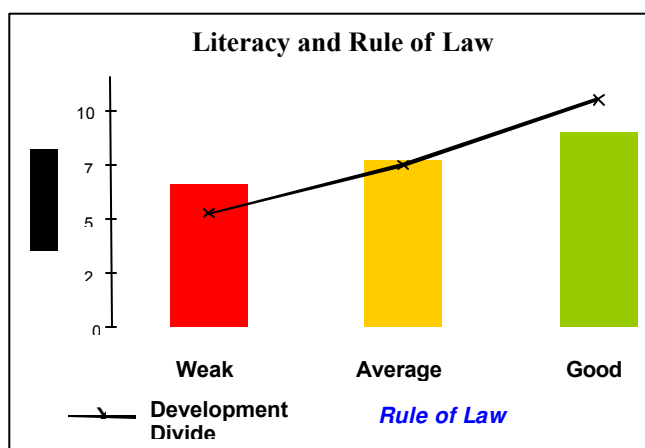
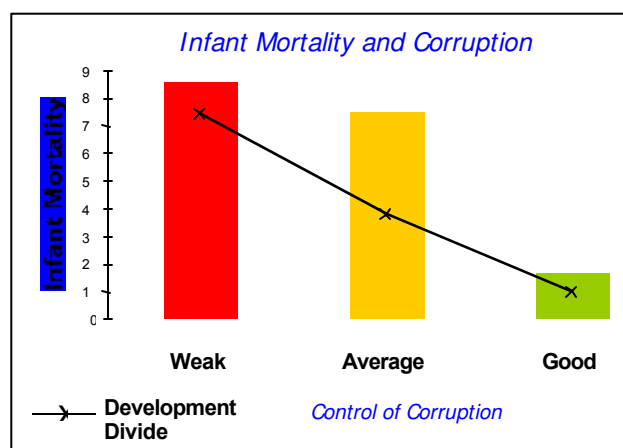
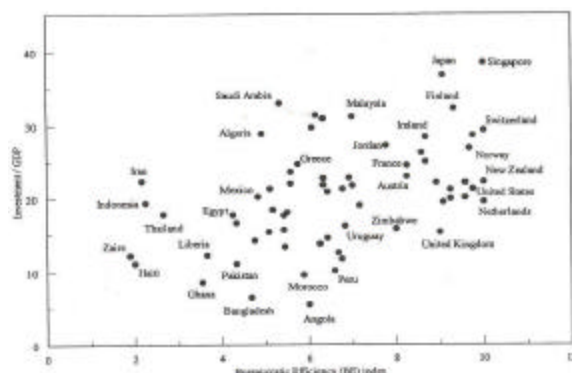
² The causality can work both ways, with growth also perhaps inducing better governance. Rodrik and Subramanian (2003) and Subramanian and Roy (2001) attempt to address this.

Figure 9.1: Corruption and investment, growth, poverty, and inequality

Corruption and Investment



Corruption and Growth



Combined with the extensive public awareness efforts of international organizations such as Transparency International and the World Bank ³, the empirical research has helped to stimulate governance reforms in developing countries. The 1990s saw a mushrooming of efforts to improve the governance of the public sector, from very focused, technical reforms of budgetary and civil service systems to more encompassing efforts such as decentralization and the overhaul of legal and judicial systems.⁴

This chapter reviews these efforts. Section 1 introduces key terms—governance, corruption, institutions—and, building on a simple framework adapted from *World Development Report 2004*, briefly discusses why governance reforms are particularly challenging. Section 2 reviews the varied efforts of countries to improve governance, focusing on a few key areas, and draws emerging lessons from this experience. Recognizing that one size does not fit all, Section 3 presents a heuristic approach to identifying possible avenues for reforms, depending on broad country characteristics. It concludes by examining the obstacles reformers face in improving governance and what potential routes one might take to address them.

1. *Understanding the governance conundrum*

Economic performance—growth, investment, and poverty reduction—depends in part on governance. In turn governance is shaped by underlying institutions. Public sector governance refers to the manner in which the state acquires and exercises the authority to provide and manage public goods and services. Corruption, which refers to the use of public office for private gain, is the mirror image of governance: bad governance invariably leads to corruption; but corruption can likewise perpetrate bad governance.

The quality of governance (and thus nature and extent of corruption) depends fundamentally on institutions, defined broadly as the “rules of the game” that shape the behavior of organizations and individuals in a society (North 1990:3). Institutions can be formal rules, such as a country’s constitution, its laws and regulations, contracts and internal procedures.⁵ Or they can be informal rules, such as the values and norms that drive bureaucratic behavior. Though scholarly research and concern with institutions is not new, a strong interest in institutions reemerged in the 1990s, primarily because the stronger macroeconomic policies of the 1980s had not brought more rapid progress in development and poverty reduction. Interest moved from “getting the policies right” to “getting the institutions right” and had a

³ The “Cancer of Corruption” speech given by World Bank President James Wolfensohn at the 1996 IMF/World Bank Annual Meetings is considered to be a watershed in the Bank in the fight against corruption and the push for reforms of governance institutions in developing countries. The publication of Transparency International’s Corruption Perception Index made governments and their constituent publics more aware of problems of corruption and helped trigger the development of cross-country empirical studies and survey-based diagnostic work on corruption (see for instance, Kaufman 1999; Reinikka and Svensson 2003).

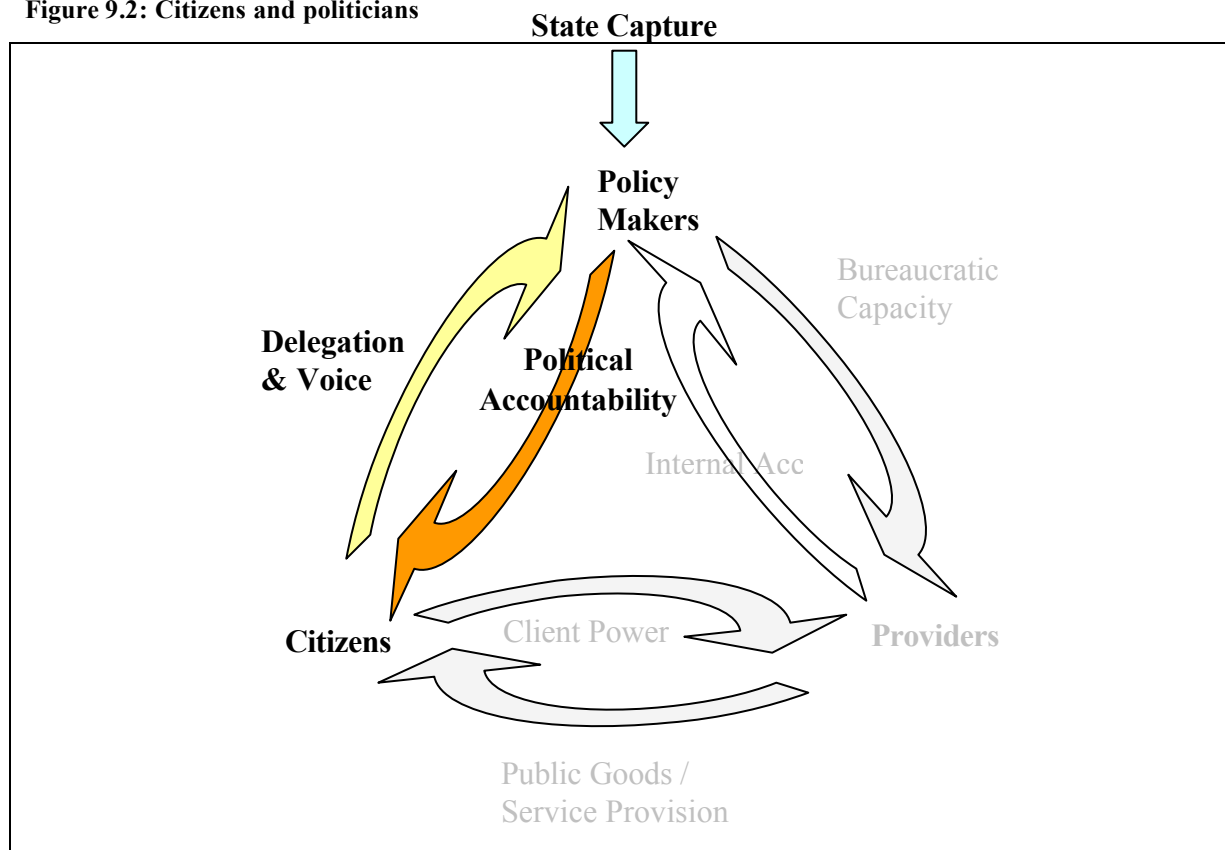
⁴ Perhaps the most encompassing reform has been the introduction of electoral institutions, which is the subject of Chapter 9.

⁵ Formal organizations such as the central bank are also often referred to as institutions. In the abstract, an organization is a collectivity functioning within a predetermined set of formal rules. That is, it is an agglomeration of rules that affects the behavior of a given set of individuals.

particular focus—the rules of the game upon which governance of the public sector is grounded.

Fundamentally, public sector governance is about the nature and quality of three principal relationships: between citizens and politicians, between politicians as policymakers and the bureaucracy (those responsible for providing public goods and services), and between the bureaucracy as delivery agents and the citizenry as clients (Figure 9.2).⁶

Figure 9.2: Citizens and politicians



Citizens and politicians: the heart of governance

In an ideal world, citizens can hold politicians accountable for their actions and for policy outcomes. Political accountability comes about through two channels. The first, which we might call the “direct” channel, is through elections and the second, which we might call the

⁶ *World Development Report 2004* characterizes the bilateral relationships as one of accountability (of agents to principals). But the relationship can also be affected by other factors—in particular, capacity issues. If the agent lacks the ability or the resources to perform his task then no matter how strong the accountability link, he or she will be unable to deliver on his or her mandate. If, for instance, bureaucrats have a poor financial management information system to work with, they cannot produce adequate information upon which to judge their performance.

indirect channel, is through checks and balances on the abuse of power.⁷ Periodic elections provide the basic means through which citizens can hold politicians' feet to the fire. Restraints in the form of court adjudication of disputes among contracting parties, especially between government and the citizenry, and legislative oversight of executive or ruling party decisions and actions, foster accountability in between elections. In well functioning democracies, these latter features are embodied in the constitution and promote the rule of law. Everyone, politicians included, behaves in accordance with agreed rules as embodied in laws and regulations and no one, even the highest elected or appointed public official, is above the law.

Reality differs significantly from this ideal world. First, many countries are not democracies. Some are purely authoritarian and others, while exhibiting the formal trappings of a democracy, lack a truly independent parliament or judiciary. And, second, as chapter 10 discusses, even in countries where there are regular competitive elections among multiple political parties or candidates, elections often do not have the desired effect, so that politicians can easily shirk from their campaign promises and responsibilities.⁸ In either case, weak institutions typically govern the relationship between citizens and politicians.⁹ Courts are easily swayed by pressure from influential politicians; the legislature rubber-stamps the narrowly focused special interest initiatives of the executive; high-ranking officials abuse their authority for private gain; and enforcement agencies prey on the citizenry. In other words, the rule of law is weak. When the rule of law is weak, a particularly aggressive form of corruption can easily emerge: state capture. Worse, when state capture occurs, the rule of law could be weakened further or attempts to improve it stymied.

State capture "refers to actions of individuals, groups, or firms either in the public and/or private sectors to influence the formation of laws, regulations, decrees, and other government policies to their advantage, through the illicit and non-transparent provision of private benefits to politicians and/or civil servants (World Bank 2000)."¹⁰ As Kaufmann (2003) argues, it is a serious problem in many developing countries. When pervasive, it becomes the principal stumbling block for efforts to reform governance institutions: why should the powers that be change the rules of the game when they benefit immensely from them?

⁷ A third channel, through so-called citizen "voice", involves mechanisms that citizens can use to inform politicians of problems, needs, and preferences. This is discussed as part of the third leg of the relationship triad: citizen power.

⁸ See also chapter 5, *WDR 2004*.

⁹ For clarity, this refers to two general types of institutions. The first are political institutions—rules or arrangements that define, govern, and influence how leaders and other politicians are selected and replaced. The second are institutions of restraint—rules or arrangements that establish checks and balances on the abuse of power and authority.

¹⁰ More specifically, the possibility of obtaining rents drives influential groups and/or individuals to bribe politicians or high-ranking civil servants. In turn, the latter introduce and maintain bad laws, policies, or regulations in order to perpetrate their illicit earnings. Note that in this context, corruption causes bad governance.

Politicians/policymakers and the bureaucracy: the core principal agent problem

Politicians are a country's primary policymakers and as such are responsible to the citizenry for the policies that are eventually promulgated and implemented. However, they do not implement policy. Rather they *delegate* this responsibility to an army of bureaucrats.¹¹ In delegating, politicians establish the rules and regulations, i.e. the institutions, that govern the operations of the civil service. These include, for example, formal institutions such as a civil service code, the budgeting system, or reporting systems and informal institutions such as the practice of *amakudari* in Japan.¹²

Delegation almost always gives rise to what economists call the principal-agent problem. The principal delegates the implementation of a task to an agent but in so doing faces the problem of insuring that the agent indeed completes it as he (the principal) has envisaged. The agent will most certainly know whether he has accomplished the task as mandated or not. But the principal, being at least one step removed from the process, will have to establish tractable means of monitoring the agent in order to confirm exactly what has been accomplished. In other words, delegation results in an information asymmetry between the principal and the agent in which the former is disadvantaged and therefore must incorporate efficient means of monitoring the latter.

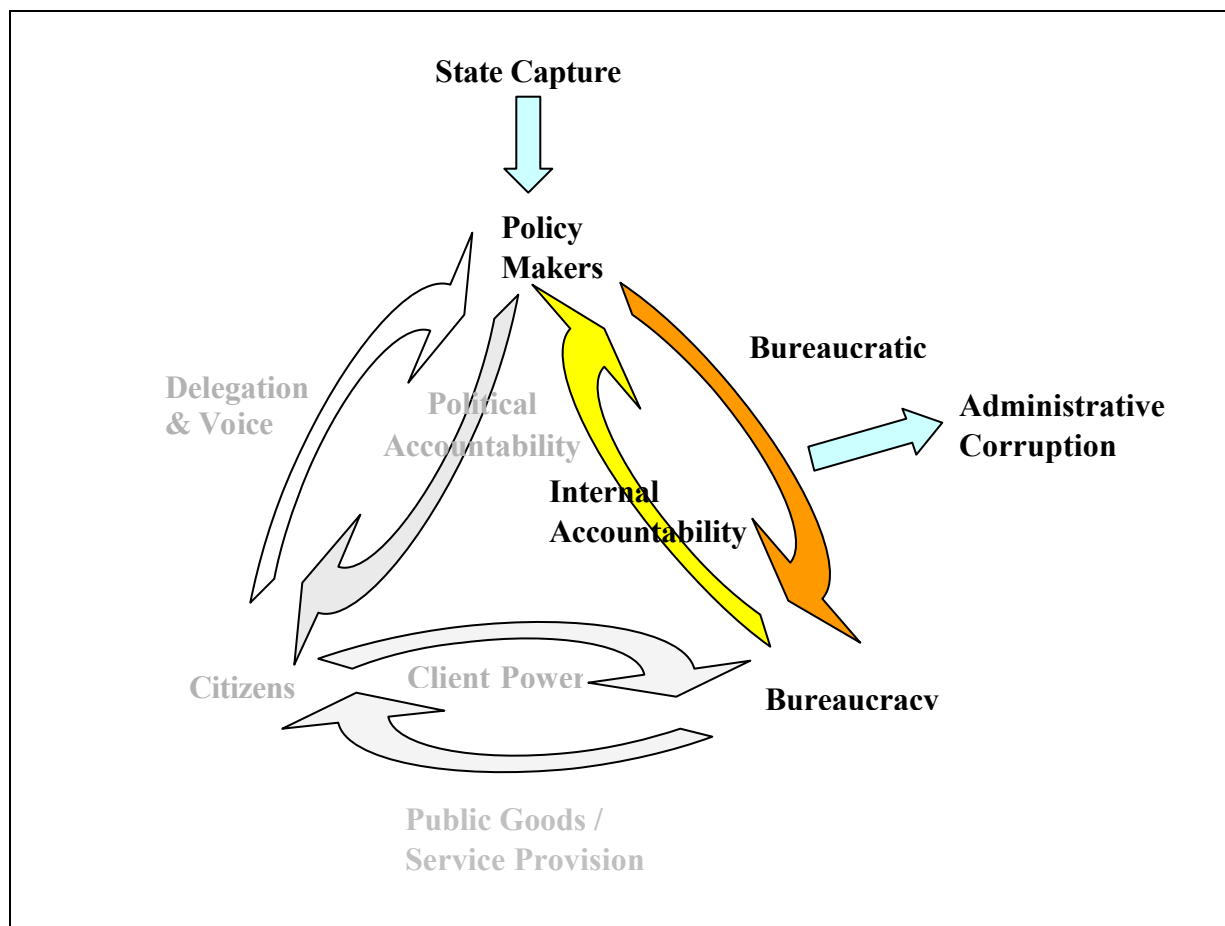
In delegating the task of implementation, policymakers establish a compact with bureaucrats. This compact has two major features. First, it provides the means through which the bureaucracy can develop and enhance its capacity to implement policies and deliver public goods and services. After all, if bureaucrats do not have adequate capacity then they cannot be expected to deliver effectively on their mandates no matter how hard they try. Capacity in this context refers to (1) the skills bureaucrats need to deliver on various mandates, (2) the resources (capital and financial) to support the needed efforts, and (3) the processes and systems (such as the budgeting system and the procedures for using it) that enable large numbers of individuals to function like a well oiled machine. Second, the compact also establishes means through which bureaucrats can be held accountable to policymakers for performing their tasks. Accountability in this context—which for clarity will be referred to as internal accountability—means that bureaucrats are responsible to policymakers for accomplishing certain tasks and are prepared to explain and face the consequences of any corresponding deficiencies or failures. Accountability mechanisms typically involve internal checks and balances (internal to government agencies), such as internal audit, ex post program evaluations, and ex post reporting, as well as external (to government agencies) restraints, such as exercised by the ombudsman, supreme audit institutions, and anti-corruption commissions.

¹¹ In practice, the bureaucracy can also delegate some responsibilities to non-government organizations, e.g. contracting out to private providers.

¹² *Amakudari* (meaning literally descent from heaven) refers to the long-standing though unofficial practice in Japan of rewarding successful high ranking career civil servants with a high paying, prestigious job in the private sector for a fixed period, e.g. five years, upon retirement. See Chalmers Johnson (1982) *MITI and the Japanese Miracle*.

Adequate capacity is necessary for accountability to work. Information is needed for auditing, performance evaluation, reporting, investigations, and prosecution. And processes, skills, and resources are needed to provide the infrastructure and create the incentives to produce the right information. In the same vein, more effective accountability helps strengthen capacity, as policymakers are more willing to grant greater flexibility and resources make the bureaucracy even more effective. Figure 9.3 highlights the salient features of the compact.

Figure 9.3: Politicians/policymakers and the bureaucracy



The quantity and quality of services and the outcomes of policies depend crucially on the nature of the compact. When the compact is defective, either because of weak capacity and/or poor accountability, administrative (or bureaucratic) corruption typically emerges. Administrative corruption “refers to the intentional imposition of distortions in the prescribed implementation of laws, rules, and regulations to provide advantages to individuals resulting from illicit private gains to public officials (World Bank 2000).” Weak capacity and/or accountability translate into numerous opportunities for soliciting or extracting bribes and other illicit side payments. Indeed, a number of empirical studies have shown that deficiencies in civil service processes and procedures tend to lead to increased administrative corruption (Van Rieckeghem and Weder 2001; Evans and Rausch 1997; World Bank 1997)

and have confirmed what numerous case studies have found (see for instance Rose-Ackerman 1978; Wade 1982; Klitgaard 1988, 1990).¹³

Though administrative corruption differs fundamentally from state capture, the two are inextricably linked. Politicians are at the heart of state capture, either as perpetrators or as willing respondents to the captors.¹⁴ But bureaucrats are the ones who will implement the distorted policies that result from capture. Hence, politicians need the acquiescence, if not the active participation, of at least some segments of the bureaucracy. What this implies in practice is that politicians constrain the capacity of the bureaucrats or weaken their accountability. For instance, in many developing countries, the annual budgets allocated to the Ombudsman or to the supreme audit institution are far smaller than what is needed for them to perform their tasks adequately, and the personnel appointed to key posts are rarely the most qualified (Heilbrun 2003). Moreover, as chapter 10 points out, politicians will prefer to sustain clientilistic practices within the bureaucracy rather than to introduce formal, transparent merit-based recruitment processes. That is, the compact is itself partly conditioned by the extent of state capture.

Bureaucrats and the citizenry: where the rubber hits the road

Most citizens' immediate contact with the state is through the bureaucracy. From obtaining a driver's license to enrolling children in the community public school to arguing with a traffic policeman, citizens have much more frequent and regular dealings with the bureaucracy than with politicians. Ideally, citizens should be able to hold civil servants directly accountable for the poor implementation of policies and programs. But in reality they have to go a longer and sometimes circuitous route: from citizens to politicians/policymakers and then from the latter to bureaucrats through the compact.¹⁵ They can complain to their congressman or mayor about the poor quality or inadequacy of some service and hope that the latter intercede with or pressure the bureaucracy on their behalf. And if they have generally been unhappy with the response they can vote the latter out of office. But they cannot penalize or punish bureaucrats directly or officially.¹⁶

Citizens do have leverage over the bureaucracy if they can organize themselves into nongovernmental organizations, parent associations, religious organizations, and so forth, and use those organizations to inform politicians about what is going on the ground—thus pressuring them to get the bureaucracy to work more efficiently or, more directly, to participate in the actual provision of some services.¹⁷ The capacity to organize gives citizens

¹³ The relation between public sector pay and corruption is controversial. It is commonly presumed that the lower public sector compensation, the greater is administrative corruption. Various empirical studies suggest that there are clearly other factors at play that confound this relationship. See World Bank, Administrative and civil service Reform website, <http://www1.worldbank.org/publicsector/civilservice/ineffectivemon.htm#4>

¹⁴ See **Global Corruption Report 2004** [Need complete reference].

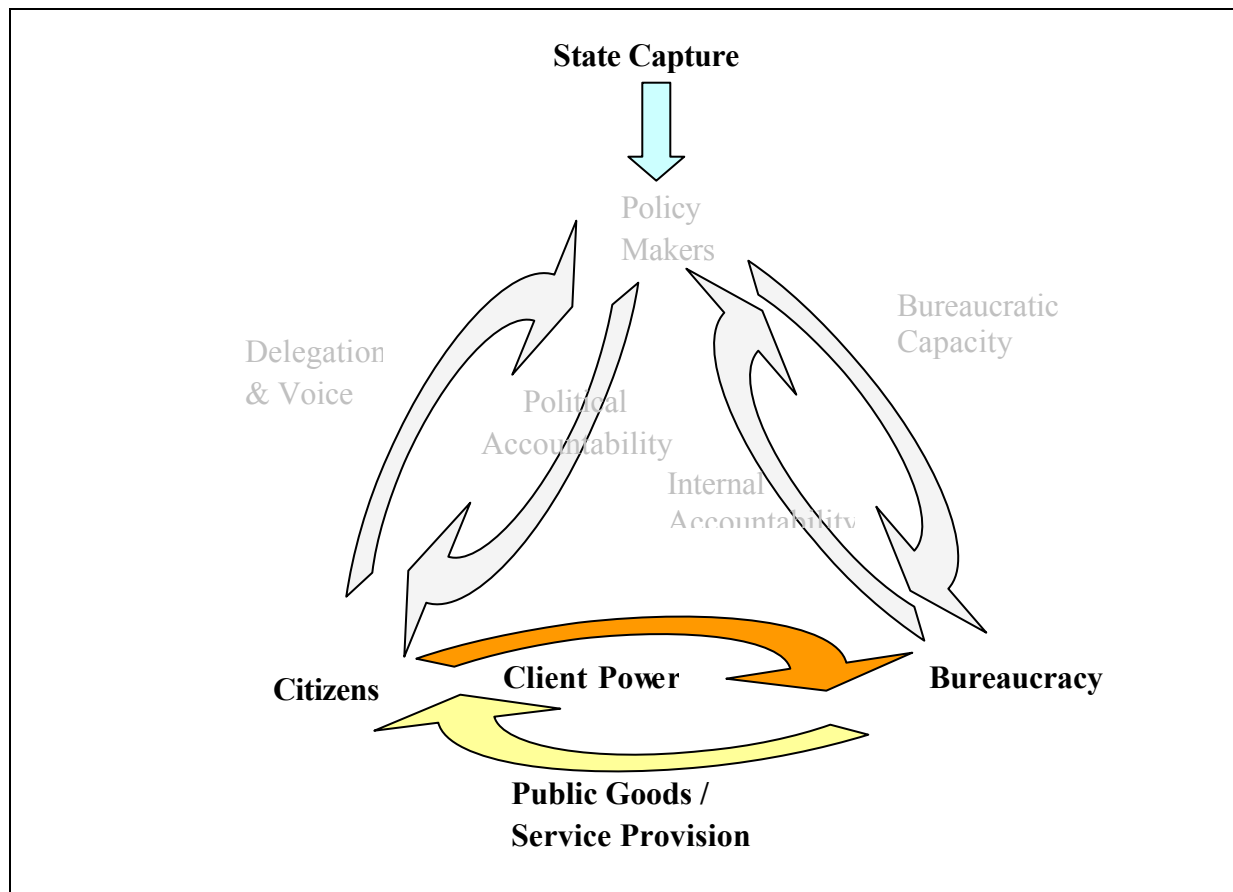
¹⁵ See the World Development Report 2004 for a thorough explanation of the long route of accountability.

¹⁶ At the community level, citizens can use "shame tactics" to pressure local level civil servants who themselves must also live within the same community.

¹⁷ Social development specialists refer to these as forms of social accountability (Ackerman 2004). While these are generally accepted, if not encouraged, in democracies, they are often presumed to be restricted in authoritarian regimes. In practice, however, authoritarian regimes do care about the satisfaction of the citizenry

so-called “voice”—the ability to monitor the performance of the bureaucracy, generate valuable information, and pressure politicians for action—and “client power”—the ability to engage directly with service providers in providing services—both of which strengthen the compact between politicians and the bureaucracy and thus help improve the delivery of public goods and services.¹⁸ Figure 9.4 highlights the role of voice and client power in the triad.

Figure 9.4: Bureaucrats and the citizenry



Citizens generally find it difficult to organize. Collective action is costly and so does not always emerge naturally. Hence citizens are often left to fend for themselves. In situations where the link between them and the politicians is weak, as when electoral processes are flawed, this can exacerbate the problem of administrative corruption. Desperate to get some

with basic public goods and services, because their legitimacy depends partly on it. For a good example, see John Pomfret, “SARS Reported in Rural China,” available online at <http://stacks.msnbc.com/news/904928.asp?cp1=1>, and John Pomfret, “China to Open Field in Local Elections,” *Washington Post* June 12, 2003.

¹⁸ It should be noted that “client power” also includes the ability of citizens to choose among different providers of the same service. This however does not require collective action on their part; rather it requires policy decisions to promote some form of competition among service providers. On the latter, voice (and thus organization) however can play a role in getting politicians to promulgate those policies

service, citizens may ultimately offer bribes or to give in to bureaucratic demands for bribes. The inability to organize can thus worsen an already defective compact. In short, one way or another, citizens can indirectly influence the delivery of public goods and services.

2. *Public sector governance reforms in the 1990s*

This section identifies some potential lessons from the governance reforms of the 1990s, using the analytical framework outlined in Section 1 as a guide. Given the scope of the issues involved and the long-term nature of these reforms, one can of course only offer a glimpse of what lessons seem to be emerging.

Enhancing political accountability

Democracies, particularly nascent ones, face dilemmas in promoting genuine political competition, and thus in establishing political accountability (chapter 10). When the citizenry cannot clearly attribute responsibility for poor outcomes to politicians, elections—already blunt instruments for accountability—become distorted, and this enables non-performing or poor performing politicians to remain in power.¹⁹ The direct channel thus remains weak.

Perhaps partly because of the immense difficulty of addressing problems in political institutions, countries, and donors turned to the other channel of political accountability, which seemed more amenable to technical solutions.²⁰

Legal and judicial reforms cannot be technical short cuts to the rule of law

Despite problems in the political arena, serious efforts at reforming legal and judicial systems emerged in developing countries during the 1990s. Two trends—the privatization thrust and the new emphasis on private sector development—helped make legal and judicial reform an imperative in many developing countries.²¹ Law and development activities skyrocketed during the 1990s, with the IFIs and key donors stepping up loans and grants to support legal and judicial reform.²²

¹⁹ Political accountability during elections can be enhanced by independent electoral commissions. However, such institutions may themselves also be subject to capture.

²⁰ Work has been done on reforming political institutions, including attempts at reform in political campaign finance. But such efforts have been far fewer than those devoted to legal, judicial, and legislative reforms.

²¹ The heightened concern with improving legal and judicial systems in the 1990s was predated by similar concerns and reform efforts in the 1960s—some of which are only now beginning to bear fruit. Moreover, there are other factors that have made governments in both developing and developed countries much more concerned with legal and judicial reforms in the 1990s. These include globalization and trade, drug trafficking, human rights, immigration, the protection of intellectual property, the suppression of terrorism, and the consolidation of emerging democracies. See Messick (2003).

²² The World Bank's first significant effort was a 1990 adjustment loan to Bangladesh followed two years later by support to Tanzania for training judges, upgrading legal libraries, and publication of court decisions. In 1992 the Bank also extended a \$30 million loan to Venezuela solely for judicial reform. This was the first of 11 investment loans totaling close to \$200 million that the Bank extended principally for judicial reform during the 1990s. Data from other organizations show a similar increase in judicial reform activities. Starting from scratch in the 1990s, the Inter-American Development Bank had made 18 loans totaling \$418 million by June 2001, and entered into 65 technical cooperation agreements comprising another \$43 million to support reform of judicial

Pragmatic approaches to legal reform have been more effective and are more likely to succeed

Most private sector law reforms were supported through short-term technical assistance involving one or more foreign law professors or practitioners expert in a particular area or sub-area (Kovacic 1995; deLisle 1999). Foreign experts typically brought the text of their own country's law, either as a basis for drafting a country-specific statute or simply for adoption wholesale. For example, in the early 1990s the Ukrainian legislature was asked to enact a verbatim translation of the Uniform Commercial Code—a lengthy American statute governing sales, leasing, and related transactions—and advisors to the Mongolian government suggested that to create a stock market Mongolia simply copy US securities laws.

The ease and low cost with which law reform assistance could be supplied produced a rash of activity. The pace was particularly frantic in the transition countries whose business-related laws were either out of date or, as in the states of the former Soviet Union, had never existed. For instance, in the three Baltic states of Estonia, Latvia, Lithuania, “hundreds of laws were passed . . . in the early 1990s, and when government regulations are added, the number grows into the thousands” (Klavins 2000: 4).

Many of the new laws have had little or no effect on behavior. Several nations of the former Soviet Union have statutes that on paper provide corporate shareholders more protection than under French or German law, but in practice, as capital flows attest, investor rights in France and Germany are much more secure (Pistor, Raiser, and Gelfer 2000: 65). Albania and Romania have enacted statutes governing the posting of collateral for a loan and the regulation of banks and securities markets, but businesses report that the statutes are ineffective (Gupta, Kleinfeld, and Salinas 2002: 13-14). And although new laws in Bangladesh, Benin, and Pakistan require bank debtors to repay their outstanding loans immediately, most debts remain unpaid (Messick 2004).

A number of lessons have emerged from these experiences. First, a new law must reflect the realities of the institutional environment within which it is to be inserted, including in particular the state of the institutions that will enforce it—judiciary, ministry of justice, the police, and regulatory agencies. When the agencies that will enforce a new law are corrupt, technically incompetent, or insufficiently independent of political authorities, the law must compensate for these deficiencies.

institutions (Biebesheimer and Payne 2001: 12). Likewise, the US Agency for International Development, which had a small court reform program in the mid-1980s, had provided \$ _____ million in grants to judiciaries throughout the developing world by _____.

Box 9.1: Bright line rules vs. standards

An early lesson that law reformers learned was the importance of substituting bright line rules for standards wherever possible. A bright line rule specifies the exact conduct expected, an example being a law establishing 45 mph speed limit, whereas a standard leaves the question of violation to the enforcement agency, such as a law making a “reasonable speed” the limit. Bright line rules put less of a burden on enforcers than standards. The determination of whether a driver was exceeding 45 mph is straightforward, whereas deciding whether a speed was reasonable requires investigation into such factors as time of day, weather conditions, and the presence of pedestrians and other traffic. Bright lines rules also leave enforcers with little or no discretion and so reduce opportunities for bribery. Since the enforcement of bright line rules is far easier to monitor, this can provide openings for self-help and other means of enforcing the law without resort to the authorities (Hay and Shliefer 1998).

Second, implementation can be made easier if custom is incorporated into the law, given that customs are norms that citizens are already observing. Hernando de Soto (1988) for instance spearheaded several law reforms in Peru that incorporated the norms and practices of street vendors, urban transit operators, and small landholders into law. Peru’s new land law, granting urban squatters property rights to their land, relies on customary methods of showing possession to establish these rights.

Third, a transparent and inclusive reform process reduces opposition to a new law and enhances compliance. The counsel for law reform of the European Bank for Reconstruction and Development, reflecting on EBRD’s experience during the 1990s, asserted that “the most important lesson for the sustainability of effective legal reform over the long term is the need to develop and nurture a transparent and inclusive legal reform process” (Bernstein 2002: 9). In its projects, EBRD has included not only representatives of various government ministries, regulators, judges, and legislators but also businesses and other civil society groups.

Poor incentives rather than weak capacity have been the root cause of poor judicial performance

The concern with improving the implementation of laws and in particular the enforcement of contracts—between businesses, between lenders and borrowers, and between consumers and vendors—gave rise to parallel reforms of the judiciary. Part of the impetus arose from seminal work on institutions and economic growth. In an influential piece that appeared in 1990, Douglass North asserted that poor enforcement of contracts was the principal reason why some countries remained poor. North contended that the absence of low-cost means of enforcing contracts was “the most important source of both historical stagnation and contemporary underdevelopment in the Third World” (1990: 54). In the context of privatizations and private investment, a well functioning judiciary meant that contracts could be affordably enforced and that the government could not therefore easily expropriate private property, either directly (through confiscation) or indirectly (through onerous taxation) without due cause. A government that has the power to coerce has the power to confiscate as well, and thus has the potential to discourage private sector activity (Weingast 1995). The

judiciary would restrain politicians (and bureaucrats) from making whimsical, self-serving decisions that violate the rights of firms and individuals.

Elaborating on this thesis, Oliver Williamson (1995) argued that when the judiciary cannot enforce contractual obligations, one of two things happens. Either a disproportionately large number of transactions occur in the spot market, where there is less opportunity for contract breach, or firms circumvent the judicial system altogether by purchasing their suppliers or customers, turning arms-length transaction into intra-firm ones. But in both cases, he argued, the results were higher transaction costs and hence a “low-performance economy.” In short, judicial reform should be of paramount concern to developing countries.

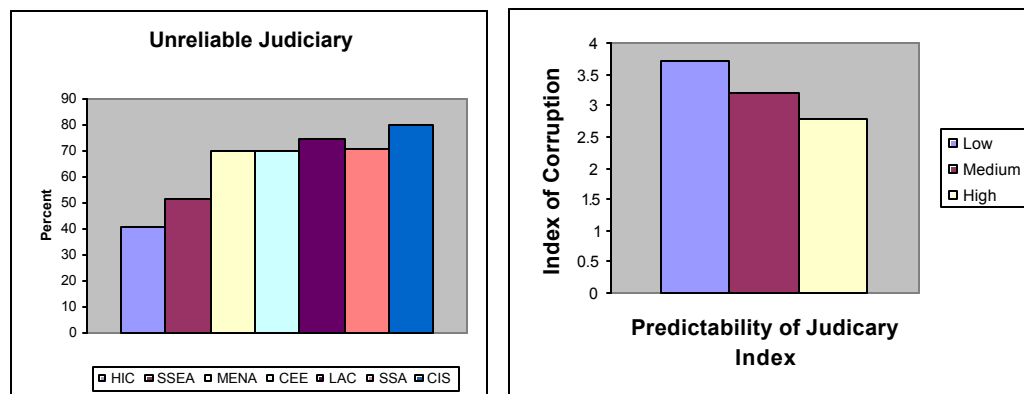
As the decade unfolded, a broader rationale for judicial reform replaced the narrow emphasis on contract enforcement. With increasing frequency a better functioning judiciary was linked to, if not equated with, the rule of law. This Anglo-Saxon concept—and related ones in use in Europe, Latin America, Asia, and Africa—can mean many different things (Stephenson 1999). But in the parlance of the development community the rule of law became synonymous with a state where laws effectively restrained rulers from opportunistically seizing private property and simultaneously promoted welfare-enhancing cooperation among the citizenry. This broader emphasis coincided with the growing recognition in the international community that a well-performing judiciary was part of the solution to many problems of development. By the close of the 1990s, judicial reform had, in the words of one practitioner, become “the big tent for social, economic, and political change generally” (Jensen 2003: 347). Perhaps somewhat unfortunately, judicial reform became the entry point to a problem that was fundamentally political in nature because it lent itself more readily to “technical” solutions.

This widening of objectives was matched by significant changes in judicial reform programming among donors, particularly the international financial institutions. World Bank judicial reform projects to create commercial courts and support similarly focused interventions rapidly gave way to much more ambitious undertakings. Projects included support for new institutions to assume responsibility for governing the judicial branch, revising rules on the selection and promotion of judges, overhauling the management of the judiciary’s human and physical resources, rooting out corruption, constructing new court houses and equipping them with modern communications and computer technology, training lawyers and judges, providing programs to reach out to women and the poor, and establishing administrative courts.

Reforming courts and related institutions has proven to be a far greater challenge than expected. At the start of the decade, judiciaries in virtually every developing and transition nation confronted a host of similar problems: decrepit buildings, inadequate equipment, poorly trained and underpaid judges and support personnel, cumbersome procedures, and poor management of personnel and physical resources. Not surprisingly, early projects aimed directly at curing these ills. But, like the attempted reforms of other public sector institutions during the 1990s (World Bank 2000), most of these interventions produced little change (Burki and Perry 1998; Carothers 1996; Blair and Hansen 1994; GAO 1993). Figure 9.5 illustrates the inertia. In 1996, the business community in various countries around the world

perceived their respective judiciaries to be unreliable and thus to have contributed to corruption.

Figure 9.5: Judiciary and corruption



Source: World Bank, *World Development Report 1997*.

[charts need more explanation. Dates, countries covered, concepts used.]

As experience grew with judicial reform, it became clear that the roots of poorly performing courts lay much less in a lack of resources and skills than in the behavior of judges, clerks, lawyers, and litigants. Domestically inspired and supported reforms to the courts in India offer a well-documented example. There, an enormous number of tribunals have been created to handle civil service, tax, land, and consumer cases to reduce the burden on the regular civil courts and to speed up the disposition of cases. But these reforms have had little effect (Moog 1997). The reason is that lawyers, clerks, and many litigants have an interest in court delay and thus continue to frustrate reform efforts. That is, state capture has compromised the proper functioning of formal institutions.

Development of complementary institutions is essential for reform

Another lesson emerging from the experience of the 1990s is that the absence of parallel institutional reforms will tend to negate any progress in judicial reform. For example, reform of the police and the public prosecutor offices are key complementary reforms, which if left unattended will hinder efforts to improve the judiciary (Box 9.2).

Box 9.2: Integrated justice sector reforms: the Jamaican case

The justice sector plays a critical role in enforcing the rule of law and protecting property rights and the rights of citizens. Safeguarding the accountability mechanisms that underpin the justice sector requires effective collaboration between the courts and the police. Successful violence reduction programs substantially increase the cost of crime by combining a high probability of capture (by the police) with a high probability of conviction (by the judicial system).

Investment climate surveys show that property crime is a growing worldwide problem that adversely affects investor confidence. Jamaica's fairly well developed judicial system has been criticized because of dramatic increases in political and criminal violence. But an effective crime prevention strategy in Jamaica would need to match the effectiveness of the judicial system with better police capabilities: to complement the probability of conviction by the judicial system, Jamaica would need to increase police accountability and improve police-community relations.

Source: US Library of Congress country study and study by the Jamaican country team, World Bank Group 2004.

While most efforts at judicial reform focused on improving the court system, some dealt with alternative dispute resolution mechanisms. These projects both under- and over-estimated the role of institutions in resolving disputes among contracting parties. Arbitration, mediation, and other dispute resolution methods were offered as a way to channel disputes away from the courts to private fora. At the same time, projects largely ignored that many disputes could be avoided altogether if more information were available on the creditworthiness and reliability of potential contracting parties.

Unlike state-sponsored courts, private dispute resolution fora can neither induce the parties to appear nor to comply with the resulting decision (Landes and Posner 19xx). For private methods to substitute effectively for resolution by the courts, the parties must have some incentive to submit their dispute and to be bound by the outcome.

In the commercial world, maintaining a good reputation often supplies that incentive. The importance of reputation helps to explain why many bargains are kept despite the inability of courts to enforce them. It is clearest in firm-to-firm transactions, where, as in the construction industry, a small, close-knit group of companies interact on a regular basis. It is also evident in the efforts of private agencies to provide data on consumers' repayment history. Where consumers know that the failure to meet an obligation to one merchant may result in the denial of credit by all merchants, the incentive to avoid default is considerably stronger. The importance of credit bureaus and other devices for sharing information is beginning to be recognized. For instance, recent research has shown its significance for deepening credit markets (World Bank 2003: 101-103).²³

²³ In a related argument, Goodpaster (2003) contends that social capital and trust-based relationships can serve as a robust alternative to the courts in the enforcement of contracts. His analysis is very much consistent with the empirical findings of Wei (1996) on kinship networks in China. Wei finds that the emergence of informal kinship networks helps to explain the huge inflows of capital into China, despite foreign investors' perception of high levels of corruption.

Addressing contract enforcement problems through information and reputation is a relatively apolitical approach to improving the rule of law. But, while important, it can only be part of the solution to the problems of credible commitment that are inherent in contracting among private parties. The question that then arises is what else a country can do to make investment environment more predictable, while waiting for the courts-based rule of law to emerge. Goodpaster (2003) argues that relationships of genuine trust, based on kinship relations, can potentially provide reasonably effective alternatives that build on political realities. The critical ingredient, he contends, is that whoever gives the assurance of contract fulfillment can indeed guarantee that the implicit trust will not be abused or that any abuse will be effectively remedied. Campos et al. (2001), who analyze and describe examples of alternative credible commitment mechanisms, from Indonesia under Suharto to present-day China, provide some evidence in support of this thesis.

Reforms of and within the legislature deserve greater attention from donors

While reforms to the legal and judicial system, as well as corresponding technical assistance, expanded during the 1990s, there was much less activity on legislative reforms (Manning and Stapenhurst 2002). The reasons included donors' lack of experience with such reforms, the more political and controversial nature of such reforms, and the nascent state of many legislatures (Lippman and Emmert 1997). Nevertheless, the spread of democracy created the space for legislatures to evolve into independent political institutions that could oversee the executive and, with or without foreign assistance, legislatures have ventured slowly to build their oversight capacity.

In most countries, the legislature is the constitutionally mandated institution through which governments, with the executive as head, are held to account by the electorate. In doing so, the legislature can use several means, including approval of budgets, the questioning of senior government officials, the review and confirmation of executive appointments, impeachment and/or the power to dismiss the government, the establishment of parliamentary committees, and the formation of commissions of inquiry.

A fundamental role of the legislature in most countries is to scrutinize and authorize revenues and expenditures and to ensure that the national budget is properly implemented. Yet while legislatures around the world have the constitutional power to consider national budgets and authorize governments to raise revenues and carry out expenditures, their actual exercise of this power has varied widely.

Industrialized countries have seen a long-term decline in the influence of national legislatures on budget policy, as the result of the devolution of spending (and, to a lesser extent, revenues) to state and local governments and of the expansion of both entitlement spending and national debt service (Schick 2002). This budgetary decline is perhaps most evident in Britain, where Parliament has long ceased to influence budget measures proposed by the executive (Davey 2000).²⁴

²⁴ Late in the 1990s, a number of legislatures responded to this weakened position with a burst of budget activism. A recent OECD study (1998) found that more than half of the legislatures were playing a larger role in

In developing and transition countries, by contrast, the 1990s saw a trend towards legislative budget activism, reflecting the process of democratization and the opening up of possibilities for legislative involvement in what were previously closed budgetary systems. In Brazil, for example, where Congress had historically played no significant role in the budget process, constitutional changes have given Congress powers to modify the budget (Blöndal, Goretti, and Kristensen 2003). In Africa, too, changes are occurring. For example, South Africa and Uganda have passed financial administration or budget acts that give more influence to the legislature during the budget formulation and approval processes.

But the experience to date suggests that developing country legislatures have a long way to go before they can adequately perform their oversight functions, especially over national budgets. Building oversight capacity involves, *inter alia*, strengthening the “money committees”, establishing dedicated research staff, enhancing complementary institutions such as national audit offices, and encouraging public input at the various stages of the budget cycle. Through the 1990s numerous organizations, including bilateral donors, multinational organizations, and international financial institutions, supported efforts to enhance the oversight capacity of legislatures. Their assistance ranged from supplying office and other equipment to helping establish legislative budget offices and strengthening committees. The assistance had mixed results.

Indeed, in the area of democracy assistance, it is support to the legislatures that most often falls short of its goals, and legislative strengthening efforts should be seen as complements to related improvements in governance (Carothers (1999). “Treating legislatures as self-contained entities that can be fixed by repairing internal mechanisms is unlikely to get very far. Rather,...it is more useful to think in terms of helping a society develop the capacity to enact laws that incorporate citizens’ interests...[this means] working with many people and groups outside the legislature, including political parties, citizens’ groups, the media, officials from the executive branch, jurists, and others (Carothers 1999:98).” In the case of money committees, this means dovetailing reform activities with broader efforts to enhance government accountability and strengthen public financial oversight, and ensuring that training activities include participants from other stakeholder organizations, such as the ministry of finance, the auditor general’s office, and representatives from civil society.

Strengthening the compact

For more than two decades now, public sector reforms have focused heavily on improving the so-called compact between politicians as policymakers and civil servants as implementers of policy and service delivery. Indeed, the now well documented and extensively studied reforms in Australia, New Zealand, and the United Kingdom that graced the reform landscape in the 1980s almost exclusively dealt with this compact. The large-scale, big bang privatizations and radical changes in financial management in New Zealand, the forward looking budget reforms in Australia, and the proliferation of Next Steps agencies in the UK

budget development than they were ten years earlier, suggesting that they had maintained their oversight role and simply shifted emphasis.

all aimed at altering the fundamental relations between politicians/policymakers and bureaucrats in order to improve the delivery of public goods and services.

With the fiscal crunch arising from the debt crisis of the 1980s, a similar trend occurred in the developing world in the 1990s. Efforts to prune and rationalize the role of the state led to privatization of state-owned enterprises. Similarly, budget and financial management reforms were initiated and even the more challenging and controversial new public management reforms of the UK and New Zealand variety were initiated in a great number of developing countries.²⁵

These reforms had essentially two thrusts. The first was to build the capacity of the public sector—personnel skills, systems, and processes—to formulate and implement policies. The second, whose emphasis increased during the decade, was to infuse clearer and more binding accountabilities of civil servants to policymakers and politicians. Underpinning both these trends was the move towards greater democratization of politics, which sought to strengthen political accountability and as a consequence the compact. This often took the form of a major decentralization of financial and functional authority to local governments, with a view to bringing governments closer to the people.

What follows is an attempt to cull some preliminary conclusions from the experience of the 1990s. These conclusions must by their very nature be tentative and subject to revision as we learn more about what drives public sector governance reforms. First it should be cautioned that given the slow pace at which institutions change, and the fact that most of these reform efforts are rather recent, it is much too early to reach definitive conclusions about successes or failures. Second, very little systematic research has evaluated results and outcomes, partly because of the stop-go nature of many reforms, and even when reforms appear to be successful it is often too early to judge whether the success is sustainable. Third, since reforms imply changes in formal and informal rules, both of which are deeply rooted in a country or organization's culture and history, it is also not obvious whether successful reform efforts in one organization can be transplanted into another organization in the same country, let alone across national borders.

What then are the promising lessons?

Fiscal management

Governments faced with populist pressures can strengthen fiscal discipline by tying their own hands. During the 1990s, governments attempted to improve fiscal discipline in a number of ways.²⁶ The most high-profile efforts granted independence to central banks, as a means to clarify the banks' direct responsibility for controlling inflation and to grant them the

²⁵ There are differing interpretations of the composition of New Public Management reforms. But there is a general agreement that the key components include deregulation of line management, conversion of civil service departments into free-standing agencies,; performance-based accountability, particularly through contracts; and competitive mechanisms such as contracting-out and internal markets. Various authors also include privatization and downsizing as a part of the package (Polidano 1999).

²⁶ Fiscal discipline was critical to maintaining macroeconomic stability, which in turn was essential to stimulate growth (see chapter 3)

flexibility to meet this mandate. But while many countries have adopted this approach, recent research suggests that the central bank's ability to play this role depends heavily on the nature and efficacy of checks and balances in the larger environment (Keefer and Stasavage 2003: 407).

On the public expenditure side, the experience of the 1990s pointed up the importance and impact of fiscal institutions. A number of studies suggested that institutions define and constrain the nature of the political bargaining that affects fiscal outcomes.²⁷ Evidence from empirical studies of fiscal institutions and budgetary outcomes suggests that well defined anti-deficit rules, especially when coupled with credible limits on government borrowing, induce smaller deficits and more rapid adjustment of taxes and spending to unexpected fiscal shortfalls.²⁸ In part, these institutions are meant to contain interest group pressures on the budget.

In recent years, a number of countries and sub-national governments in developing countries, including Brazil, have passed fiscal responsibility acts to strengthen fiscal management. These laws require the executive to present to the legislature, prior to presenting the proposed budget, the policies and parameters that it intends to adopt to bind government over the medium term, and to explain to the legislature ex post any deviations from the budget during the fiscal year. The laws enhance transparency as well as accountability (of the executive to the legislature and of both the executive and the legislature to the citizenry), by stimulating discussion both within the legislature and the public/media of fiscal policies and their implications before and after budget deliberations. Though no studies have yet assessed their effects, the expectation is that the new laws will strengthen fiscal discipline.

Hidden contingent liabilities destroy the fabric of fiscal discipline. The Asian financial crisis highlighted the importance of budget transparency: the budget should not only reflect the actual expenditures to be made during the fiscal year but also include the budgetary implications of all fiscal risks—including contingent liabilities arising from loans made by state-owned banks that could become real liabilities in the medium term. Greater budget transparency matters, since it provides a basis for informed debate about budgetary policy among the public and the legislature, and within the executive. By increasing the chances that fiscal risks will be identified and policy responses put in place, fiscal transparency was seen to be essential to maintaining fiscal discipline. But again, progress has been slow partly because of capacity constraints and partly because of political considerations Box 9.3.

²⁷ See Poterba (1996) for a review of the literature circa 1996.

²⁸ Alesina and Perotti (1996) discuss institutions in terms of the degree of centralization of authority in the budget process and the degree of transparency. Von Hagen (1992) provides summary information on the budget process in European Community nations. Von Hagen and Harden (1995) suggest that tighter budget rules are associated with smaller budget deficits and lower levels of government borrowing

Box 9.3: Fiscal transparency and developing countries

The **fiscal transparency code** was introduced in 1998 as a response to the financial crises of the late 1990s when potential vulnerability was seen to have been hidden by the lack of relevant fiscal information. The fiscal Report on the Observance of Standards and Codes (ROSC), which is a **voluntary diagnostic**, assesses the availability and quality of fiscal data but goes further to also evaluate the fiscal management framework, including relations between levels of government, and accountability for fiscal activities outside the budget.*

The fiscal ROSC applies a uniform approach to countries, assessing systems relative to “good” practice while avoiding a pass/fail judgment. As of end-2003, ROSCs had been completed in 63 countries; 58 of these reports are posted on the IMF website. Countries in which the fiscal ROSC has been undertaken include industrial economies, emerging market economies, transition economies, and developing economies. Application of the fiscal ROSC has met with some challenges in ensuring even-handed treatment of countries at different levels of development and revisions to the guidelines have sought to address these differences appropriately.

Countries electing to have a fiscal ROSC reflect an element of reform self-selection, and are often already engaged in fiscal management reforms. Nevertheless, in developing economies, the fiscal ROSCs have identified pervasive problems of data quality (unreconciled accounts, lack of clarity in accounting policies, weak external audit), excessive discretion in tax administration and poor enforcement, unrealistic budgeting, weak internal controls, significant payment arrears, and lack of clarity in defining responsibilities of various levels of government. In a number of developing economies, the scope and extent of off-budget activities (including quasi-fiscal activities) is an issue to be addressed. Other than a few industrial countries, most countries also do not quantify tax expenditures.

* For a more extensive discussion of assessment instruments in the area of public financial management, see Allen, Schiavo-Campo, and Garrity (2004).

Source: “Assessing and Promoting Fiscal Transparency: A Report on Progress”, March 5, 2003. Fiscal Affairs Department, International Monetary Fund.

A medium-term expenditure framework (MTEF), while technically attractive, will work only if politicians embrace it. MTEFs gained currency as an important reform during the 1990s, with many countries adopting them as a way to increase the transparency of budgeting and enhance the predictability of agency budgets. The primary function of an MTEF is to infuse a multi-year perspective into budgeting, enabling policymakers to recognize the implications of current budgetary decisions for future government finances and creating a more disciplined, sequenced budget process that clarifies the deliverables and accountabilities of both central and line ministries.²⁹

²⁹ An MTEF has seven key features: (1) a top-down process for establishing hard budget constraints at the aggregate and sectoral level, (2) a bottom-up process in which line ministries prepare forward estimates of expenditures over a three or four year period, (3) a system for reconciling the forward estimates and the hard budget constraints, which includes processes for making intersectoral reallocations, (4) a transparent system for incorporating changes to the forward estimates during rollovers to the following year, and (5) a tractable system for undertaking program evaluation. World Bank (1998), *Public Expenditure Management Handbook*.

Few of the OECD countries have adopted the full plethora of features of MTEFs, whether by choice or by circumstance.³⁰ Their adoption of multi-year features evolved gradually, usually as technical improvements to the budget process rather than big-bang reforms. Unbundling the key features of an MTEF, and pursuing them individually, appears to be a more effective approach than wholesale adoption of the full gamut of features. OECD countries' experience suggests that an MTEF may be better used as a conceptual framework for thinking how elements of budget reform fit together, rather than as a reform in and of itself. Yet, in developing countries, the MTEF has been introduced—largely through donor initiatives—as a process technically superior to annual budgeting.

In Africa, the MTEF has not produced the results expected of it. Implementation has been slow. Of the 19 countries with MTEFs³¹ at some stage of implementation, as of 2002, only five had integrated MTEFs in a meaningful way into their budget processes. In most cases, MTEFs have operated in parallel to the general budget process (Le Houerou and Taliercio [date]). Only four countries submitted MTEFs to both cabinet and parliament and, in some cases, the MTEF has remained strictly a technical document of the ministry of finance.³² An MTEF's value comes from the multi-year information that it can generate and from the ensuing discussion, debate, and agreement among different parties engaged in the budget process—in particular the legislature—about the tradeoffs that need to be made among programs, activities, and projects. Hence, for an MTEF to be effective, it needs to be integrated into the budget process and budget documents. Quite clearly, just like the budget, an MTEF is fundamentally political. So its effectiveness depends in large part on the willingness of politicians to embrace it as a reformed budget process and to accept the discipline it brings. Hence, not surprisingly, progress in many developing countries has been slow.

Organizational and human resource management

Capacity constraints are binding: Strategic incrementalism may be the only option for many developing countries. *World Development Report 1997* argued that the state should match its role to its capacity, since taking on too much makes the state less effective. This was certainly evident from the various reforms that were pursued in public expenditure management. But it is perhaps most salient in the attempts of many developing countries to adopt New Public Management (NPM) approaches.

NPM reforms proliferated in the 1990s, with organizations set up at arms length from the parent ministry and having a contractual arrangement with it, and a budding love affair with

³⁰ More than 70 percent have multi-year expenditure estimates incorporated into their budgets and 67 percent have a medium-term fiscal framework with ceilings for expenditures, deficits, and revenues over multiple years as part of their budget (see World Bank/OECD Survey on Budget Practices and Procedures 2003). Available at: <http://ecde.dyndns.org>. As of December 2003, 27 (of 30 total) OECD and 17 developing countries are included in the database.

³¹ Benin, Burkina Faso, Chad, Ethiopia, Gabon, Gambia, Ghana, Guinea, Kenya, Lesotho, Malawi, Mali, Mozambique, Namibia, Rwanda, South Africa, Tanzania, Uganda and Zambia.

³² Le Houerou and Taliercio. "Medium-term Expenditure Frameworks: From Concept to Practice. Preliminary Lessons from Africa", p.13.

performance measurement. Privatization of state-owned enterprises has been a key element of NPM.³³

New Public Management reforms are a challenge even in countries that have strong capacity. These reforms basically put the cart before the horse. Manning and Parison (2003) argue that they are difficult to implement even in developed countries, and nearly impossible in countries that lack institutionalized “organizational discipline”—that is, whose basic civil service management systems do not function as intended. In environments where the basics are very weak, resort to NPM-style performance management techniques is associated with poorer performance, as measured by increases in administrative corruption (Anderson, Reid, and Ryterman 2003).³⁴ These authors found that the most fundamental and significant factor contributing to better performing public organizations is the creation of merit-based personnel management practices: putting in place recruitment and selection systems, performance evaluation procedures, promotion procedures, salary setting rules and procedures, wage bill controls, and due process protections, and ensuring they function as planned.³⁵ The implication is that these core systems and practices are preconditions for effective performance management practices.

Performance-based budgeting emerged as a corollary reform of NPM, primarily from the experiences of the UK and New Zealand in dealing with their respective fiscal problems. Over the past 20 years, OECD countries have gradually shifted the focus of public sector budgeting and management from inputs to outputs, in an attempt to clarify (both within government and externally to the general public), *what* agencies should be providing. Arguably this development has enhanced public sector management and increased the government’s effectiveness and efficiency.³⁶ But, like the multi-year expenditure framework, it has taken many years to mature. And the experience has debunked the earlier belief that performance measurement can often be an effective catalyst for organizational change.³⁷ An important lesson for developing countries is the fact that OECD countries already had very well functioning basic personnel management systems, many in the Weberian tradition, before launching into performance management and budgeting.

³³ Typically, state-run commercially viable entities are spun out of the state sector and into the private sector as part of an overall program of trimming the state. See chapter 5.

³⁴ A point that Schick (1998) makes more generally.

³⁵ Their finding is very much consistent with earlier related work by Evans and Rausch (1997), and with research at the sector level. Gunnarsson et al. (2004) find strong evidence indicating that the granting of autonomy to local district school principals (akin to delegation under NPM) improves student performance only if the principal and the school staff have adequate capacity to take advantage of the increased autonomy.

³⁶ For a discussion of the limitations of outcome-oriented management and budgeting see OECD (2001).

³⁷ Schick (2003). Schick cites the Britain’s Next Steps initiative in which government established new agencies by separating service delivery from the policymaking functions of ministries. Then it set performance targets. More than 100 agencies were created, and each was given operating independence and a charter (called a framework document) that spelled out its responsibilities and the manner in which it is to be held accountable. Each agency negotiates annual performance targets with the parent ministry to which it is responsible, and each compares results to these targets. The Next Steps reforms are generally regarded as among the most effective innovations in British public management. Although the Conservative Party initiated them, the Labour Party continued and deepened them when it came to power in 1997.

Capacity constraints and political imperatives can severely impede civil service reform
In many developing countries, establishing basic (core) systems requires overhauling the civil service. This poses two major problems. First, opposition will be much more widespread and thus more politically challenging to address. And second, managing this “whole of government” process severely taxes the limited capacity of many developing country governments.

The impact of politics is especially acute in the context of civil service reforms. A key part of the difficulty is that such efforts must inevitably transfer some authority from the political echelons—legislators, ministers, and their political appointees—to a cadre of de-politicized officials—civil servants.³⁸ In many developing countries, the political history and environment make this a gargantuan task.

A malfunctioning civil service system creates disillusionment among the populace since public services will tend to suffer. One would thus expect politicians to be interested in improving the internal incentive mechanisms that govern the civil service. A de-politicized, reasonably well compensated, and skilled civil service can in fact serve as a credible commitment mechanism to foster better service.³⁹ Politicians could thus promise better primary health care or greater access to, and better quality of, primary education and be credible to the citizenry. However, many developing countries attempted reforms under conditions where clientelist politics of one form or another were already deeply entrenched. Hence the reforms met formidable opposition and, not surprisingly, their results have been quite discouraging.⁴⁰

With appropriate design and sufficient political commitment, “enclaving” can potentially be a path to sustained reforms of the civil service. The challenges of politics and capacity constraints have led some countries to experiment with enclave approaches to civil service reform—spinning off selected government entities from central government ministries—essentially as a means to match capacity with the demands of managing the political process. Among the more visible of these reforms was the thrust towards increasing the autonomy of

³⁸ See Stevens and Teggemann (2003) and Manning and Parison (2003). For a case study on reversibility, see World Bank on Albania CSR (need exact reference).

³⁹ See Shepherd (2003) for a discussion of this point.

⁴⁰ See for instance, World Bank (2000) (Institutional Governance Review: Bolivia), and a World Bank study on experience with civil service reforms in Africa. The latter concludes, “For each of the reform areas considered, there exists a well-understood set of mechanisms which have the potential to align the administrative system to support developmental goals. Each of the chapters takes these normative ‘best practices’ as the starting point, and examines the degree to which they have been realized in practice. In all but a few cases, the results so far have fallen far short of the normative model. For example, comprehensive efforts at administrative reform achieved some success only in 3 of 7 sample countries where they were attempted and have achieved little in the remaining four countries where political constraints short-circuited ambitious programs. What plausibly underlies this implementation shortfall is the ‘politicians dilemma’ . . . the need to balance the technocratic logic which shapes many proposals for reform with the political imperatives of building and sustaining alliances with powerful patrons, of avoiding conflict with powerful social groups, and of maintaining electoral support. Depending on the severity of the political constraints, even well-intentioned leaders are thus limited in how ambitious a reform agenda they can take on. A key lesson is that it can be counterproductive to ignore these constraints, and bulldoze along with an agenda (Levy and Kpundeh 2004: 12, 16).”

revenue collection agencies, which was driven in large part by declining tax to GDP ratios. This became a key feature of governance reforms in Latin America in the early 1990s, starting with Peru in 1991, followed by Venezuela, Mexico, Bolivia, Guatemala, Argentina, and Colombia. Such reforms became popular in Africa in the late 1990s, with 12 countries experimenting with revenue boards or semi-autonomous agencies. In Asia, by contrast, only Malaysia and Singapore have given greater autonomy to their tax administrations, although other countries in the region are beginning to consider this.⁴¹

In general, an autonomous revenue agency has more flexibility in managing personnel and finances and more control over corporate governance than does the typical government agency. At the same time, it also has clearer and more transparent accountabilities. The overall implication of introducing such agencies was that collections would increase and service would be more taxpayer friendly. A properly functioning autonomous revenue agency signals to taxpayers that tax policies and regulations will be credibly and fairly enforced, that firms that comply faithfully with the rules will not be at a competitive disadvantage, that everyone will pay his fair share of financing public goods and services, and that the transactions costs of paying taxes will be reduced.

In practice, the performance record of these agencies has been mixed. Some countries have improved performance dramatically across a number of indicators, while others have had difficulty attaining the expected results or sustaining initial progress.⁴² Problems in performance have resulted primarily from the lack of political support, tensions between the autonomous revenue agency and the ministry of finance, and poor organizational design, including weaknesses in the new accountability regime. Nonetheless, on the whole the record suggests that, with enough political push and proper design, these agencies can improve tax administration and be sustainable (Box 9.4).⁴³

⁴¹ The establishment of large taxpayers' units (LTUs) was a related reform that many countries explored to improve the tax compliance of the largest taxpayers and to pilot new organizational structures, systems, and procedures. More than 40 developing and transition countries have set up special large taxpayer units. The reforms were first implemented in Latin America, followed by a number of African countries and transition economies. Only five Asian countries (Bangladesh, Cambodia, Lao PDR, Philippines, and Sri Lanka) have developed special large taxpayer structures so far. The percentage of total taxes revenue collected by LTUs ranges from 28 percent in Sri Lanka to more than 80 percent in Benin, Burkina Faso, Togo, Mexico, and Uruguay.

⁴² For a particularly strong critique, see Fjelstad (2002); and for a more general country survey and balanced assessment, see Taliencio (2003).

⁴³ The same political support might perhaps have achieved the same results without the move to an autonomous revenue agency, but in some instances introducing such an agency has energized and crystallized support for more wide ranging administrative and civil service reform.

Box 9.4: SUNAT in Peru: A modest success

In the late 1980s, Peru decided to set up a semi-autonomous revenue authority (SUNAT), as tax administration was riddled with corruption and on the verge of collapse, with revenue collections dropping to a record low of 9 percent of GDP in 1988. A comprehensive staff screening and replacement program was initiated, and less than one third of the original tax administration staff was rehired by the new organization. A modern human resource management system was introduced and SUNAT was allowed to operate under private sector labor laws. Salaries were adjusted to private sector levels. A new financing mechanism provided financial stability and the agency was able to operate without undue political interference. By 1997 tax revenues had recovered to 14 percent of GDP.

After its successful start, however, SUNAT, suffered from decreasing political support for efficient revenue collection; a decline in the quality of the tax policy framework, which made fair and efficient tax collection more difficult; and increased interference by the Ministry of Finance. As a consequence, SUNAT has suffered a loss of standing in public opinion. Despite these problems, however, its creation has permitted the launch of far-reaching efficiency and integrity-enhancing reforms, which are having an ongoing impact. Revenue collection, at 12 percent of GDP in 2001, remains far above the pre-reform level.

Given the immense difficulty of overhauling the whole of government, for many developing countries enclaving reforms may be the only game in town. The important lesson is that enclaving must be strategic if it is not to constrain and/or distort the capacity building efforts of government (Box 9.5).⁴⁴ Part of the reason why autonomous revenue agencies have been modestly successful in some countries is that revenue collections dictate the budget envelopes in most developing countries, so that much of what government does depends heavily on the performance of its tax collection agencies.⁴⁵ Moreover, since many of these countries faced serious budgetary problems, reforming the tax administration apparatus was seen to be strategically important because the control of the budget deficit and thus the performance of government as a whole depended crucially on it.

⁴⁴ At the sector level, see Harding (2003) for an extensive comparative review and analysis of different approaches to health care provision: direct provision by the public sector, through non-profit providers, through for profit providers, and through informal providers. The lessons suggest possibilities for focused strategic interventions in the health sector.

⁴⁵ Taliercio (2003).

Box 9.5: The enclave conundrum in Uganda

The Government in Uganda now has to decide the fate of more than 70 enclave units, most of which are outgrown project implementation units and semi-autonomous organizations called secretariats. These were set up at the behest, or with support, of donors who doubted line ministries' capacity and were dissatisfied with ministries' procurement practices. The enclave units were allowed to set their own wage rates, above ministry levels, based on the premise that the necessary skills would not be available at the public service's low salary levels.

Ironically, with these higher salaries, the enclaved units have recruited substantial numbers of skilled personnel from within the public service and have drawn staff away from their parent ministries, further depleting the capacity of ministries and demoralizing competent ministry staff.

Enclaving has also undermined the budget process. First, although accounted in the budget under development expenditures, two-thirds (71 percent) of the enclave units' expenditure is of a recurrent nature. These recurrent expenditures come from the government's 10 percent contribution to donor funded projects. While this may seem a nominal proportion of any project's total budget, the total constitutes nearly one-third (28 percent) of government's own generated funds. This significant part of government's own generated resources is spent without the rigor that is associated with allocating other government expenditures.

Source: Draft report, "Affording Uganda's Public Administration Sector" (December 2003), World Bank. The report is currently being reviewed by the Government of Uganda.

A study by Levy and Engberg-Pedersen (2004) on African experience suggests that narrowly focused, strategic interventions may indeed be more successful than broader reforms over the long run. The authors also find that, among the more narrowly-focused reforms, the capacity building initiatives that focused on improving expenditure accountability were considerably more successful than those that focused on human resource management.⁴⁶ They conclude that the more technical nature of expenditure accountability reforms may have been less threatening to vested interests than the more politically sensitive administrative reforms, and, perhaps more importantly, that these reforms produce more readily observable results that generate needed support from the general public (to counter vested interests).

Values, commitment, and pride in public service matter as much as controls and compliance. Judith Tandler argues, with some merit, that mainstream development advice has paid little attention to worker commitment "except to argue that government workers are doomed by their self-interest to be uncommitted" (Tandler 1997:136). The New Public Management reforms were in fact based partly on this premise and thus driven by a desire to introduce stronger market-based incentives as a means of reforming government bureaucracies. Emulating the experiences in developed countries such as New Zealand and the UK, developing country governments attempted to adopt performance management techniques that grew out of reforms in the private corporate sector. These reforms aim at enhancing the autonomy of public sector managers and staff while at the same time increasing their

⁴⁶ Evaluations by the World Bank's Operations Evaluation Department (OED) found that eight of the nine expenditure accountability projects were successful, but only two of the eight projects on human resource management were successful.

accountability. But while they have arguably led to improved service and performance in developed countries, they have had little success in developing countries.

Tendler contends that industrial countries' experience with industrial performance and workplace transformation has shown that workers' dedication to the job is an important explanation for improvements in performance. Recognition of this has caused firms that perform well to pay close attention to innovative practices that increase worker dedication. "Almost all these innovations involve greater worker discretion and autonomy, greater cooperation between labor and management, and greater trust between workers and managers" (Tendler 1997:4-5). She contrasts this with the development literature, which has been "riveted by the absence of worker commitment" and the suspicion that "civil servants are self-interested, rent-seeking, and venal, unless proven otherwise".⁴⁷ Tendler cites as evidence the preoccupation with downsizing in civil service reforms without corresponding efforts to reorganize work "in ways that increase worker commitment". Her own research on public bureaucracies at work under an innovative state government in Ceará, Brazil shows how important to successful outcomes is the infusion of a sense of calling and dedication (Box 9.6).

Box 9.6: Building a sense of calling and commitment in public service delivery: Ceará, Brazil

High performance and significant developmental impact in various programs in Ceará, Brazil, has provided a new interpretation for factors motivating the state, civil society, and civil service. Ceará saw substantial improvements in preventive health indicators such as infant mortality and vaccination coverage. Agriculture programs saw a significant measurable increase in output and productivity. Spillover effects from procurement reform programs resulted in local economic development, in addition to increasing output and productivity for small-firm suppliers. Public works construction created more jobs in the economy than usual, resulting in a greater share of public expenditure being allocated to labor.

Four closely intertwined explanations can be offered for this improved performance:

- First, civil servants in these programs showed high dedication to their jobs. Either they were dedicated entrants into civil service, and work conditions perpetuated that dedication, or the circumstances of the jobs elicited their commitment.
- Second, the government repeatedly and publicly demonstrated admiration and respect for the civil servants by regularly announcing successes and openly rewarding good performance, building a sense of calling and pride around the workers and creating a sense of chosen elite in the public service. Publicity also increased citizen awareness and public monitoring of civil servants and local governments, and created a new constituency that would help leaders and agencies overcome political opposition.
- Third, innovative organization of tasks for workers in the public programs resulted in often voluntary ownership of varied and multiple tasks. These multiple tasks often coalesced into client-centric, problem-solving approaches to service delivery.
- Finally, repeated messages from the government and reorganization of tasks kept rent-seeking behavior under control by creating a sense of pride, ownership, and recognition around public service, in the eyes of society and civil servants alike.

⁴⁷ At its core, this is the basic assumption of the principal-agent model. NPM reforms have been driven by principal-agent concerns.

This case challenges the mainstream developmental belief that poor performance of public programs is due to the inherent self-interest of civil servants. It demonstrates that the creation of a sense of calling and ownership around public service by a committed leadership, a dedicated work force, and an informed and engaged civil society can increase acceptance of reform and improve service delivery.

Source: Tandler (1997): 135-165.

The effectiveness of information and communications technologies (ICT) depends on the reengineering of underlying processes and the proactive use of change management.

In a quest to improve the delivery of frontline services, many countries began adopting ICT in such varied areas as tax collection, customs valuation, procurement, treasury and cash management, issuance of licenses, land registration and titling, passport issuance, and many other focused frontline public services. This 1990s trend, which has come to be known as “e-government,” involved significant experimentation with the application of ICT to various internal processes to increase transparency and efficiency.

e-Government applications have normally evolved through a four-stage process. The first stage includes the publication of information on a website for citizens to seek knowledge about procedures governing the delivery of different services; the second stage is interactivity online, allowing clients to download applications for receiving services; the third stage involves electronic delivery of documents; and the fourth results in electronic delivery of services, where more than one department may be involved in processing a service request or service.

Box 9.7: Mexico’s e-SAT Program—striving for greater efficiency in tax administration

Inspired by the early successes of Argentina, Brazil, and Chile in using ICT to improve the delivery of government services, the Mexican government (as part of its OECD-based program of regulatory and administrative reform), began moving government information and services online. Within this framework, Mexico’s federal tax administration (Servicio de Administración Tributaria, or SAT) embarked on e-SAT, a program to offer tax services online. Starting in 1995, e-SAT has evolved gradually. By 1998, SAT had established an interactive web page that (1) contained basic information pertaining to Mexico’s tax laws and procedures and (2) permitted obligated taxpayers to file their annual declarations electronically. The primary beneficiaries of the first phase of this new system were the large corporations. In 2000-03, SAT expanded the nucleus of online tax services to allow taxpayers to: (1) obtain a personal form of electronic identification, (2) obtain a corporate tax ID for new entities via the Internet, (3) submit a tax declaration and other relevant forms, 4) enquire into the status of a taxpayer account, and (5) schedule an appointment with a SAT tax counselor. In August 2002, the SAT promulgated a new regulation requiring the electronic submission of most individual and corporate taxpayer declarations (through SAT’s portal) and payments (through the portal of the taxpayer’s bank). SAT is now working to develop and make operational online systems for the receipt and processing of credit card payments and the realization of tax refunds. e-SAT has greatly reduced the amount of paperwork previously managed by Mexico’s tax registry, declaration, and collection units.

Source: Roberto M. Kossick (2003), “Modernizing Mexico’s Tax Administration: The Development & Implementation Of The e-Sat.” Case study written for the World Bank e-Government Thematic Group.

e-Government has been a powerful tool for enhancing the efficiency and effectiveness of public services.⁴⁸ Table 9.1 shows some examples.

Table 9.1: Examples of efficiency gains from ICT

Country	Type of government application	Number of days to process before application	Number of days to process after application
Brazil	Registration of 29 documents	Several days	20-30 minutes per document, one day for business licenses
Chile	Taxes online	25 days	12 hours
China	Online application for 32 business services	2-3 months for business license Several visits to multiple offices for filings	10-15 days for business license Several seconds for routine filing for companies
India, Andhra Pradesh	Valuation of Property	Few days	10 minutes
India, Andhra Pradesh	Land Registration	7-15 days	5 minutes
India, Karnataka	Updating Land Registration	1-2 years	30 days for approval, request completed on demand
India, Karnataka	Obtaining Land Title Certificate	3-30 days	5-30 minutes
India, Gujarat	Interstate Check Posts for Trucks	30 minutes	2 minutes
India, Andhra Pradesh	Statutory Certificates on caste	20-30 days	15 minutes
Jamaica	Customs Online	2-3 day for brokers to process entry	3-4 hours
Philippines	Customs Online	8 days to release cargo	4 hours – 2 days to release cargo
Singapore	Issue of Tax Assessments	12-18 months	3-5 months

Source: Bhatnagar, Subash, and Arsala Deane (2003).

Experience suggests, nonetheless, that e-government is not a panacea for basic problems. First, for real gains to be made, processes need to be simplified and automated in ways that reduce the discretion of government officials.⁴⁹ For example, to facilitate import and export procedures Tunisia has implemented Tunisie TradeNet (TTN), an electronic system connecting all actors involved in external trade operations. The new system has involved reengineering the trade-related processes of nine public and private entities. While this has led to some delay in realizing some expected efficiencies and cost savings, TTN has

⁴⁸ It can also enhance transparency. For instance, the use of electronic bulletin boards in government procurement has made information on government contracts much more widely available. Bhatnagar and Deane (2003).

⁴⁹ A study on the effectiveness of efforts to introduce computerized integrated financial management systems in Africa concludes that “technology can only add value in the context of an underlying commitment to disciplined decision making, and internal management systems geared to monitoring compliance.” Dorotinsky and Floyd (2004).

benefited users, reducing the average time needed to perform import operations from ten days to two or three days.⁵⁰

Second, most e-government projects have faced substantial resistance from public servants tend to see such projects as a threat to their jobs. Publication and easier access to information dilutes their control and diminishes their responsibility as information brokers. Hence, reform projects can stall unless adequate change management processes are adopted.⁵¹

Third, political support from top leadership is critical. Such support has facilitated buy-in from other government departments and has helped “sell” such projects to a larger internal audience and to the general public. In Andhra Pradesh, India, for example, top leadership publicly pushed for e-government and allocated resources accordingly for an ambitious program. Several services are now delivered online and the state secretariat is moving to a paperless office and electronic workflow. In Korea, the success of the OPEN project has been largely due to the support of the Mayor of Seoul, who took a multi-pronged approach (including setting up online tracking of permit and license applications) to curb corruption.⁵² In Gujarat, with strong support from the leadership, computerized check-posts trebled the fines collected from overloaded trucks. But when this support waned, the verve to reduce corruption weakened, with new forms of extortion hampering the overall effectiveness of the program.

External restraints

To combat corruption, prevention may be more effective than investigation and prosecution. Complementing the more prevalent, macro-based judicial reforms were a scattering of efforts throughout the developing world to establish institutions of restraint that focused primarily on enhancing internal accountability. With the spiraling concern over corruption in the public sector, countries began to look to supreme audit agencies, the ombudsman function, and anticorruption agencies to help telescope efforts to curtail corruption. Among these, the establishment of anti-corruption agencies gained most currency, with countries from Latin America to Africa hoping to fast track anti-corruption efforts.

Anti-corruption agencies emerged in the 1990s as a means of introducing independent checks on abuse of office by public officials. The basic logic put forth is that a single agency (as opposed to the more typical multiple agency) approach makes it easier to overcome limitations of coordination, information, and leadership. The widely known successes of Singapore’s CPIB and Hongkong’s ICAC (though quite different in approach) have provided an important stimulus for these efforts.

The few assessments of various single agency reforms have found mixed results. Resource constraints, weaknesses in complementary institutions such as the judiciary and the police,

⁵⁰ Tunisie Trade Net Case Study written by Mustapha Mezghani for the World Bank e-Government Thematic Group. August 2003.

⁵¹ Bhatnagar and Deane (2003) estimate that roughly 40 percent of an e-government project’s cost must be allocated to managing the change process.

⁵² <http://www1.worldbank.org/publicsector/egov/seoulcs.htm>

and multiple goals have tended to impede anti-corruption agencies in meeting their mandates (Meagher 2002). Some anti-corruption agencies have been set up to satisfy a political need—such as an outcry from a corruption scandal or a loan conditionality—but lack enough resources or political backing to actually do their work. They have served to deflect demands for action against corruption while the authorities fail to undertake any real responses (Heilbrun 2002). Box 9.8 outlines the demanding requirements for an effective anti-corruption agency.

Box 9.8: What it takes to create a successful anticorruption agency

A recent study of comparative experience with anti-corruption agencies noted the following factors that drive success of anti-corruption commissions:

- *Establishment*: The success of an anti-corruption agency depends on its being carefully situated from the start within a set of well-defined supports. These would include a comprehensive anti-corruption strategy, careful planning and performance measurement, realistic expectations, and strong enough political backing (across class/party) to make it effective regardless of political and personal consequences. The agencies that seem to score highest on these measures are those in Hong Kong, Singapore, Malaysia, Uganda, and Australia's New South Wales.
- *Focus*: The anti-corruption agency needs to define its focus in a way that will maximize its effectiveness. For example, an agency could focus on prevention and monitoring government implementation of anti-corruption policy (forgoing a comprehensive mandate, as in Korea); its jurisdiction could be mainly prospective (with only limited concern with past cases, as in Hong Kong); it could choose cases selectively, based on clear standards (as in Argentina and NSW); or it could deal only with the probity and reputation of the public service (as in the US and India). Clarity of focus seems to be consistently associated with success, except where massive resources are available.
- *Accountability*: This refers to such factors as the application of legal standards, the availability of judicial review, systems of public complaints and oversight, a requirement that the agency answer to all branches of government and the public, and precise and comprehensive expenditure accountability. Some commentators also suggest keeping the agency's size, as well as the "free" support given by aid donors, to a minimum. Accountability is not uniformly associated with success; indeed frequently stops or delays agencies from taking desired actions. Many of the successful anti-corruption agencies are strongly accountable, but this is probably an outgrowth of the rule of law, which seems to be more consistently associated with success (see below)
- *Independence*: This in some cases arises simply from outside accountability, sometimes from the agency's placement and line of responsibility, the appointment and removal procedures for top officials, or some forms of fiscal autonomy. The most important sign of independence is the absence of political intrusion into the agency's operations. De facto autonomy, on the other hand, enables anti-corruption agencies to operate on a consistent and professional basis with relatively little partisan intrusion. In most environments, this mode of operation is important to success.
- *Powers*: Observers have suggested that a successful anti-corruption agency will have strong research and prevention capabilities, along with the authority to do the following: access documents and witnesses, freeze assets and seize passports, protect informants, monitor income and assets, propose administrative and legislative reforms, and exercise jurisdiction over the chief of state. Many agencies have most or all of these powers on paper but frequently cannot put them into effect due to lack of coordination, weak capacity in cooperating institutions, and political factors.
- *Resources*: Agencies in this field, as in others, depend on well-trained personnel, including sufficient numbers with highly specialized skills. Staff should also be well compensated, subject to integrity reviews and quick removal, and endowed with strong ethic of professionalism, integrity, and

high morale. Also important are sufficient funds, adequate facilities and assets, high-level information sharing, and coordination with other government bodies.

- *Complementary institutions:* The stated criteria here include adequate laws and procedures, basic features of the rule of law including functioning courts, free and active media, an active community of NGOs and public interest groups, and other capable institutions such as supreme audit and central bank. Anti-corruption agencies do not succeed in the absence of the basic features of the rule of law. On the other hand, civic factors such as free media and capable non-governmental watchdogs are not as clearly associated with their success.

Source: Patrick Meagher, “Anti-corruption Agencies: A Review of Experience”. IRIS Center, University of Maryland. August 2, 2002.

Supreme audit agencies are crucial for enforcing the financial accountability of the government, and during the 1990s such agencies were established or restructured in many developing countries. Their effectiveness has been highly variable (Heilbrun 2003). In many countries, the independence of the auditor general is often compromised by an executive that seeks to prevent the opposition from learning of possible cases of illicit enrichment. For instance, in one country, reports from the auditor general are submitted to the president who then makes a determination of when and how to release the information. Unfortunately, all too often, the information is never released.

A major goal of institutions of restraint is to control corruption in the public sector, and efforts to reform these institutions have stemmed in large part from the need to address corruption. This approach however concentrates on cure rather than prevention, and because it requires a considerable degree of coordination among equally difficult complementary reforms, it has rarely worked in developing country contexts, at least not in the short to medium term. As the 1990s ended, it became clear that the gestation period for such reforms would be much longer than had been expected and that, over the medium term, focusing on preventive measures, as opposed to “curative” measures grounded on prosecution, would probably yield better, longer lasting, results.

Anti-corruption efforts pay off when they focus on preventive measures that reduce opportunities for corruption. These include efforts to:

- *Reduce the likely benefits from corruption.* Promoting competition in the private sector, through lowering barriers to entry and reforming regulations where there are natural monopolies, serves to reduce rents and rent seeking. Ensuring competition in procurement through nationwide advertising and efforts to prevent collusion can also greatly reduce corruption. More radical measures include calling for a referendum for the public to approve large projects and the tax and expenditure allocation choices these imply.
- *Reduce the number of transactions that create opportunities for graft,* for example by liberalizing imports, removing price controls, removing industrial and trade licensing requirements, or making such licensing automatic. For example, when India liberalized industrial licenses in the early 1990s, a large industry aimed at obtaining licenses disappeared, along with the corruption associated with it. Similarly, when Indonesia liberalized its trade regime in the 1980s it radically reduced corruption in import licensing. Streamlining bureaucracy, reducing the number of approvals required for particular

transactions, and reducing bureaucratic instructions, simplifying rules, improving service standards, and decentralizing services all have this effect.

- *Increase information, transparency, and public oversight.* Corruption often occurs because of lack of information. Governments lack information on what their agents are doing on the ground. Consumers of government services are not aware of what rules or charges are legitimate. Clarifying rules and increasing transparency helps to reduce opportunities for corruption, as does involving beneficiaries in the oversight of government programs. The World Bank's Kecamatan Development Program in Indonesia is a good example of this.⁵³

Prevention can also be enhanced by establishing time-tested, basic systems of personnel management. Evans and Rausch (1997) show empirically that merit-based recruitment systems and long-term career path arrangements—essential attributes of a Weberian system—significantly reduce bureaucratic corruption. In related work, Von Rijkeghem and Weder (2001) provide evidence supporting the thesis that smaller pay differentials between the public and the private sector lead to lower levels of bureaucratic corruption.

Much current thinking about fighting corruption is influenced by the principal-agent problem. The above approaches assume that the “principal” (the politician or the head of a government agency) is himself not corrupt, and that he has an interest in ensuring that his “agents” are not corrupt. In other words, “it presumes that (the principal) can act with monopoly and discretion to structure the incentives for (the agent), without it then following that (the principal) will act corruptly” (Philip 2003). Indeed, upward accountability to the principal may increase his monopoly and discretion.

This principal-agency model only works when the state is able to pursue the common good of the people in an unfettered manner. But most principals, that is, politicians, even if they themselves are honest, need money to stay in power, fight elections, or buy off opposition. Those who contribute such money can then influence the way power is exercised. If politicians are beholden to special interests or are captured by various interest groups, fighting corruption becomes rather difficult (see discussion below of reform strategies under State Capture).

Decentralization

Despite troublesome measurement difficulties, especially the extent to which local governments have real autonomy in decision making, it is fair to conclude that many developing countries embarked on wide-ranging decentralization efforts in the 1990s (WDR 2000; Litvack, Bird, and Ahmad 1998; Burki, Perry, and Dillinger 1999; Wetzel 2001, Ebel and Yilmaz 2002). Although some of these efforts may have been indirectly stimulated by fiscal crisis, as in Indonesia, they were inspired largely by significant changes in the political landscape: the collapse of long-standing highly centralized regimes and the emergence of strong global pressures for democratization. In many countries, including Thailand, pent-up distaste among the citizenry for tight, unchecked central control and a greater desire for holding political leaders accountable provided the impetus towards decentralizing government functions and services. A growing number of transition countries began

⁵³ World Bank (2003b).

reporting sub-national expenditure data. More generally, among developing countries, the share of sub-national governments in total government spending increased on average by 20 percent from the 1980s to the 1990s.⁵⁴

Decentralization is fundamentally a political choice (rather than a technocratic solution), whose design and implementation may not lead to better service delivery. If it is designed well, decentralization can move decision making closer to the people, enhance the efficiency and responsiveness of service delivery (Faguet 1997; Kahkonen and Lanyi 2000; Bardhan and Mukherjee 2002), support economic growth, and offer a potentially powerful tool for alleviating poverty. But if it is designed inappropriately or introduced without strong local participation and accountability (of local officials to local citizens), it can lead to macroeconomic instability (Prudhomme 1999), declining service levels (Martinez-Vazquez 1998), heightened regional disparities or conflicts (Smoke 2001), and increased corruption (Brueckner (1999).

Absent hard budget constraints, spending by local governments can worsen a country's fiscal situation. Throughout the 1990s, intergovernmental fiscal reforms featured prominently in decentralization efforts. Laws, regulations, and processes were changed to provide a basis for systematically transferring responsibility for delivering services, as well as nationally collected revenues (either through intergovernmental fiscal transfers or devolved revenue sources), to local governments. The experience has varied widely across countries, but one lesson that has emerged is the importance of imposing credible, hard budget constraints on local governments (Rodden et al. 2002). Absent such constraints, local governments might borrow recklessly to fund local initiatives or find other mechanisms to transfer liabilities and potentially expose the national government to unwanted fiscal risks.

Box 9.9: Hard budget constraints: the challenge of fiscal decentralization in Argentina

Argentina's experience highlights the challenges in the design and evolution of a good intergovernmental fiscal system. Provinces in Argentina depend on federal transfers for the bulk of their fiscal resources. Revenue sharing (*coparticipaciones*) was introduced in the 1930s to compensate provinces for the introduction of national income and sales taxes, and in 2000, 56 percent of provincial resources came from this common pool. Roughly 60 percent of the provinces financed less than 30 percent of their spending from own resources (Tommasi 2002).

The challenge of ensuring hard budget constraints under fiscal decentralization depends on the social, cultural, and institutional features of each country. The experience in countries such as Argentina, and Brazil, underscores that a mix of central commitment problems and limitations for effective regulation can conspire to weaken sub-national hard-budget constraints (Rodden et al. 2003). Strong efforts on the part of central government to regulate can deepen problems, for example when sub-national governments circumvent the spirit of regulations through recourse to affiliated state-owned enterprises, including regional banks. Argentina's experience underscores that such problems have no quick fixes. They require the evolution of credible policies—and political will—buttressed by effective institutional arrangements, whether predominantly market based or hierarchical and dependent on central oversight.

⁵⁴ Based on IMF *Government Financial Statistics*.

Sources: Eaton (2003), Perry and Servén, Rodden, Eskeland, and Litvack (2003), Saiegh and Tommasi (1999), Tommasi (2002), Webb (2002)

In many countries, decentralization was seen as a means to bring government closer to the people and thus to improve the delivery of basic services, by shortening the so-called long route of accountability. In principle, decentralized participatory local governments were better informed about the needs of the local poor. Locally elected officials may be held more accountable by local citizens and may be more responsive to the needs of the poor.

But, as the 1990s experience suggests, the allocative benefits of decentralization cannot be achieved without strengthening accountability at the local level. Traditionally, accountability was assumed through political representation (local democratic governance), with some recognition of the importance of local revenue mobilization. But political representation appears to be insufficient, reflecting concerns about capture by elites, and the weaknesses of local political processes (Crook and Manor 1998; Conning and Kevane 2001).

Accountability at the local government level is a multi-faceted phenomenon. Because the ultimate objective of devolved arrangements is to provide the public services needed by local residents in an equitable and technically efficient manner, the most critical concern is the political accountability of locally elected officials to local residents. However, local government accountability also extends vertically from the local government to higher levels of government. Likewise, since the local bureaucracy constitutes the group with the most direct impact on services ultimately obtained by local residents, they too must be considered as part of the mix. Even if local officials are strongly committed to responding to local needs, the intended services may not be forthcoming without appropriate inputs by the bureaucracy (Schroeder 2002; Schleifer and Vishny).

A local government should be just as accountable for funds transferred to it as for funds collected directly from local taxpayers. Likewise, since centrally imposed rules over local government actions are, at least in principle, often made to encourage accountability to local residents, ensuring that those rules are followed should be of concern to the higher level of government. Instruments for ensuring financial accountability are often in place, but their implementation is often poor. Financial audits of local accounts, for example, tend to be delayed for long periods, and as a result, they have not become effective instruments of accountability.

The administrative aspects of decentralization are as important as the fiscal aspects. While a good deal of emphasis has been placed on the financial aspects of decentralization, much less attention has been paid to implementation arrangements, whose details ultimately determine outcomes: (1) redefining the role of central government away from directly providing most services to facilitating and monitoring local service provision, (2) transferring civil servants and assets to local governments, (3) defining an effective structure of local governments, and (4) developing personnel, budgeting, and reporting systems.

The challenges that have emerged fall into three categories: (1) adoption of a more systematic view of decentralization (Bahl 1999), (2) balancing of responsibility with resources, capacity, and accountability, and (3) creating incentives for implementation to

match formal decentralization arrangements. A potential way to address these challenges is to develop a pragmatic strategy for implementing decentralization (Litvack, Ahmad, and Bird 1998; Bahl 2000; Nielson 2001; Bahl and Smoke 2003). While such a strategy would be unique to each country undertaking decentralization, it should include a general vision and framework for reform, mechanisms for coordination and resolving conflicts, a prioritization of reforms and plan for sequencing them, information to monitor outcomes and adjust the reform program, and incentives to change central and local behavior.

Nurturing voice and client power

By the mid-1990s, due in part to the rising trend towards greater democratization, there was a clear recognition of the important role that civil society organizations—such as nongovernmental organizations and religious organizations—could play in inducing better performance from government. While strengthening the compact was key to better performance, reform politicians had to be supported in their efforts and the more traditional politicians had to be cajoled into supporting reforms. In many developing countries, elections opened up the gateway for citizens to hold politicians accountable for the performance of the public sector. By themselves, however, elections have proven to be insufficient and blunt in their impact.⁵⁵

Strengthening voice and building client power can often lead to a more effective compact: service delivery problems are a strong foundation to build on

With elections came an environment better suited for experimentation, particularly at the subnational level. Many innovative (and effective) homegrown experiments with citizen and media advocacy, community monitoring of government performance, or NGO involvement in policymaking and implementation sprouted throughout the developing world as a means of pressuring and/or encouraging both politicians and bureaucrats to improve the delivery of public goods and services.⁵⁶ For example:

- Citizen report card surveys, which originated in Bangalore, India (Box 9.10), have spread to other parts of India and are now being tried in other developing countries including Peru and the Philippines. This instrument has served to coalesce the collective voice of citizens seeking better public services.
- Different forms of participatory budgeting have emerged in parts of the developing world including Brazil and South Africa. At its core, participatory budgeting engages citizens of a community and their elected representatives, such as the mayor or governor, in a partnership to determine the priorities of the community and what projects will be funded from the local budget during the coming fiscal year. Typically, this process has been launched by forward-looking local politicians as a means of locking future politicians into a transparent budget process for which they can be held accountable.
- NGO advocacy for greater transparency and fairness in public procurement and monitoring of procurement processes has become more common as well. So-called integrity

⁵⁵ See chapter 9 on political institutions, for reasons why this is so.

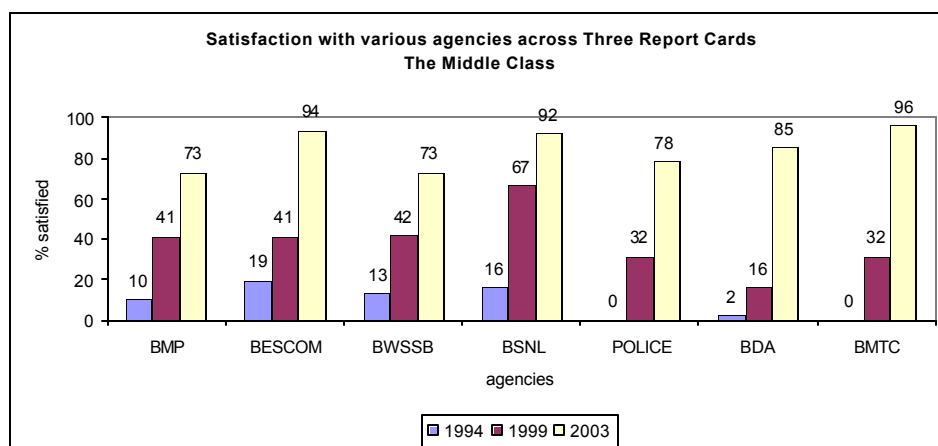
⁵⁶ *World Development Report 2004: Making Services Work for the Poor*, provides many examples and indicates the extensiveness of citizen-based mechanisms for raising the demand for better governance.

pacts developed by Transparency International have now been used in several countries as part of huge procurement contracts, for example in Colombia and Mexico.⁵⁷

A major implication of the above experiments is that active civil society participation in reform can potentially lead to much needed improvements in the compact. The ten-year experience of the Public Affairs Center in Bangalore, India, illustrates the potential of using client surveys as a lever to induce long overdue upstream public management reforms and an improvement in service delivery (Box 9.10).

Box 9.10: The report card survey in Bangalore, India: Stimulating administrative reforms

The Public Affairs Center (PAC), was born in Bangalore, India, in 1994 with the goal of improving the quality of public sector governance in India. Its primary focus and strength lay in assisting citizen groups in “using knowledge as a basis for collective action.”* To undertake this task, it developed the now well known Report Card Survey. In 1994, the PAC conducted its first survey, effectively an opinion poll, of citizens in Bangalore on their perceptions of various aspects of the quality of services provided by eight key government organizations: the City Municipal Corporation, the Electric Authority, the Water and Sanitation Board, Bangalore Development Authority, Telecom, the City Transport company, and the City Police. Citizens were generally dissatisfied with delivery of public services, with some agencies seen to be doing extremely poorly. The results of the survey were published in a leading newspaper, raising their visibility. This led public officials in a number of the agencies to discuss their agencies’ problems with the PAC and citizens’ groups. The PAC offered to help these agencies in addressing some of the problems. In 1999 and again in 2003, the Report Card was once again undertaken to evaluate whether agencies had improved their delivery of services. As the chart below indicates, over ten years, there have indeed been significant improvements in public satisfaction with the service delivery across all eight agencies (similar results obtain for the “poor”). The lesson: demand pressures can lead to needed public sector reforms.



*See Samuel Paul (1995), “Strengthening Public Accountability: New Approaches and Mechanisms”. Public Affairs Center, Bangalore, India.

Source: Samuel Paul, “The Report Card Survey: A Ten Year Retrospective,” seminar presentation, World Bank, November 2003.

⁵⁷ An integrity pact actually embodies a transparent process of procurement which all participating bidders agree to bind themselves to. A civil society organization, e.g. local chapter of TI, monitors the process step by step to assure all bidders that each has kept to the joint commitment.

The Bangalore experience suggests a further implication for engaging civil society organizations: interventions to improve service delivery provide a potentially viable and sound entry point for governance reforms. Demand-driven reforms have generally focused on the delivery of public services, whether in response to local communities seeking better schools for children or to private firms demanding quicker processing of license applications. This is because service delivery is where the state meets the average citizen. Changes in the quality, quantity, and access to services affect everyday lives and thus make citizens more prone to support, if not to seek, reforms in governance.

Box 9.11 illustrates the huge potential for this approach. In the Middle East and North Africa (MENA), many countries are non-democracies and political accountability is relatively weak. The governance gap in MENA is significantly wider than those in other developing regions, largely as the result of weaknesses in public accountability (World Bank 2003).⁵⁸ In these countries, there appears to be much less governance reform activity, but at the community level, civil society efforts to address poor service delivery appear to be sprouting.

Box 9.11: Service delivery and civil society in West Bank and Gaza

A 1998 review of service delivery in the West Bank and Gaza asked a representative sample of beneficiaries about the provision of health and education services by NGOs, the private sector, and the Palestinian Authority. To evaluate the quality of the equipment and service, specialists also carried out institutional reviews of education and health facilities. The findings show that beneficiaries often select a particular provider because of easy access to the service or because of the providers' quality—areas where NGOs and the private providers ranked higher than the government. The findings were presented at dissemination workshops that were attended by ministers, senior civil servants, and senior representatives from NGOs and private organizations. The ministers of health and education reacted by using the findings to improve the quality of health and education services across the board and to improve coordination among the government, the NGOs, and the private sector.

Source: World Bank (1999), "West Bank and Gaza: Strengthening Public Sector Management". Washington DC.

This phenomenon is not inconsistent with the regimes in place in the Middle East and North Africa. All regimes care about their legitimacy, and one way that non-democratic regimes can maintain, if not enhance, their legitimacy is by providing adequate public services.⁵⁹ To do this, they need information about the existence, nature, and location (i.e. which agencies) of service delivery problems. CSO efforts such as report card surveys provide such information which leadership can then use to introduce needed reforms to the compact.

⁵⁸ See in particular figures 1.4, 1.5, and 1.8 of this report, which states that public accountability "measures the openness of political institutions and participation, respect for civil rights, transparency of government, and freedom of the press." It is more or less an index that reflects a combination of the quality of political accountability and client power.

⁵⁹ While dictatorial tactics have certainly kept the Castro regime in power for almost four decades, there is something to be said about the high quality of Cuba's health services, which are among the best in the developing world, as a factor that has contained citizen dissent.

To be effective, civil society efforts require an adequate supply response

The known experience with demand-raising efforts in developing countries is still rather thin, partly because many occur at the local government level and are not reported in national media. But such efforts can be and have been effective in taking politicians and bureaucrats to task for poor performance. The “People Power” episode in the Philippines, which led to the resignation of a duly elected but highly corrupt president, is an extreme example of what the engagement of civil society groups can do despite difficult collective action problems.

To be effective, however, demand-raising efforts require an adequate supply response. In practice, this means that certain public officials (career or appointed) must be willing to work closely with concerned civil society groups on a given issue, and that the latter must be willing to engage constructively with the former. Often, public officials see civil society organizations as a threat to their authority, while advocacy-focused civil society organizations tend to view public officials with disdain. But, to be able to move things along, civil society organizations need partners inside the public sector, since they have the knowledge and understanding necessary to move a reform agenda within the government. Likewise, reform minded politicians and civil servants need civil society organizations to galvanize public support. Box 9.12 below illustrates one such effort.

Box 9.12: Procurement watch – working with the “enemy”

In 1998, the Government of the Philippines launched a program to reform the public procurement system. With assistance from US Agency for International Development, the Department of Budget and Management (DBM) identified many serious problems, whose solution called for new legislation to bring together the many disparate laws and regulations impinging on procurement under a single, clearly written law. Getting such a law passed was a daunting task, since the law would fundamentally affect age-old arrangements between politicians and contractors, and for a year the reform program stalled.

But in 1999, the mood of the polity began to sour and, as survey after survey indicated, the focal point of the disenchantment was corruption. Of the activities that the citizenry considered seriously plagued by corruption, procurement was second only to revenue collection. Around this time, the World Bank had just completed a corruption diagnostic study, “Combating Corruption in the Philippines”, whose results further raised citizen awareness of the problems. Again, procurement stood out as a major problem area. These developments provided an opportunity to move forward once again on the reform program.

Procurement Watch Inc (PWI) was born in part from the need to harness the collective anger and frustration of the citizenry. It was organized as a non-profit institution with encouragement from the DBM and seed funding from the World Bank’s ASEM grant facility, along with private contributions by (then) recently retired government officials, academics working on corruption issues, and private citizens with long-standing concerns for problems in government procurement.

To establish its credibility with citizen groups and legislators, PWI quickly developed technical expertise in the area of procurement. With well trained and experienced staff and an active board of directors, it drew attention from the media on the need for a procurement reform bill. It secured advocacy support from different citizen groups throughout the country, was invited to participate actively in the three technical working groups formed to formulate the law – one in the executive,

another in the House of Representatives, and the third in the Senate—and was sought after for advice by proponents of the bill in both the House and the Senate.

With technical assistance from donors* and advocacy support coordinated and managed by PWI, the DBM finally secured the enactment of the Government Procurement Reform Act of 2002. The President signed the bill into law on January 10, 2003, almost four years after the effort was initiated.

* USAID provided the bulk of the assistance with complementary support from the World Bank, Canadian International Development Agency, the Asia Foundation, and the Asian Development Bank.

Information builds citizen voice and power

The media can be a powerful instrument for galvanizing citizen action. A free press raises popular awareness of inappropriate actions by elected and appointed officials. When people are aware of corrupt officials or networks, their reaction may include voting against incumbents, protests, and manifestations of unrest, or disengagement from the formal economy.⁶⁰ Widespread press coverage was notable in the deposition of former Brazilian president Collor in the early 1990s (Box 9.13, which brought citizens to the streets to protest. It was also instrumental in building the people power movement in the Philippines to depose then President Estrada in 2001, and widespread protests in Ecuador to oust then-president Bucharam in the late 1990s.

Box 9.13: Media and the impeachment of a president

In Brazil, investigative pieces published by various outlets set the stage for Fernando Collor's departure as president. In early 1991, a *Jornal de Brasil* reporter used a computer access code provided by a senator to examine federal finance ministry files and discovered that "money distributed to the president's wife . . . and earmarked for charity had gone to her relatives and family in her hometown". The following year, after months of cultivating Collor's brother as a source, *Veja* magazine published an interview in which the brother, Pedro Collor, accused the president's campaign treasurer, Paulo Cesar Farias, of running a multimillion-dollar influence peddling ring on Fernando Collor's behalf. Congress set up a commission to investigate the charges. During its hearings, a flurry of hard-hitting insert reports by various outlets – particularly *Isto It* magazine and the *Foha de Sao Paulo* newspapers – drew on a variety of documents including bank records, cancelled checks, telephone records, and even photographs of Collor's lavish private residence, as well as interviews with senior officials and their aides to reinforce a picture of massive high-level corruption within the Collor administration. It ultimately emerged that Farias had extorted more than \$55 million from firms in exchange for their favorable treatment by the government. By year's end, amid a national uproar, Collor stepped down, one day before he was to be impeached.

Source: Rick Stapenhurst (2000), *The Media's Role in Curbing Corruption*. World Bank Institute Working Paper. Washington DC: World Bank Institute, p. 3.

⁶⁰ An excellent study that analyzes the effect of type of electoral system on policy outcome is Roger B. Myerson, "Theoretical Comparisons of Electoral Systems," *European Economic Review* 43 (1999): pp. 671-697. Torsten Persson, Guido Tabellini, and Francesco Trebbi, "Electoral Rules and Corruption," CEPR Working Paper (London: 2000) assess the impact of corruption and voting in different electoral systems (e.g. majoritarian or proportional representation).

Information to build citizen power can also be effective at the local level. One of the most successful experiments in the use of information to engage community action was in Uganda. The Ministry of Finance launched a public expenditure tracking survey to monitor the flow of funds from the budget for per capita education grants to local school districts. The survey showed that, in 1994, the local districts received on average only 13 percent of the funds due them. Alarmed by this huge leakage, the ministry launched a nationwide awareness program that informed local communities of the funds that were due to their respective districts, thus giving communities a benchmark for monitoring the flow of funds. The results have been astounding, with the leakage falling to less than 20 percent of the budgeted funds.⁶¹ The Uganda experiment indicates the power that information can have in galvanizing civic action. It also suggests the influence that laws on the right to information may have in empowering NGOs, business organizations, and civil society more generally. For example, a grassroots campaign in Rajasthan, India led by a local NGO, the MKSS, used information gleaned from government files to expose and then combat massive corruption at the local level, showing how public officials skimmed money off the wages of workers and paid friendly contractors for work never done. A recently passed freedom of information law made it possible for the MKSS to conduct this vigorous and successful campaign.⁶²

3. *Strategy and implementation: the challenge for governance reforms*

The 1990s provide a plethora of emerging lessons for governance reforms. Given the long time it takes for such reforms to mature, these lessons can at best be tentative. Nevertheless, as discussed above, there are many that developing countries can reflect on in contemplating and mapping out their future programs and actions.

The decade also offers insights into reform strategies, which typically fell into two broad categories: the big bang, shot gun approach or ad hoc incrementalism. The former was largely inconsistent with capacity constraints and political realities and the latter were isolated efforts not linked to a longer-term, overall game plan.

“Big bang” approaches were bound to fail as they often overstrained limited implementation capacity. In Hirschman’s words, countries with the wherewithal to carry out a coordinated big push “would not be underdeveloped in the first place” (Ellerman 2000). The main results from such vanguard approaches to governance reforms were major changes in formal rules: new or amended constitutions, new legislation, ostensibly independent courts and audit institutions, and so forth. Such changes are not unimportant: formal rules should matter in shaping behavior. But in practice they rarely do shape behavior unless there is an equal commitment to better aligning *informal* rules to improve the incentives that face politicians, bureaucrats, and citizens (World Bank 1998:128).^{63,64}

⁶¹ Reinnika and Svensson (2003 and 2004).

⁶² For more on lessons on freedom of information laws, see World Bank, *PREM Note* (forthcoming).

⁶³ For an excellent example, see “Combating Corruption in Indonesia”, World Bank Report No. 27246, 2003.

⁶⁴ There is “often a vicious circle whereby the failure of the state breeds more corrective rules which both reformer and opportunist applaud—the reformer under mistaken formalistic notions about how to reform and the opportunist in the knowledge that reform will be frustrated and his opportunism can continue” (World Bank 1998:128). This is not to imply that in developed country settings there are no informal rules. These never

Ad hoc incrementalism, on the other hand, has also been problematic. With few exceptions, the ad hoc reforms were often symbolic in nature, intended to preserve the old rules and informality while pretending to reform. In some cases they represented attempts of individual or small groups of reformers whose efforts are well motivated, but, for lack of support, were ultimately undermined by jealousy, intrigue, or fatigue. More important, they tended to be unrelated to a more coherent reform strategy and thus over time many lost their steam.

Thus, big bang approaches are unlikely to work in most settings, nor will ad hoc uncoordinated interventions without an overall game plan relevant to the conditions facing the country. What are needed instead, perhaps, are highly focused, pragmatic interventions, which may be termed “strategic incrementalism”. These interventions may be opportunistic because they exploit the willingness to reform, but they are better grounded in the political realities and consistent with the capacity constraints of the country concerned. Knowing what is appropriate in which country situation is often half the battle.

Providing a detailed road map to guide strategy is beyond the scope of this chapter and is a task requiring fundamentally new research and analysis. But we can offer a glimpse of what is possible. While empirical evaluation and assessment of public sector reform is still in its infancy, an analysis of past developmental experiences suggests a possible approach to governance reform strategies in developing countries.

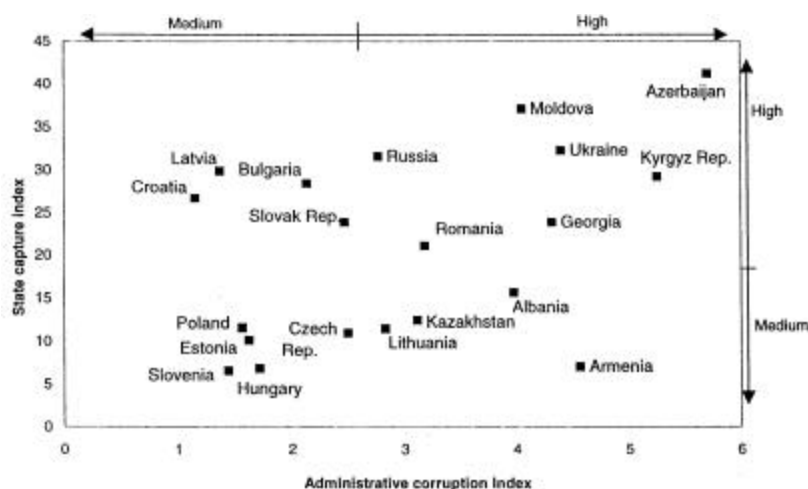
A recent survey of firms conducted by the World Bank in the Eastern Europe and Central Asia (ECA) region provided information that can be used to array the countries of the region along a two-dimensional matrix, with administrative corruption on one dimension and state capture in the other.⁶⁵ Recall that administrative corruption reflects the quality of the compact and that state capture affects the strength of political accountability. So the quality or state of governance in a country can be broadly characterized along these two dimensions Figure 9.6.⁶⁶

disappear. But they tend to be better aligned with formal institutions rather than being inconsistent with them. North (2002).

⁶⁵ This is the Business Environment and Enterprise Performance Survey (BEEPS) conducted first in 1999 and most recently in 2003. The findings of the 1999 survey were analyzed and published in 2000 in a World Bank Report, *Anticorruption in Transition*.

⁶⁶ Ideally, a third dimension measuring client power would be desirable. Data on citizen voice are available and so it would be possible to construct this third dimension.

Figure 9.6: Classification of states: by governance profile



The matrix suggests a classification of countries into four possible types: capable, weak, captured, and restrained. And for each type, possible potential entry points for strategic interventions can be identified.

Capable: In these states, administrative corruption tends to be low and state capture not heavily entrenched. Examples of such states are South Korea, Chile, Hungary, and the Czech Republic. To a lesser extent, Botswana and the Indian states of Andhra Pradesh and Karnataka may fall into this category as well. In capable states, the challenge is usually to increase the quality and efficiency of public services, in order to best utilize limited public resources. Episodic scandals, reported by vigilant media or civil society organizations, usually result in public dialogue and ultimately in a set of actions to reduce opportunities for corruption. In these countries it is often possible to undertake difficult systemic reforms using more or less a technocratic approach, providing there is leadership and support that coalesces around the reform objective.

Weak: Many of these countries have only recently emerged from conflict or attained statehood, and are missing many of the basic structures needed to manage the public sector. Both bureaucratic capacity and accountability are weak, and administrative corruption is high. Often weak states have relatively low levels of state capture from business interests, not because accountability mechanisms are effective, but because the state is itself insufficiently developed to be captured. In fact, as these basic structures are established, the risks of state capture quickly increase. Examples of such states are Albania (in 1999) and Armenia (in 1999). Nepal and Tanzania may also be examples, as may many of the states in the LICUS category.⁶⁷ In these states, the primary challenge is to ensure that taxes are collected, key

⁶⁷ World Bank data suggest that 25 to 30 countries qualify as low-income countries under stress. In these countries, securing law and order and ensuring the delivery of very basic public services remain the primary governance tasks. Beyond this, the evidence suggests that comprehensive and/or more technically demanding governance reforms are unlikely to be feasible. The LICUS Task Force Report ([reference](#)) suggests that starting with narrow, manageable “zero-generation reforms”—institutional or socioeconomic changes that are

services are delivered, and budget execution is sufficiently controlled. Given limited bureaucratic capacity, it is especially important that reform efforts are targeted and that international support for these reforms is highly coordinated.

Captured: These states have serious problems of administrative corruption nested in an environment highly subject to capture. There is often an urgent need to build capacity in the public sector. However, investments in capacity are unlikely to produce sustainable improvements, because of political corruption (grounded on rents) that permeates the system at all levels. Examples of such states include Azerbaijan (in 1999), Russia (in 1999), and Kyrgyz Republic. States that are “weak” but resource rich or dominated by a few valuable industries can fall easily into this category. The challenge in these states is to break the stranglehold of special interests, for example by breaking up powerful monopolies—if capture is by private interests—or by reducing military expenditures—if capture is by the military. Not surprisingly, these types of reforms are the least likely to be adopted while the vested interests remain strong.

Restrained: The bureaucracy in these states tends to have sufficient capacity and accountability so that administrative corruption is relatively mild. Political accountability is likely the “weakest link in the chain”, resulting in a high level of state capture. Examples of such states are Croatia (in 1999), Slovakia (in 1999), Serbia and Montenegro (in 1999), and Latvia. Argentina, the Philippines, and some states in India may also be examples. Options are limited while the existing leadership is well entrenched. When genuine change in leadership occurs, as in Croatia, Serbia and Montenegro, Slovakia, and Latvia, and where civil society is relatively robust and can play an important role in stimulating demand for change, reforms can emerge fairly fast and can potentially be sustained.

Table 9.2 summarizes this discussion and highlights the potential entry points for strategic interventions in each of the four types of states. Each type faces different challenges and different opportunities for reform. Among the four, “breaking through” a captured state presents perhaps one of the most difficult strategic challenges in governance reform.

politically feasible and socioeconomically non-divisive—are likely to provide quick pay-offs and have some potential to catalyze further change.

Table 9.2: States and entry points for strategic interventions: a governance typology

Type of state	Governance profile	Main implications for the triad	Key challenge	Possible entry point
Capable state	<ul style="list-style-type: none"> low to modest administrative corruption mild state capture 	Some gaps in bureaucratic capacity and internal accountability	Increasing efficiency of public service delivery	Technocratic reforms in public administration, as needed; comprehensive reform strategy may be feasible
Weak state	<ul style="list-style-type: none"> high levels of administrative corruption mild state capture 	Very weak bureaucratic capacity and/or internal accountability	Ensuring delivery of basic public goods	Highly targeted reforms in key sectors only, supplemented by limited reforms in budget execution to ensure financial accountability
Captured state	<ul style="list-style-type: none"> high levels of administrative corruption high state capture 	Very weak political <u>and</u> internal accountability; possibly weak bureaucratic capacity	Breaking hold of vested interests on the process of policy and institutional reform	Build demand for reforms; possibly explore opportunities at sub-national level
Restrained state	<ul style="list-style-type: none"> low to modest administrative corruption high state capture 	Very weak political accountability	Increasing “voice”	Build demand for reform; await change in leadership due to crisis related to corruption, after which technocratic reforms to increase political accountability may be possible

Public sector governance has been in many ways the grand challenge facing developing countries. A crisis of governance of varying intensities pervades much of the developing world, with the poor paying the heaviest price for this. Perhaps the most important lesson of the 1990s is that technocratic responses to this crisis work only in very limited settings—where there is committed leadership, a broad-based coalition in support of the reform, and sufficient capacity to carry the reform process forward. Clearly, these conditions exist in only a minority of developing countries and rarely in the countries in most urgent need of governance reform. This is the crux of the challenge for the decade ahead.

Rising to this challenge invariably must start with a deeper understanding of the political dimensions of reform, and in particular, of how reform can be used to identify and build constituencies that are capable of sustaining the reform momentum. This requires fundamental changes in our methods of analysis. In this context, a focus on “drivers of change” is a potentially promising avenue (Duncan 2003). While the particular drivers will naturally vary from country to country, the common thread of this approach is a focus on solving specific, highly salient problems facing individual communities—for example in healthcare, sanitation, or business regulation. These are problems around which constituencies for reform both inside and outside of government may be easier to build and maintain than, say, upstream reforms in civil service reform or financial management.

In many countries, the drivers of change may be a group of young, perhaps inexperienced, leaders, in need of training and support. Almost all successful reform efforts have been shepherded through by dynamic leaders: “Such leaders seize opportunities as they appear, but they also create them, by identifying and reaching out to potential beneficiaries, reshaping institutions, and articulating a compelling and achievable vision of the future.” (World Bank 1997: 154). The challenge in this instance is how to create and nurture an environment that can encourage dynamic, forward-looking individuals to push much needed reforms. In some cases, this may well be through political decentralization and economic liberalization, where the former gives local public officials autonomy over their localities and the latter creates pressures for competition among the localities.

In other cases, the pressure for reform may come from the outside. Civil society groups, media, business associations, and/or religious organizations are fertile sources of change. While these groups are often plagued by collective action problems, experience shows that they are fully capable of overcoming these problems. The challenge they face is one of sustainability; a problem that donors and private foundations can address through technical assistance and funding. Better governance is a public good and thus groups working on governance reforms will generally find it more difficult to solicit contributions from the general public.

Whether this focus on problem solving and results-oriented “drivers of change” will help countries to navigate the difficult terrain of governance reform in the next decade remains to be seen. What is certain is that governance reform will retain a high place on the reform agenda.

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