

# Working towards more effective collective donor responses to corruption

Background study of how donors have responded to corruption in practice

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## SYNTHESIS REPORT AND RECOMMENDATIONS

### Executive summary

In 2006, the OECD Development Assistance Committee (DAC) Ministers of Development expressed a desire to move towards more effective collective responses to governance issues, particularly as regards corruption. In 2007 the OECD Policy Paper on Anti-Corruption “Setting an Agenda for Collective Action” proposed developing a voluntary code of conduct for co-ordinated donor responses to deteriorating corruption contexts. The DAC Network on Governance (GOVNET) was tasked with producing a framework for joint responses. To inform this work the Anti-corruption Task Team (ACTT) of the GOVNET commissioned this retrospective study of how donors have responded to corruption in practice in the past, so as to understand better the opportunities, constraints and incentives for more effective collective responses and to establish principles on which a draft code of conduct could be based.

Three case study locations were selected by the ACTT – Afghanistan, Indonesia and Mozambique. These countries were selected to ensure coverage of a range of corruption “situations”, different donor architectures, different aid delivery mechanisms, varying degrees of donor harmonisation and a geographical spread of countries in Africa and Asia, including one conflict or post-conflict state. Each case study led to a set of recommendations that are intended to be of use beyond the specific country context and inform development of a code of conduct for collective donor responses. This report is the executive summary of a report which synthesises the findings of the three case studies (the full report is accessible through the GOVNET website at [www.oecd.org/dac/governance/corruption](http://www.oecd.org/dac/governance/corruption)). Tentative conclusions about how donors have responded to corruption in certain types of contexts have been drawn, based on these studies, key informant interviews from other locations, including donor headquarters, and a literature review. Additionally, the executive summary draws on additional comments from a “headquarters” or “policy” perspective provided by donors via the GOVNET Anti-Corruption Task Team.

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This report has been prepared by a consultant commissioned by GOVNET, and will inform the development of DAC guidance on joint responses to corruption.

## Background and purpose of this work

In 2006, the OECD Development Assistance Committee (DAC) Ministers of Development expressed a desire to move towards more effective collective responses to governance issues, particularly as regards corruption. In 2007 the OECD Policy Paper on Anti-Corruption “Setting an Agenda for Collective Action” proposed developing a voluntary code of conduct for co-ordinated donor responses to deteriorating corruption contexts. The DAC Network on Governance (GOVNET) was tasked with producing a framework for joint responses. To inform this work, the Anti-corruption Task Team (ACTT) of GOVNET commissioned this retrospective study of how donors have responded to corruption in practice in the past, so as to understand better the opportunities, constraints and incentives for more effective collective responses and to establish principles on which a draft code of conduct could be based.

## How donors have responded to corruption in practice

This report synthesises the findings from three very different<sup>1</sup> country case studies chosen by the ACTT: Afghanistan, Indonesia and Mozambique. Based on these studies, key informant interviews from other locations including donor headquarters, and a literature review, only tentative conclusions can be drawn about how donors have responded to corruption in certain **types** of contexts – in many ways each context is unique. However, all these countries had in common an environment permeated with high levels of corruption – in some cases a steady deterioration and in others specific cases of deep corruption. Responses have taken place at different stages in a programming cycle and in the context of ongoing engagement between donors and other stakeholders. “Situations”<sup>2</sup> have arisen that have sometimes caused donors to reassess the nature of that engagement and perhaps modify it – the response.

Even while delivering short-term responses to corruption in order to manage fiduciary and reputational risk, donors have continued to pursue longer-term approaches to strengthen accountability and improve transparency;<sup>3</sup> their assumption is that corruption is a symptom of weak governance that will improve over longer periods of reform. Donors’ priority has often been to remain engaged with partner governments to achieve their development objectives. That approach established, a degree of inertia has arisen among donors to modify their stance where there is evidence of lack of progress in tackling corruption, of stagnation, or of deterioration in governance. Variations between donor responses to similar corruption situations in different contexts have primarily reflected the characteristics of the aid relationship and/or geostrategic importance of partner countries to donor countries.

### Country cases

The way donors have engaged with anti-corruption in *Mozambique* has similarities with donor responses in other multi-donor budget support contexts where the partner country is aid dependent and high aid volumes are provided. In light of evidence that poverty is being reduced, partly as a result of donor efforts, donors have given greatest priority to ensuring that aid is delivered predictably, while managing the fiduciary and reputational risk<sup>4</sup> associated with corruption. Donors and government have made significant efforts to establish and adapt the aid architecture around multi-donor budget support, so that performance is monitored jointly and responses to stagnation or deterioration in performance take place predictably and in a way that protects development outcomes. This framework has provided the flexibility for individual donors to present a strong message against corruption – for example, if political pressure from their home constituency increases – while protecting the overall aid partnership. In addition since 2006, an informal network and, subsequently, a formal donor working group, was established to share information and identify key anti-corruption messages and actions which would be the focal point for technical dialogue and performance monitoring around budget support and across sectors.

1 For example, the three differ significantly in that one is a central Asian country that has been in conflict for several decades; one is a very large middle-income country with a highly successful development record; and the third is a country that has emerged from conflict but is a mid-sized lower-income African economy. Each country has a specific aid architecture (although there are similarities), while the constellation and balance of influence between donor countries varies from case to case.

2 The study examined “situations” – events, triggers or decision points for responses – including assessments of deteriorating governance/corruption, new evidence of corruption, leakages in donor-controlled programmes and budget support operations, and new opportunities for reform. More than one “situation” may arise simultaneously.

3 With little more than a decade of experience of “anti-corruption” efforts, however, some donors in some contexts have more recently begun to target specific drivers of corruption where they believe there is scope for reform, and complement more traditional nationally based approaches with international action.

4 Fiduciary risk is the risk that funds are not used for their intended purposes or do not achieve value for money. Reputational risk is that donors and partner governments are perceived not to be managing taxpayers’ funds appropriately. These risks can contribute to development risk, *i.e.* that funds are not used effectively to achieve development outcomes and that public support for development in donor countries is lost.

In *Afghanistan*, donors' engagement with anti-corruption was shaped initially by the most urgent requirements to stabilise and restore basic services, while maintaining security, after the fall of the Taliban in 2001. As in many other conflict and post-conflict fragile states, a higher priority was accorded these other strategic objectives at early stages than to tackling corruption, with little attention to the longer-term effects of this approach. Provision of high aid volumes into weak systems has nurtured old and new systems of patronage; corruption has increased, threatening political stability and other stabilisation and security objectives. While donors have become increasingly co-ordinated in their technical responses to corruption, until recently it has proved difficult to agree on a common strong message to government on corruption across different dialogue channels, or to reinforce this with concrete agreements on anti-corruption measures and monitoring of progress.

In *Indonesia*, by contrast, donors responded when a crisis after the fall of Soeharto provided an opportunity to tackle corruption and a new partner government demonstrated a strong lead. Donors co-ordinated dialogue with government through the Consultative Group for Indonesia (CGI). Donor support to civil society through the Indonesian-led Partnership for Governance Reform in Indonesia (PGRI) helped to sustain demand for reform. Although there are signs of progress in tackling corruption, due to fiduciary concerns, most donors still do not channel aid through government systems. Government ended the CGI in 2007 and has since prioritised dialogue with important creditors as Indonesia becomes less aid dependent and donor responses less co-ordinated. As Indonesia has "graduated" from LIC to MIC status, donors' technical governance capacity has been withdrawn, putting at risk sustained engagement to ensure that effective institutions are built over time.

### *Responses to different situations of deteriorating governance and corruption*

When corruption arose in donor-controlled projects or sector programmes, donors responded in line with corporate instructions – *e.g.* via suspension of aid, audit, investigation, reimbursement. The response was sometimes strengthened by bilateral political dialogue. As well as efforts to recover funds, controls in these projects and programmes were reinforced, further use of government systems was avoided, and additional safeguards were introduced. These responses had a short-term and local impact, although additional safeguards may have done little to strengthen government systems. Some responses also involved reviewing and refocusing wider support to governance and anti-corruption reform where sustained effort was required to achieve longer-term results. Sometimes such reviews strengthened the hand of key reformers within partner governments, even in the short term.

Donors have sometimes responded to corruption in donor-controlled programmes or sectors by raising the issue at the level of the overall aid partnership. In such situations, and where leakages are reported from government systems in multi-donor budget support contexts, flexible response mechanisms allow individual donors or groups of donors to vary disbursements in a pre-agreed and signalled fashion in response to corruption, while protecting development spending and ensuring predictability. However, such responses can generate mixed messages to partner governments on the importance of tackling corruption. Sometimes a strong message, such as reduction in budget support by an influential donor or critical mass of donors, has encouraged partner governments to take action on corruption.

A general deterioration or stagnation in governance and corruption is often reflected in indicators being monitored jointly by donors and government in performance assessment frameworks (PAF) or assessments outside the PAF. Bilateral aid agreements and joint financing agreements establish in advance how donors can and should respond to these corruption situations. Often they provide for a graduated response of consultation and dialogue, escalating to reductions or delays in aid disbursements if action is not taken to improve performance against the reform indicators. These graduated response mechanisms can focus partner government attention on the need to deepen or accelerate certain reforms, except where local political dynamics resist this.

## Opportunities, incentives and constraints for more joined-up responses

When choosing how to respond to corruption, donors manage tensions and trade-offs between fiduciary or reputational risk and development goals. The last ten or so years have seen donors develop responses that prioritise aid effectiveness and the principles of the Paris Declaration, encouraging donor co-ordination and greater efforts to ensure predictability of aid flows in order to maximise development outcomes. However, when reviewing the findings of this report's retrospective research in November 2008, the ACTT drew attention to the potential impact of the global economic crisis. Looking ahead, it appeared that this might shift the balance of trade-offs for donors, limiting their appetite for risk and leading to greater emphasis on fiduciary management and a search for responses that achieve more immediate action against corruption.

In recent years donors and partner governments have constructed aid architecture and performance-monitoring mechanisms that encourage donors to co-ordinate dialogue, monitoring and aid delivery among them and to minimise disruption to aid flows. Formally and informally donors have increasingly ensured that, when they need to respond bilaterally to domestic demands for accountability or corporate policy on managing fiduciary risk, they minimise the risk of a “domino effect” on others' aid disbursements. It remains to be seen whether this pattern prevails in the context of deepening concerns for fiduciary risk during the global economic downturn.

Separate dialogue mechanisms – with partner governments, among different donors and where there are different strategic priorities even within a single donor government – can be a constraint to joint responses. They may generate mixed messages if actors take different stances on corruption. A crisis or perceived increase in corruption may be an incentive to improve co-ordination, but donors are better prepared to manage corruption situations if they and partners already have well-established and quality dialogue mechanisms. If the approach is agreed in advance among donors, they can take advantage of separate dialogue channels and styles to deliver similar messages effectively. By contrast, mixed messages can also absorb scarce government time because of the transaction costs and capacity required to attend to different donors or parts of donor governments. This can cause confusion over sequencing and priorities for reform.

Partner governments' leadership and ownership of measures to improve governance and reduce corruption present an opportunity for donors to respond jointly with support, both generally and when monitoring reveals that reforms are off-track. Where partner governments do not own approaches to tackle corruption, donors often disagree on whether this is due to weak capacity or weak commitment, and may then disagree on how to respond. Even where partners' commitment to reform is weak, there are sometimes reformers and identifiable benchmarks of reform in some key areas, and these can be furthered with targeted and sustained donor support.

Joint and prior analysis by donors is important for understanding the political drivers and policy priorities that motivate partner governments, so as to identify areas with traction. This can facilitate monitoring of a few critical benchmarks, drawn where possible from partner governments' own plans (AAA 25). Donors should jointly prepare to respond to corruption situations by sharing information and discussing likely trade-offs well in advance. This advance preparation should include considering circumstances in which all, or a critical mass of donors consider that government shows little or no commitment to reform. In such circumstances, where donors need to convey a strong joint message, fiduciary and reputational risk are likely to outweigh the benefits to development outcomes of continuing with existing dialogue and aid flows.

Donors' policies on governance, corruption, conditionality and aid effectiveness have converged in recent years, although policy is constantly evolving and agencies adopt new approaches at different rates. The resulting differences in practice, especially in the field, are a constraint to joint responses. Donor staff often face competing priorities and may lack appropriate technical skills to assess evidence of corruption and the trajectory of change, making it more difficult to judge and agree appropriate responses. Multiple assessments of governance and corruption have also been a constraint to joined-up responses, although this can be mitigated if information is shared and analysed jointly (OECD DAC GOVNET, 2009a).

New policy has the potential to complement existing efforts to improve transparency and accountability in systems of national governance. For example, donors' anti-corruption policies have begun to focus increasingly on the global incentive environment,<sup>5</sup> which includes measures to trace illicitly acquired assets and reduce money laundering. Proponents of these initiatives believe they could deter corrupt individuals and networks. Some parts of donor organisations see the UN Convention against Corruption (UNCAC) as a framework around which donors could co-ordinate support and monitor progress when it has been adopted by partner governments. There are opportunities for donors to link international and national anti-corruption efforts more effectively and work with other parts of their own governments and the private sector – for example, to address international bribery. Analysis of the effectiveness of such tools, compared with more traditional approaches, would be a valuable complement to this study.

Many donors' policies now reflect a conviction that strengthening partner governments' accountability to their citizens is an important means of improving governance and reducing corruption even if progress toward that accountability has been piecemeal. However, more co-ordinated donor responses to corruption may be seen as reinforcing accountability to *donors* rather than to citizens in partner countries, especially where donors provide large aid volumes and partner countries are aid dependent. Donors have supported reforms in partner countries to improve formal institutions of horizontal accountability within the state and, to a lesser extent, vertical accountability to citizens. Progress has been made where there has been a strong government lead, but in many instances informal patterns of accountability and established patronage systems have impeded implementation. In such cases donors have an even stronger imperative to strengthen the "demand side"<sup>6</sup> for greater transparency. Sustained donor support may be the only means by which civil society can maintain pressure for reform, resist threats, challenge existing patronage networks, build capacity, participate in policy debates, monitor reforms, generate information and carry out advocacy. Donors have an opportunity to analyse jointly the type of support that may be needed to strengthen vertical accountability and then identify comparative advantage for the provision of technical support, or niches where there is a limited political space to work on sensitive areas, such as political party reform.

## Towards more effective collective responses

In March 2008 the ACTT agreed that joint donor responses to corruption would be effective to the extent that they maintain emphasis on tackling corruption *while*:

- a) maximising and protecting development outcomes and the future development agenda;
- b) ensuring that dialogue mechanisms remain intact;
- c) minimising unpredictable aid flows for planning and disbursement purposes;
- d) allowing for anti-corruption efforts to be seen in context of wider governance reforms and concerns;
- e) being proportionate to the corruption scandal/deterioration etc.; and
- f) promoting accountability.

There was considerable evidence from the case studies that donors were successful in managing these policy and operational trade-offs while responding to corruption, and in maintaining emphasis on tackling corruption both through short-term signals and in longer-term support to reform. It was not the primary purpose of this research to assess systematically the effectiveness of donors' responses to corruption *per se* – whether short-term reactions such as intensified political dialogue and delayed aid disbursements, or longer-term refocusing of efforts to strengthen accountability and transparency. A more comprehensive review of donor approaches to tackling corruption, including new international initiatives, might<sup>7</sup> assist in making that assessment robustly, although it is likely that many existing approaches will require a longer period to demonstrate their effects.

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<sup>5</sup> Donor responses incorporating international action are not discussed further in this report since the primary scope, as required by the ToRS, refers to responses in country. For further examples of measures to address the global incentive environment see OECD, 2007.

<sup>6</sup> It is also important to complement measures to strengthen demand with support for measures to improve transparency, access to information, and other mechanisms of accountability to improve state responsiveness to increased citizen demand.

<sup>7</sup> Although there would be many methodological challenges, including tracing cause and effect of donor interventions and measurement of impact.

Neither the case studies nor key informant interviews demonstrated that short-term pressure by donors in partner countries, through dialogue or via aid disbursements, had a lasting impact on corruption where local political dynamics resisted this. Often partner governments' counter-response was to take formal demonstrable action, for example passing anti-corruption legislation or signing UNCAC. *Cumulative and sustained pressure* by a critical mass of donors, combined with technical and financial support for key reform programmes, has the potential to improve accountability and transparency where there is a degree of ownership and leadership from partner governments. Such action has resulted in clear progress, particularly in PFM reform.

Experience, however, suggests that there are also reputational and fiduciary risks associated with this approach, particularly where partner governments are not truly committed to reform. For example, by taking a longer-term view of change and attempting to understand better the underlying institutional incentives that drive corrupt behaviour, donors may be perceived to condone it (Mathisen, n.d.; Unsworth, 2007). Introducing large aid volumes into corrupt and entrenched patronage systems can both sustain and strengthen them (Cammack, 2007). It is recommended that further research be undertaken to explore partner government perspectives on how donors respond to corruption and understand how and why partner governments counter-respond. It is important to understand fully the political economy of each partner country and weigh the longer-term consequences of more gradual approaches in advance. It is equally important to keep the trajectory of reform and appropriateness of responses under regular review.

### *Principles that could form the basis for a code of conduct*

Based on the findings from this research and prior work carried out by the OECD DAC, including the "Policy Paper and Principles on Anti-corruption" (OECD, 2007), the following principles<sup>8</sup> are proposed:

1. Prepare in advance for responses, with joint, shared and regular analysis.
2. Follow the government lead where this exists. Otherwise foster this lead, promote accountability and co-ordinate donors even where a government lead is absent.
3. Agree in advance on a graduated response if performance stagnates or deteriorates.
4. Act predictably; encourage other donors to respond collectively to the extent possible, but allow flexibility for individual donors and make use of comparative advantage.
5. Maintain dialogue at different levels, use comparative advantage, and focus on long-term development objectives.
6. Foster accountability and transparency in country and internationally, including publicising the rationale for, and nature of responses.
7. Act internationally but support partners and field staff to link international action to anti-corruption efforts in partner countries.

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<sup>8</sup> These principles are elaborated in the Annex of the full report.



### *Acknowledgements*

The synthesis paper is based primarily on the findings of three field-based case studies by Karen Hussmann (Afghanistan), K. Sarwar Lateef (Indonesia) and Jose Jaime Macuane (Mozambique). Additional key informant interviews were carried out by Justine Davila and Marcus Cox. The fieldwork was carried out between June and August 2008.

The Executive Summary draws on the findings of the synthesis paper and additional comments from a “headquarters” or “policy” perspective provided by donors via the OECD Development Assistance Committee (DAC) Anti-Corruption Task Team (ACTT).

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