OECD

Working towards more effective collective donor responses to corruption

Background study of how donors have responded to corruption in practice

SYNTHESIS REPORT AND RECOMMENDATIONS

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Synthesis Report and Recommendations

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/ governanc e/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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ACKNOWLEDGEMENTS

AAA	Accra Agenda for Action
ACTT	Anti-Corruption Task Team of the OECD DAC GOVNET
A-CS	Anti-Corruption Strategy
ADB	Asian Development Bank
AfDB	African Development Bank
ANDS	Afghanistan National Development Strategy
ARTF	Afghanistan Reconstruction Trust Fund
CGA	Country Governance Assessment
CPI	Corruption Perceptions Index (Transparency International)
CPIA	Country Policy and institutional Assessment
DAC	OECD Development Assistance Committee
DANIDA	Danish Agency for International Development
GBS	General Budget Support
GoM	Government of Mozambique
IWA	Integrity Watch Afghanistan
JCMB	Joint Coordination and Monitoring Board (Afghanistan)
KPK	Komisi Pemberantasan Korupsi (Indonesia's Corruption Eradication Commission)
LIC	Low-income country
Men-Pan	Meneteri Negara Pendayagunaan Aparatur (Indonesia's Ministry for State Apparatus)
MIC	Middle-income Country
MOU	Memorandum of Understanding
PAF	Performance Assessment Framework
PAPs	Programme Aid Partners
PEFA	Public Expenditure and Financial Accountability
PFM	Public financial management
PGRI	Partnership for Governance Reform in Indonesia
RAN-PK	Rencana Aksi Nasional Pemberantasan Korupsi (National Action Plan for the Eradication of Corruption)
SGACA	Strategic Governance and Corruption Analysis
SIDA	Swedish Agency for International Development
StAR	Stolen Assets Recovery Initiative
UNAMA	United Nations Assistance Mission in Afghanistan
UNCAC	United Nations Convention Against Corruption
UNODC	United Nations Office of Drugs and Crime

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[1] 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"[2] 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;[3] 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[4] 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

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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 midsized 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.

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.

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 govern-ment 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 strength-ened 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 contraints 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 govern-ment 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,[5] which includes measures to trace illicitly acquired assets and reduce money laundering. Proponents of these initiatives believe they have 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 account-ability 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"[6] 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 oppor-tunity 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[7] 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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5 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.

6 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.

7 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[8] 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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8 These principles are elaborated in the Annex of the full report.

1. Background to 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 corruption. In April 2007 ministers agreed that the DAC Network on Governance (GOVNET) should prepare a framework for joint donor responses to corruption. This commitment was incorporated into the DAC policy paper and Principles on Anti-Corruption, "Setting an Agenda for Collective Action" launched in October 2007 (OECD, 2007). In line with the 2005 Paris Declaration commitments on aid effectiveness, the paper recognised four areas in which "donor action on a one-by-one basis is likely to be ineffective ... therefore, a concerted approach is necessary". These four areas were: joint corruption assessments carried out together with other organisations and building on existing work; support for anti-corruption benchmarks and targets, agreed jointly by donors and partners and used to monitor progress; co-ordination of anti-corruption and governance work; and development of a set of good practice principles or voluntary code of conduct on co-ordinated donor responses to deteriorating corruption contexts to be endorsed by ministers and rolled out at country level.

The GOVNET Anti-Corruption Task Team (ACTT) established a work stream to examine the opportunities, constraints and incentives for improving joint donor responses to various corruption situations in partner countries, and to produce recommendations for principles that could form the basis for a draft code of conduct to make responses more effective. The work stream comprised a feasibility study,[9] a literature review, and this set of country case studies.

The literature review highlighted the overall context for donor responses.

1. The context, donor architecture and incentives when responses to corruption are formulated are highly complex.

2. Donors face competing time scales: fiduciary concerns have intensified, as donors are accountable in the short term to their domestic constituencies for results *vis-à-vis* increasing aid expenditure. Meanwhile, analysis indicates that more realistic expectations of improvements in governance and corruption should be based on a longer-term, historical view and future prospects for change.

3. A wide range of different actors, with competing priorities and incentives, influence how responses to corruption are formulated. These include: individual donors' field and headquarter staff; individual governments' ministries or diplomatic and security interests; different-sized bilaterals acting individually, in groups or through multilaterals; and emerging donors with less interventionist approaches to governance.

4. There is often tension between the principles of the Paris Declaration and donors' need to manage development, fiduciary and reputational risk. When corruption situations arise, donors may feel pressure to react in ways that conflict with efforts to implement the Paris Declaration. It is difficult to respect partner country leadership that does not appear committed to tackling corruption. It is frustrating to align with partners' anti-corruption strategies where these do not appear to address corruption effectively or show tangible results quickly. It is challenging to defend reliance on partners' financial management systems when leakages are reported. It is hard to disburse aid predictably when there is domestic pressure to take action against corruption.

5. Anti-corruption policy has evolved considerably in recent years. Formerly, donors often viewed anti-corruption reforms separately from wider governance reform and focused on technical improvements to government anti-corruption capability. It is now more commonly recognised that corruption is largely a symptom of wider governance weaknesses; that support for country-led reform coalitions is needed; and that donor action must be underpinned by understanding of partner countries' political economy. In addition, techniques and frameworks for assessing governance and corruption have multiplied within and among donors and in partner countries.

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9 The feasibility study was based on the assumption that field-based donor staff members are best placed to assess the desirability and feasibility of developing such joint responses. In 2007 the ACTT gathered feedback from donor groups in seven partner countries (Cameroon, Honduras, Sweden, Peru, Sierra Leone, Tanzania and Zambia). The majority supported development of some form of common response principles. They also recognised the challenge of reaching agreement on reliable indicators and benchmarks, and the need to adapt to country contexts.

The UN Convention Against Corruption (UNCAC) has been adopted in some countries as one such framework for technical assessment of anti-corruption capacity. Donors now see that it is necessary to complement reforms in partner countries with steps in their own countries and internationally to combat bribery and track, freeze and recover illegally acquired assets.

6. It has been widely acknowledged that policy and *ex ante* conditionality of aid on policy and governance reform is largely ineffective (see Boehm, 2008 for the arguments summarised). Lessons learned from attempts to use political conditionality, for example in Uganda and Ethiopia, confirm that ineffectiveness, except in limited cases where donor co-ordination is strong and internal processes are already at work (de Renzio, 2006). Aid partnerships still involve conditions, but increasingly these relate to overarching partnership principles/processes/outcomes. It is increasingly accepted that while donors have legitimate fiduciary concerns, graduated responses should be made in a predictable fashion, so that donors set out clearly in advance situations in which they will review or cut funding.

7. Corruption situations (like other challenging governance or human rights issues) test efforts to harmonise to the limit, because common positions are complicated where individual donors' conditionality policies, definitions of corruption, approaches to governance assessment and sanction policies still vary significantly. Policies are constantly being updated,[10] but different donors adopt new international approaches at different speeds and these approaches may take time to reach field offices from donor headquarters.

2. Structure of this report

This report synthesises findings from the literature; from the three case studies carried out in the field in Afghanistan, Indonesia and Mozambique between June and August 2008; and from desk-based key informant interviews concerning other countries that receive high levels of aid which includes a significant proportion of budget support (*e.g.* Uganda and Cambodia). The three case study locations were selected by the ACTT to ensure coverage[11] 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.

It was evident from the research that the precise nature of this complex mix of factors, as well as the patterns of governance and accountability in each of the countries, provides a unique environment for efforts to improve governance and reduce corruption and for the way donors respond to corruption (Part I).

Each context or setting provides its own set of incentives, constraints and opportunities for joint responses, although a number of common themes emerge. These are analysed in Part II.

The ACTT indicated that joint responses to corruption would need to avoid mixed messages and promote consistency and coherence among donors. The ACTT considered that joint donor responses to corruption could 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 corruption efforts to be seen in context of wider governance reforms and concerns;*

   e) *remaining proportionate to the corruption scandal/deterioration etc.; and*

   f) *promoting accountability.*

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10 For example, while the research for this report was under way, the Accra Agenda for Action was adopted in September 2008, with the aim of deepening and accelerating implementation of the Paris Declaration.

11 As expressed in the terms of reference: How responses to corruption have been formulated in practice (OECD DAC ACTT, 2008).

It was clear from this work that identical action by different donors was often neither achievable nor desirable. Both donors and partner governments generally require or appreciate a degree of flexibility allowing donors to respond differently, but in a "joined-up", coherent and complementary fashion to corruption. Part III records the lessons learned and recommendations for more effective collective responses.

3. Key terms

Contexts

This term is used loosely to refer the environment in which responses take place. For example, it may refer to a country, its political economy or the dynamics between stakeholders.

Corruption

Policies of donors interviewed for this study converge around definitions of corruption similar to the "misuse of entrusted power for private gain". They tend to view corruption as a symptom of weakness in governance and an outcome of failures and conflicts in accountability relationships. Donors have tended to use this framework as a basis for policy and interventions. However, the framework may well differ from the way government interlocutors and citizens in recipient countries define corrupt behaviour.[12] That divergence can limit the scope for joint and effective responses.

Corruption situations

Corruption *situations* for which joint responses might be considered useful were defined (in OECD, 2007) as those where "efforts to improve the governance framework are unsuccessful or inappropriate and where corruption is seriously affecting poverty reduction efforts". The case studies examined events, triggers and decision points that provoked a response from donors and exposed tensions between managing risk and development goals. Situations can arise simultaneously and donor responses to them generally need to be understood as part of ongoing engagement with processes of reform and different stakeholders in an individual country context. In these contexts, political opportunities to address corruption may arise or be blocked.

Examples of triggers or decision points in the case studies and interviews included the following. Since they may occur simultaneously, descriptions and analyses in the paper necessarily overlap:

Part I, Section 2.1-2
- governance or corruption assessments showing a deteriorating or stagnating trend;
- new evidence of corruption emerging;

Part I, Section 2.3-4
- monitoring of government performance indicates declining or stagnating performance, including situations where there are other signs of limited or reduced government commitment to reform;

Part I, Section 3
- allegations or evidence of leakage or corruption emerging in donor-controlled projects or programmes;

Part I, Section 4
- allegations or evidence of leakage or corruption arise in government systems where donors provide budget support.

Donors

This term is used broadly to cover bilateral and multilateral agencies and development banks.

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12 The UN Convention against Corruption (UNCAC) notably avoids defining corruption, instead providing examples of corrupt practices (Arts. 15-22).

Donor responses

A *response* to corruption is not an isolated incident. Responses take place at different stages in a programming cycle and in the context of ongoing engagement between donors and other stakeholders. The ongoing engagement involves analysis, diagnosis and preparation, as well as efforts to support processes of change, transparency and accountability. In the course of this ongoing engagement, a *situation* may arise that causes donors to reassess the nature of that engagement and perhaps modify it – the response.

Responses also occur – sometimes simultaneously – at different levels of donor country and agency engagement *(Figure 1)*. These include:

- country strategy and aid allocation/modality decisions (HQ/country)
- management of expected fiduciary risk (HQ policy, country programme design and safeguards)
- intensified consultation and dialogue with other donors and partner governments
- modifications to the aid architecture for managing responses
- adjustments to the timing or size of disbursements, *e.g.* freezing or delaying disbursements, fixed and variable tranches (HQ/country)
- freezing of disbursements during investigation of allegations of corruption
- ongoing support to key governance reforms to build accountability and transparency (based on international lessons and country priorities), *e.g.* public financial management (PFM); public administration reform; justice sector reform; critical drivers of corruption (natural resources)
- refocusing of support to governance reforms
- nurturing demand for greater transparency and accountability
- tackling the global incentive environment for corruption, *e.g.* reducing international bribery and money laundering.[13]

Figure 1.   **How donors respond to corruption**
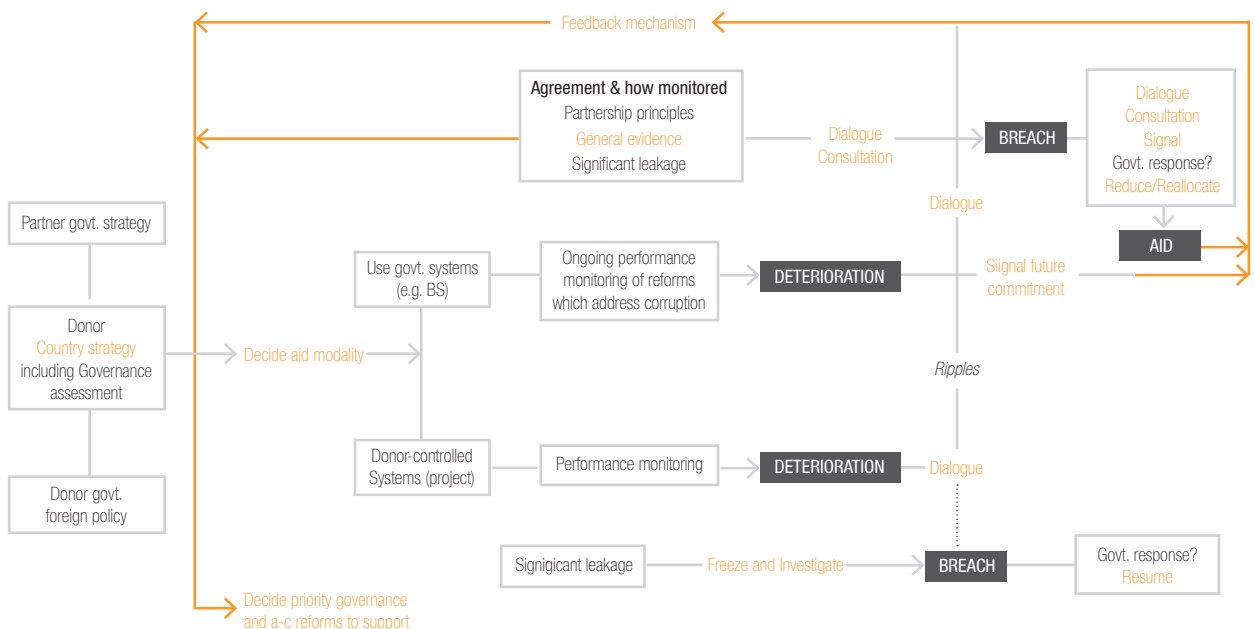
*Orange lines indicate responses.

13 In accordance with the ToRs this is largely beyond the scope of this study. For more information on this type of response see OECD, 2007.

SYNTHESIS OF FINDINGS

1. Contexts

The case studies document how donors have responded to corruption in the past in a range of different country contexts. Responses are viewed as part of an ongoing engagement with a range of anti-corruption and governance reforms and with different stakeholders. Each individual country context i) uniquely frames the opportunities, constraints and incentives affecting donor responses and ii) poses a particular set of governance challenges.

1.1 Governance, politics and patterns of accountability [14]

Donor responses to corruption take place in a range of different governance contexts. These provide opportunities and barriers to efforts to improve governance and tackle corruption. Donors' assessment and understanding of these contexts shape the nature and effectiveness of their responses.

Each of the case study countries has experienced a crisis of conflict and/or governance at some point in the past 20 years. Since then there has been a formal transition to democracy, and governments have put considerable effort into reforming the public administration and service delivery.

Donors have supported reforms 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 of these types of reforms. Finding and agreeing appropriate collective responses in these instances is particularly challenging.

Donor policies (*e.g.* WB, 2007; USAID, 2005; DFID, 2007; Danida, 2007) have been updated in recent years to reflect a conviction *(Box 1)* that strengthening partner governments' accountability to their citizens for improvements in transparency may in some circumstances be more effective and sustainable in the longer term. Thus donors have also responded to corruption by trying to strengthen civil society. This has happened via support to international NGOs and to anti-corruption and other civil society organisations in country. That support has often led to a proliferation of civil society organisations, as noted in Mozambique and Indonesia, dependent on donor funding and therefore themselves accountable to donors. On the other hand, such support has provided space for civil society organisations to advocate improvements to governance and anti-corruption efforts, where it otherwise might have been considered too risky[15] for individuals or organisations to challenge existing patronage networks or predatory behaviour.

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14 Here the term vertical accountability refers to citizens holding leaders to account directly, for example via elections. Horizontal accountability refers to mechanisms between parts of the state apparatus, for example supreme audit or judicial oversight of the executive.

15 For many it still is too risky or illogical to challenge patronage systems that protect them, compared with relying on donor support that may be transient. For example, in Afghanistan some civil society actors are more aware of loyalty to power-holders who will likely outlast current international intervention.

Box 1. The impact of strengthening citizen demand for anti-corruption reform

The impact of 'demand-side' interventions on reducing corruption is difficult to establish due to methodological challenges, but a set of case studies support the claim that they can (but do not automatically) contribute to reducing corruption and improving governance. Most studies and evaluations suggest that such interventions have an indirect impact on factors likely to affect corruption, such as increased participation, access to information or levels of awareness rather than an immediate impact on levels of corruption. Additional benefits include greater responsiveness of public policies, improved quality and quantity of public services and better outcomes of development projects. There is a growing recognition that maximising the impact of such interventions implies strengthening the supply side as well. Citizen demands need to be met by governments that have both the will and the capacity to respond.

The effectiveness of such interventions is likely to be enhanced when:

• Broad, democratic and truly inclusive constituencies are built to avoid voice capture by narrow interest groups within the communities;

• There is a legal standing or formal recognition for non governmental representatives in policy making institutions;

• Ongoing presence of citizens is ensured throughout the institution's work process;

• There is structured and liberal access to the flow of official documentary information;

• Citizens have the right to issue dissenting reports directly to authorities such as legislative bodies to challenge poor performances on controlling corruption;

• Service users have the right to demand a formal investigation and/or seek legal redress for poor or non-delivery of services.

Source: U4 Expert Answer: Chêne, 2008.

Nonetheless lessons from elsewhere (*e.g.* Tisne and Smilov, 2004) show that if governments lack capacity to respond, strengthening demand alone can also lead to disillusionment and alienation by citizens. Therefore it is important to complement measures to strengthen demand with support for measures to improve transparency, access to information and other mechanisms of accountability.

More co-ordinated donor responses to corruption may be seen as reinforcing *accountability* to donors rather than to citizens in partner countries. This effect is compounded where donors provide large aid volumes and partner countries are aid dependent.

In *Mozambique,* civil war ended in 1992 and was followed by the first democratic elections in 1994. Subsequent governments have adopted a comprehensive approach to governance reform, focusing on reform in public service, public financial management (PFM), the justice sector and oversight institutions such as the Attorney General's Office and supreme audit institution.[16]

Nonetheless, the legacy of earlier one-party rule still vests significant power in the ruling party, Frelimo, which continues to dominate the state bureaucracy. The executive dominates other branches of the state – the legislature and judiciary. In the context of a weak parliament and civil society, accountability tends to be skewed toward donors as aid flows to the budget are significant. This trend is sometimes reinforced if donors, particularly from Northern Europe, face strong parliamentary pressure at home to account for how aid money is used[17] and focus their attention on managing fiduciary risk. Political and business élites in Mozambique are closely linked with each other and with the ruling party, binding their fates together and creating strong incentives against both greater transparency and more effective formal accountability mechanisms.

16 The Administrative Tribunal.

17 For example in the case of Danish support to the Zambezia education sector, discussed below.

Meanwhile in *Indonesia*, the Asian financial crisis of 1997-8 exposed the underlying weaknesses in governance that had coexisted with economic and social progress. The first democratic elections in over 40 years took place in 1999. During the subsequent *reformasi* period, a new Constitution established formal checks and balances and civil society was given greater freedom.

President Yudhoyono was elected on an explicit anti-corruption platform in 2004 and, with a small group of reformers and pressure from civil society, has made progress with governance reform. Building on earlier reforms, he rapidly introduced a national anti-corruption action plan that focuses on service delivery, public financial and human resource management, and strengthened law enforcement. Unlike the other cases explored here, Indonesia's Anti-Corruption Commission (KPK) has had the political backing, leadership, capacity and independence, to prosecute cases of corruption successfully[18] and reduce impunity. Reforms to tax and public financial management have also made progress. The dramatic decentralisation of political and economic power to the lowest levels of government following the fall of Soeharto have also begun a process of strengthening accountability for service delivery to citizens at local level. However, civil service and judicial reform have made limited progress while leakages from petroleum and forestry sectors are still significant. Reforms are still needed to deepen horizontal accountability to Parliament and the judiciary, and by strengthening political competition.

Following a brief but severe fall into low-income status after the Asian financial crisis, Indonesia has returned to middle-income status and made improvements to governance despite limited reform capacity, weak formal institutions and strong vested interests. A strong civil society may maintain the momentum against the resurgence of vested interests and deepen reform. Although Indonesia is not aid dependent, it is of strategic and commercial importance to several donor countries, not least as the largest Islamic country, developing East Asia's second largest economy, and a land rich in natural resources.

In *Afghanistan*, following the ousting of the Taliban in 2001, immediate priority was given to peace-building and introduction of a formal democracy; improving security; and re-establishing systems of state administration and service delivery based around a strong central government. Presidential and parliamentary elections were held in 2004 and 2005, respectively. As in other conflict or post-conflict contexts, the central administration lacked human resource capacity.[19]

Although the government has taken several formal institutional and legal measures to fight corruption, given competing priorities it has not proved able to provide a strong lead in this area. The formal measures do not appear to have had tangible impact; they do not have sufficient political support and are increasingly perceived as lacking traction. Some ministries with strong leadership have achieved noticeable results, for example in PFM or health. However, progress has generally been very slow and public administration is permeated with informal patronage networks. Formal accountability institutions are weak and not generally respected by citizens. The National Assembly has begun to exercise some oversight of the executive, although there are allegations of corrupt practices by the executive intended to limit this.

Civil society is weak or aware of the need to protect its position beyond the, perhaps more transient, presence of the international community. Similarly to Mozambique, financial dependence on foreign aid tends to skew executive accountability towards the international community.

In the interests of stability, the Afghan government considered it necessary to compromise with provincial power holders and former warlords; as power struggles and conflict have continued, government has lost control of parts of the country. Ongoing conflict and the huge opium economy[20] undermine efforts to build a rules-based public administration. Informal patterns of accountability prioritise obligations to relatives or religious or political groups.

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18 Supported by the Special Court on Corruption.

19 For example, Cambodia emerged from two decades of conflict in 1998 having lost an entire generation of educated professionals.

20 The opium economy accounts for roughly one-third of the national economy.

1.2 Responses to opportunities and blockages to reform in these contexts

In *Mozambique* government and donors have institutionalised a process of continuous dialogue and negotiation built around the multi-donor budget support instrument and its related architecture (Box 2). The memorandum of under-standing (MoU) and performance assessment framework (PAF) have locked donors into a co-ordinated response. A variable tranche option allows individual donors flexibility to adjust aid disbursements in a predictable way, while maintaining overall dialogue and only marginally affecting aid volumes.

This established architecture and process has generally helped donors to obtain a common understanding of the opportunities and blockages to governance reform. Donors have supported reforms in key governance areas, including PFM, public service reform and the justice sector. These reforms have improved horizontal and vertical accountability, although attempts to improve the legislature have been limited and ineffective. Donors have come to rely more on Mozambican institutions[21] to manage fiduciary risk.

Donors have acted as a hub connecting civil society and government, for example by ensuring that civil society participates in the working groups that underpin the review of government performance. Mechanisms for civil society to influence or participate in decision making have not, however, been formalised.

In *Indonesia* donors responded in three ways to the governance and corruption challenges following the fall of the Soeharto regime. They reinvigorated a World Bank (WB)-led Consultative Group for Indonesia (CGI) as a forum for government-donor dialogue. A new donor-funded Partnership for Governance Reform provided an Indonesian-led vehicle for national dialogue on governance and anti-corruption, support to governance reforms and civil society. Donors also reviewed and updated their analysis and approach to governance, corruption and fiduciary risk in projects and programmes, strengthened their support for key areas of governance reforms – particularly decentralisation and legal and judicial reforms – and brought in technical governance staff to help implement these programmes.

Donors' overall response to governance and corruption has been affected by Indonesia's return to middle-income status. Those donors who are not motivated primarily by strategic and geopolitical concerns face a dilemma about how to continue supporting institutional reform. Corporate priorities drive such donors to concentrate resources in low-income countries, and staffing for governance work in middle-income countries has therefore been reduced. Government focuses its interaction on three principal creditors (the Japan Bank for International Co-operation, Asian Development Bank and World Bank). A smaller grouping of bilaterals interacts indirectly through support for multilateral trust funds and on an ad hoc basis with individual state agencies like the Anti-Corruption Commission.

In *Afghanistan*, the initial priorities of donor countries after the fall of the Taliban were to ensure security and to restore state administration and capacity for service delivery. These priorities crowded out other concerns. Large inflows of international assistance and pressure to spend resources quickly generated new sources of corruption and strengthened old patronage systems, a situation exacerbated by the massive resources employed by participants in the opium economy illicitly to influence or buy off government officials. Donors initially prioritised safeguards to protect development aid from abuse, then began to respond to corruption more widely from 2006. By 2006 survey material and perceptions indicated a dramatic increase in corruption, provoking a series of responses from donors. Corruption is now increasingly acknowledged as a key threat to security, state building and counter-narcotics.

Donors have advocated action against corruption in successive high-level international meetings and annual meetings of the Joint Co-ordination and Monitoring Board (JCMB). In order to accommodate the divergent views of different donor countries and government preferences, these messages and government commitments have tended to be fairly general. Limited progress has been made in identifying concrete benchmarks of reform.

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21 For example, in June 2008 the press reported USD 8 million had been diverted from the National Institute of Social Security (INSS). Donors' response has been to monitor the situation and obtain information from government, but to rely on the Accountant General and Auditor General to resolve the issues.

Donors have supported a range of governance reforms, guided largely by the priorities set out in the Afghanistan Compact. Donors' specific involvement in governance reforms is guided, as in other countries, by their corporate policies and technical skills. Measures to prevent corruption have prioritised PFM. Although efforts have been made to reduce impunity by strengthening justice and police reforms through seconding advisers to the respective institutions, corruption prevention in these sectors is in its infancy. In the absence of a government lead, donors have also established an informal co-ordination group to prepare common policy positions and inputs to donor-government dialogue. Dialogue about policy and monitoring of reform takes place exclusively between donors and government, which do not appear to consider civil society as relevant actors.

In *Cambodia*, donors' efforts to promote a broad-based approach to anti-corruption reforms have made little headway. To improve traction, the multi-donor budget support instrument that commenced in 2007 has a policy matrix limited to three governance areas: PFM, private sector development and natural resource management. Donors do not have a fully harmonised approach to conditionality, but retain flexibility to respond to government performance in different ways. For example, if a critical benchmark is not met, one donor may suspend disbursement until it is. Other donors may determine their level of disbursement based on an overall assessment of performance in the previous period. Donors do not see this instrument as a way to break through entrenched resistance to certain reforms, but to sustain support for complex reform processes to which the government is committed.

1.3 Aid volumes and modalities

It is interesting to view donor responses to corruption in the context of aid volumes and modalities *(Table 1)*.

Table 1.   Aid volumes, dominant aid modalities and most influential donors
(In the case study countries, on the basis of aid volumes)

	ODA	Per capita	% GNI	% budget	Major donors
Mozambique	2000: USD 876 million 2006: USD 1.6 billion 36% is GBS	USD 48 in 2000 and USD 77 in 2006	26.2% in 2006	55.8%*	WB, AfDB, EC provide 37%; 7 N. Europe bilaterals provide 42%
Afghanistan	2000: USD 136 million 2006: USD 3 billion 1/3 through core (GoA-controlled) budget via trust funds managed by WB and UNDP. Remainder "off-budget"/ donor-controlled	USD 57 in 2003/04 and USD 83 in 2005	35.7% in 2006	90%	United States provides 1/3 of aid (all off-budget); Also Canada, N. Europe, Japan, EC, WB, ADB
Indonesia	2000: USD 1.6 billion 2006: USD 1.4 billion 95% is credit	USD 8 USD 6	1.1% 0.4%	90%	5% of gross official aid flows from 3 creditors: ADB, Japan, WB

*Aid 38% and credit 17.8%.
Source: Country case studies.

The volume and modalities affect donor responses to corruption in several ways; donors assess governance and corruption before deciding on the appropriate mix of aid modalities, and they monitor and manage fiduciary risk related to the chosen aid modalities. A donor or group of donors that provides significant aid volumes may be particularly influential in dialogue with partner governments. The dialogue and monitoring structures established around the most significant financial flows from donor governments to recipients tend to be the places where important dialogue takes place concerning governance and corruption.

In *Mozambique* and *Cambodia*, the architecture established for dialogue and monitoring around budget support provides an important platform for donors to respond to corruption, for example at the annual joint review. Not all donors use country systems to the same extent however,[22] and this may require expansion or modification of the budget support architecture to bring other donors into the dialogue. In Mozambique, the G19 group includes 16 bilaterals and 3 multilaterals. This architecture also provides space for non-budget support donors, for example as observers, to ensure that information flows effectively and donor responses can be more consistent with each other, even if they are not identical *(Box 2)*.

In *Afghanistan*, donor contributions to the government budget are mainly provided through trust funds administered by multilateral agencies, like the WB and the United Nations Development Programme (UNDP), with multi-stakeholder boards. A Joint Coordination and Monitoring Board (JCMB), including government, donors and security sector and chaired jointly by government and UNAMA, meets quarterly to oversee and report on progress with the Afghanistan Compact. Until recently, the United States, which provides one-third of aid but most off-budget, often carried out dialogue with government on corruption-related issues through bilateral channels, although there is now evidence of greater co-ordination.

In *Indonesia*, there is no longer a high-level forum for all donors to discuss policy and governance reform with government, following the demise of the CGI. However, dialogue does take place between the Ministry of Finance and the three large creditors (the World Bank, Japan Bank for International Co-operation and Asian Development Bank), who monitor public financial management, customs and tax reform. A smaller grouping of bilaterals interacts indirectly with government through support for multilateral trust funds and on an *ad hoc* basis with individual state agencies like the anti-corruption commission. Most donors have not felt the need for formal or informal co-ordination mechanisms; no one donor has been prepared to take the lead and until very recently, government has not seen a need for this. However, the situation may be changing. As a signatory to the Paris Declaration, Indonesia recently also set out plans for a new framework of dialogue with various stakeholders, including donors, the private sector, global funds and other new actors such as the Gates Foundation. The new initiative, entitled "Jakarta Commitments: Aid for Development Effectiveness" is aimed at strengthening country ownership of development, delivering and accounting for development results, and building more effective partnerships. The framework draws on the experience from the Multidonor Trust Fund established for Aceh-Nias following the tsunami. Smaller bilaterals have welcomed this as an opportunity to encourage government to take the lead in aid co-ordination and take a broader view of the governance agenda. The government also intends to require donors to put all donor funds through the national budget, and to use national systems for procurement.

In some highly aid-dependent contexts, financial dependence may appear to make partner governments, at least formally, more accountable to donors than to their own citizens. It can also distort performance monitoring if partner government officials feel pressure to accept indicators they do not own or cannot fulfil due to capacity constraints, in order to access funds.[23] However, the picture is complicated by informal patterns of accountability in partner countries. Politicians and factions within partner country governments are often situated within complex webs of patronage that they must manage effectively to remain in power (Cammack, 2007), limiting checks and balances against the executive. These patronage systems have their own flows of financial resources, which may dwarf,

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22 For a discussion of donors' guidance and incentives for using country PFM systems, see the "Report on the use of country systems in PFM" for the Working Party on Aid Effectiveness – Joint Venture on PFM (OECD 2008). This found that some donors (such as the MDBs, DFID and SIDA) consider the use of country systems to be the default operational policy. Others (*e.g.* the United States) see it as exceptional rather than routine.

23 This emerged in the Uganda water sector, analysed for this study. A similar situation arose in Niger (Hayes and Pereira, 2008).

compete[24] with or even be nourished by aid flows. These systems generate alternative patterns of accountability that cut across or run parallel to accountability to donors and other formal institutions.

2. Assessing governance and corruption as a basis for responses

This section looks at the kinds of evidence donors have used in the past as a basis for responding to corruption, and how they have used it in the case study countries. While considerable work has been done in recent years to establish good practice in assessment (OECD DAC GOVNET, 2009b), this study records the *methods actually used by donors* in case study countries with respect to corruption, which may not yet reflect emerging good practice.

The case studies and key informant interviews indicated that donors have reviewed or carried out assessments of governance and corruption at various stages[25] in the planning and delivery of country programmes where different types of responses occur *(Figure 1)*, Such stages include, for example, when designing country strategy and the relevant mix of aid modalities; when determining which types of reform programmes to support or monitor as a priority; and when monitoring delivery of reform and impact of reform as a basis for confirming or altering future support.

2.1 General assessment material

International surveys and indicators were widely used by donors in the case studies in forming an overall view of governance and corruption. For example the World Bank (WB) Country Policy and Institutional Assessment (CPIA) was mentioned by donors interviewed in Mozambique and Indonesia. Other international data sets referred to by donors, which locate the case study countries in cross-country comparisons, include Global Integrity in Indonesia and Mozambique and the regional Ibrahim Index and Africa Peer Review Mechanism[26] in Mozambique. The effect of corruption on doing business is surveyed in Investment Climate Assessments in Afghanistan and Indonesia, and the WB's ease of doing business index and the World Economic Forum's Global Competitiveness Report in Indonesia.[27] In all case study countries interviewees from donor agencies referred to Transparency International's Corruption Perceptions Index (CPI). Although tools for and methodologies of governance assessment have proliferated in recent years, and the way donors use the CPI has been criticised,[28] it is often still valued by donors for providing a snapshot of perceptions of corruption and how these change over time. Although it is not an appropriate tool for measuring progress in anti-corruption reform, some donors do still use it for this purpose. The CPI methodology may also often be challenged by partner governments if they dislike or disagree with the perceptions of corruption that the CPI score records. Recent research indicates that external or donor assessments cannot be used to drive dialogue in partner countries or between donors and partner governments in the same way as nationally driven and peer-based assessments (OECD DAC GOVNET, 2009b).

Donors have also drawn on perception surveys produced by local NGOs, although availability varies. In Afghanistan, government and the international community have only begun to generate knowledge and data locally[29] about corruption since 2006,[30] there are logistical difficulties in conducting surveys due to security. In Mozambique, the first national survey[31] on corruption was carried out in 2001, and studies of corruption in key sectors[32] in 2006. In Indonesia, the Partnership for Governance Reform carried out a national survey on corruption in 2001 (PGRI, 2001), and TI Indonesia and other NGOs carry out periodic surveys.

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24 In Afghanistan, the opium economy is estimated to account for roughly one-third of the national economy. The drugs trade is linked to a complex pyramid of state protection and patronage, with a web stretching across government ministries and into the National Assembly.

25 Recent research into governance assessments indicates that they broadly serve three different sets of purposes: those related to donor decisions and concerns; to general donor-partner co-operation; and to promotion of or support for governance reform in partner countries. (OECD DAC GOVNET, 2009b).

26 Although the APRM process is still under way in Mozambique.

27 Mozambique is also covered by both the doing business index and GCR, although donors did not refer to these in case study interviews.

28 For a critique of the way the CPI has been (mis)used by donors for aid allocation and year-to-year performance measurement, see Arndt and Oman, 2006.

29 Arndt and Oman (2006) point to the way indicators suit the needs of different users, and local stakeholders need indicators that will enable them to target and monitor reforms precisely.

30 The Afghan NGO Integrity Watch Afghanistan produced a comprehensive perceptions survey covering 13 of 34 provinces in 2006 and a study on local views of forms, causes and consequences of corruption.

31 The Etica Mozambique perceptions survey, which focused on three provinces out of ten.

32 The Centre for Public Integrity (CIP) carried out surveys of corruption in the education, health and justice sectors.

Donor support can be critical to ensuring research institutes and other NGOs have the capacity and funding to produce survey material. As material from different perspectives is produced, it can provide a more comprehensive and differentiated picture than was previously available. However, an increase in availability of information about corruption can often complicate analysis of trends, giving the impression that corruption has increased even if that is not the case. This can contribute to shifting attitudes and less tolerance of previously accepted behaviour, creating demand for reform in society and among donors.

Different donors[33] have commissioned further surveys and assessments for a variety of specific purposes in the case study countries. For example, several donors in Afghanistan have produced "Corruption Vulnerability Assessments" for different ministerial departments and sectors. In Mozambique USAID commissioned independent consultants to carry out a corruption assessment to inform its country strategy in 2005, the Netherlands commissioned an SGACA in 2008. In Indonesia, the Asian Development Bank (ADB, 2004) and WB (2004) produced analytical work in 2004. The latter improved understanding of issues of governance and corruption among donors and officials as it was shared with staff at the supreme audit institution and anti-corruption commission. Donors have also subsequently carried out several separate assessments of governance and corruption. For example the Netherlands produced a SGACA in 2006, USAID completed a Democracy and Governance Assessment in 2008 and the WB commissioned a review of government corruption policies in 2006.

In the country case studies and key informant interviews it was clear that particular attention has been paid to indicators of quality and improvement in PFM systems. This information is considered vital to donors' assessment of fiduciary risk, and to determining the extent to which aid is channelled through government financial management systems and whether additional safeguards are required. In Mozambique, the Report of the State General Account on budget execution has become an important source of information as its quality has improved in the wake of PFM reforms. Public Expenditure and Financial Accountability (PEFA) methodology has been used in all case study countries. In Afghanistan, PEFA assessments carried out in 2005 and 2008 show significant progress. In Mozambique donors and government agreed to use PEFA methodology: PEFA indicators form part of the performance assessment framework for budget support. Three successive assessments[34] have shown substantial improvements in areas relevant to tackling corruption. By contrast, in Indonesia a PEFA assessment carried out by a team of major donors came to nought as the government did not wish the findings to be made public and had not been persuaded in advance to use the scores generated to measure performance of reforms over time.

Governments have sometimes produced assessments of corruption or worked with donors on assessments in the case study countries. Recent research (OECD DAC GOVNET, 2009b) on governance assessments indicates that the legitimacy of assessment is likely to be enhanced when country officials participate or when assessments are conducted jointly with donors. In Mozambique, the government carried out a national baseline survey of governance and corruption in 2004 with technical support from the World Bank Institute (WBI) and donor funding. Although a complete draft was never published, a version appeared in the press and is now available on an NGO website. It is considered a credible survey, regularly referred to by donors and NGOs. By contrast, in Afghanistan the government produced the *Azimi Report*, a comprehensive review of the forms and causes of corruption, with a strategy to respond to this analysis. However it is not yet clear how the analysis will be used by donors as it has not been integrated with the Anti-corruption Strategy contained in the Afghan National Development Strategy (ANDS), which had largely been produced by an international consultant working with local stakeholders.

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33 For a review of different donors' governance perspectives, tools and methodologies, see OECD DAC GOVNET, 2009b.

34 PEFA assessments in 2004, 2005 and 2006 showed improvements, for example, in financial reporting, quality of auditing, availability of information and procurement.

2.2 Responses to evidence of corruption and stagnating or deteriorating governance trends in assessments

Corruption assessments such as perception surveys and other governance assessments have been used[35] by donors in case study countries and elsewhere as a baseline for subsequent monitoring of the trajectory of governance change. They have been used to identify areas where it is important to support reform or to raise awareness of corruption. They are used in addition to public financial management assessments to assess fiduciary risk.

In light of this evidence donors build up a picture of current practices and perceptions of corruption, and the expected trajectory of change. They respond by deciding which mix of aid modalities to use and the degree to which additional safeguards are needed to manage fiduciary risk. If additional evidence comes to light that changes the picture of current corruption or the trajectory of change, donors sometimes feel the need for an additional or different response, or even a change in the nature of engagement. Sometimes more general evidence of corruption stimulates donors to conduct additional reviews in projects or programmes they control before they respond.

In *Afghanistan* an increase in the volume of survey material, media reports and anecdotal evidence from 2006 onwards was a stimulus to donors to improve their responses to corruption. Prior to this, greater priority had been given to the state-building and reconstruction agenda, but there has subsequently been a series of high-level statements on the need to tackle corruption and a greater focus on anti-corruption analysis and programming. In 2006 the WB took the lead by voicing concerns about corruption at the *London Conference*.[36] Several donors advocated concrete anti-corruption benchmarks for inclusion in the Afghanistan Compact, although it was finally agreed that a higher-level benchmark concerning introduction of UNCAC should be included.

Meanwhile, two agencies began to develop their first "anti-corruption" project. Nine donors and multilateral banks formed a technical working group to co-ordinate anti-corruption work and policy positions. Since that time, donors have initiated and supported an increasing amount of explicit anti-corruption work. Some has targeted prevention and analysis of vulnerabilities to corruption in different sectors and ministries. A few donors have focused specifically on law enforcement seconding technical advisers to justice institutions and the Attorney General's Office. There has been (limited) support to civil society watchdog functions. This range of programmatic responses, though anchored in government reforms, has reflected the anti-corruption approaches and mandates of different parts of donor governments with respect to emphasis on prevention or sanction. An integrated approach focusing on systematic corruption prevention in all core governance and sector reforms has not yet been taken. Also, the anti-corruption approaches have as yet to place greater emphasis on the links between corruption and the opium industry – for example linking anti-corruption work to counter-narcotics efforts, specifically with regard to police reform and at the Ministry of the Interior.

Donors' response to corruption in *Afghanistan* has affected their choice of aid modalities. On the one hand donors have faced the challenge of spending large amounts of aid rapidly and effectively, and are prepared to use government systems while monitoring PFM reform. On the other hand two-thirds of the USD 3 billion in aid to Afghanistan is still off-budget.[37] The main reasons cited by other donors for not using Afghan PFM systems to a greater extent include lack of confidence in the systems, limited absorptive capacity, and associated corruption.

Likewise in *Indonesia*, most bilateral donors (apart from Japan) do not provide budget support due to concerns about fiduciary risk. This trend is reinforced as bilaterals are not part of the agreements between government and the World Bank and ADB on reforms and performance monitoring around their development policy loans. These loans are, though, helping to strengthen country systems, and there is evidence of progress in several areas of PFM. This is likely to facilitate greater use of country systems by donors over time.

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35 See OECD DAC GOVNET, 2009b for analysis of the different purposes for which donors use assessments.

36 This was a high level international conference organised to discuss support to Afghanistan.

37 Although the largest donor, providing one-third of aid – the United States – has a general policy of not using government systems to provide aid.

In *Mozambique*, the study carried out by consultants to inform USAID country strategy *(see above)* was highly critical of government. It included allegations of state capture by criminal networks and linked part of the ruling élite with organised crime. It highlighted corruption in the judiciary and service delivery. It also scrutinised donor approaches to corruption and concluded that despite reviews, particularly of PFM, and strong statements condemning corruption, donors had not successfully influenced government to take serious measures to tackle it. Although many of the findings were not considered new, the tone of the report was particularly strong. USAID sent the draft report to government, which never commented formally. In a context of strong development dialogue and confidence in development outcomes, donors were divided as to how to respond to the report. Some favoured using the evidence in dialogue with government; others were more concerned that doing so could undermine existing cordial dialogue. In the end, although there was some discussion of the findings among donors and with civil society, the report was not used in dialogue with government by a group of donors or the United States.

Also in Mozambique, there have been instances where a single donor country has carried out different assessments, leading to a mixed response, or where different donors have carried out assessments in parallel and each responded in line with their own assessment. At the same time as the critical USAID study was being prepared, the US Embassy was co-ordinating a parallel process that led to Mozambique's subsequent qualification as a threshold country for the Millennium Challenge Account. In Mozambique in 2006 a modification to international data used to inform the World Bank CPIA – which determines aid allocations – led the WB to reduce funding. In the same period the EU increased funding in response to a governance assessment that showed a positive trend. In 2007 the WB CPIA governance indicators improved, but other donors who were monitoring governance via the PAF decided to reduce their budget support.

2.3 Monitoring of governance and anti-corruption reform programmes

Many of the donors operating in the case study countries have policies that implicitly or explicitly view corruption as a symptom of weak governance. They assess the progress of a range of different reform programmes that are expected to improve governance and reduce corruption. These reform programmes are sometimes collated or targeted as part of a national anti-corruption strategy. Sometimes donors monitor reforms aiming to address corruption in a sector.

For example, among donors present in *Mozambique*, a review of corporate policies suggests that these converge around definitions similar to corruption as a symptom of weak governance (WB, USAID, Denmark, UNDP): weakness in national and global governance systems (DFID); the result of a weak state, a weak public administration and weak media (SIDA); result of bad governance (Netherlands); symptom of poor governance and lack of transparent, accountable management and control systems (EC).

The PAF for multi-donor budget support in Mozambique covers areas including PFM, the justice sector, public sector reform, auditing, the financial sector and procurement, all acknowledged (for example GoM and PAPs, 2007) by government and donors as important in the battle against corruption. The Mozambican Anti-Corruption Strategy (A-CS) adopts a comprehensive approach comprising preventive and punitive measures, some building on existing reform programmes. Some of the activities in the A-CS are also covered by PAF indicators. The A-CS has five sector plans for education, health, justice, finance and the interior. The PAF and A-CS are monitored at the annual and mid-year joint reviews and between times, in 29 thematic working groups. This is similar to a number of other budget support contexts in Africa, where donors monitor the PAF and also progress on a separate anti-corruption strategy.

In *Mozambique* donors combine information from their own and external assessments, with information from PAF indicators to assess progress in tackling corruption. For example, the Netherlands combines budget support joint review reports, the CPIA and its own diagnostic tool, the Strategic Governance and Corruption Analysis (SGACA). DFID uses joint review reports, NGO reports and its own tool, the Country Governance Assessment (CGA).

In *Afghanistan* a variety of government policy documents, particularly those prepared with a great deal of donor input, conceive corruption as a symptom of poor governance. Programmatic responses prescribed in these policies include technical measures to improve public sector management, public integrity, law enforcement, counter-narcotics, awareness raising and political accountability.

However, there are several competing anti-corruption analyses and strategies in place. Only one of these, the *Azimi Report*, is genuinely government owned. This complicates the picture for monitoring purposes. In 2006, the JCMB required the government and the international community jointly to commission a comprehensive anti-corruption strategy as part of preparation of the ANDS. In parallel the president had commissioned the *Azimi Report*, which was produced over a period of two years. The government stresses it is a purely Afghan document with no international contributions. In 2008, following a recommendation of the *Azimi Report*, the government drafted a new anti-corruption law to replace the anti-corruption commission, GIACC, and set up a new institution to oversee implementation of the *Azimi Report*.

In *Indonesia*, President Yudhoyono signalled his commitment to tackling corruption soon after taking office in 2004. He issued a Presidential Instruction, sending a message to the bureaucracy, and followed up with a National Action Plan (RAN-PK) with three components for prevention, repression and monitoring. Monitoring and evaluation of RAN-PK was assigned to the ministry responsible for administrative reforms (Menpan) and the national planning agency (Bappenas). Six-monthly reports were envisaged and progress was to be judged by changes in the TI CPI rating. In fact, Bappenas' role in the monitoring was not clear and Menpan lacks capacity and political influence. Government has provided a strong lead to the governance reform programme, but in 2007 it dissolved the previous Consultative Group for Indonesia (CGI) framework. Under the CGI, thematic multi-stakeholder working groups had served donors as a means to monitor progress on reforms, including governance and anti-corruption, legal and judicial reforms and decentralisation.

In general, the demise of the CGI has left a void in the co-ordination of monitoring of different reform programmes within government and for donors. This in turn contributes to *ad hoc* donor responses to governance challenges. Now there is no government agency systematically attempting to discern links between the needs of different governance-related agencies. (Bappenas is beginning to take steps to fill this void in anticipation of the next medium-term develop-ment plan and as a follow-up to the Accra Agenda for Action.) Currently, neither government nor donors are carrying out analytical work on governance in sectors or provinces. The KPK chairs three or four meetings a year for donors, but these are largely for information exchange. Without co-ordination, donors undertake their own governance and corruption assessments. Progress with PFM, customs and tax reforms is still monitored via benchmarks set through WB and ADB analytical work, and WB reports indicate that progress is steady, although it has not yet been possible to use quantitative PEFA indicators as government did not fully own the process.

2.4 Responses when performance indicators/other observations show that reforms are not progressing or performance is deteriorating

Although donors have similar definitions of corruption and sometimes a common framework to monitor a range of governance and anti-corruption reforms, in practice donors have different corporate interpretations as to how to address corruption while achieving other development goals. These differences become evident when the trajectory of governance change is perceived to stagnate or deteriorate, provoking donors to respond.

In *Mozambique* lack of information about progress in the sector activities identified under the A-CS has made some donors sceptical about the effectiveness of the strategy and commitment to implement it. As explained above, donors' view on the trajectory of governance change is based on the PAF and multiple other assessments. A review of this combination of evidence in 2007 has led Sweden and Switzerland to respond by reducing their budget support (variable tranche), but other donors have not responded in the same way. This response reflected the assessment approach of each country and their corporate policies for responding to corruption and deteriorat-ing governance. Following these responses, action has been taken by government to arrest two senior figures on

corruption charges – although it is not clear if this action is related to donors' stronger message at the joint review and/or reductions in budget support.

In another budget support context in Africa, key informant interviews indicated that donors were sceptical about the quality and credibility of the government's anti-corruption strategy. This created uncertainty among donors about the trajectory of reforms to address corruption. When information then became public about a large diversion of funds from a state institution, this increased some donors' desire to respond by altering budget support disbursements.

In *Afghanistan*, government policies to address corruption and proposed technical responses were developed over a year and a half ago with donor inputs, but donors perceive little progress in government taking the work forward. This is complicated by the existence of different analyses and strategies in circulation: the ANDS and the *Azimi Report*. The clearest signs of action have been on PFM, which is deemed to prevent corruption, and in simplification of administrative procedures to reduce the scope for corruption. However, donors perceive other actions by government as unlikely to have impact as the government institutions involved lack capacity, credibility and political support. This lack of tangible evidence of action to address corruption provoked a series of responses from some donors as follows.

Early actions by the government to address corruption included establishing an anti-corruption commission (GIACC) and signing UNCAC. Donors, however, consider that the GIACC lacks political support and institutional capacity. In early 2007, President Karzai appointed a new head of the GIACC who lacked credibility with donors.[38] Ten donors responded by sending a joint letter rejecting the appointment and calling for action on measures included in the Roadmap produced by donors and adopted as a government document (WB, ADB, DFID, UNDP, UNODC, 2007). Although President Karzai pledged to change the appointment this did not happen.

Apart from the quarterly meeting of the JCMB, since the new GIACC head was appointed in 2007, there has not been a regular forum for dialogue with government on anti-corruption or a clear, politically mandated and credible government counterpart as an ongoing interlocutor with donors. Corruption has been raised at high-level meetings but messages have often been softened to ensure that a range of donors and government accept them. At the Paris Conference in June 2008, individual donors raised the issue of corruption publicly as a threat to other efforts towards development and stabilisation in Afghanistan. Ultimately they were unable to reach agreement with government on a strong joint public message. Moreover, the credibility of donor messages was weakened as government took the opportunity to highlight lack of transparency and accountability in how donors have managed their off-budget aid in Afghanistan.

In *Cambodia* several donors focused considerable staff and political resources on ensuring the passage of an international-standard anti-corruption law, as a key measure of government action to tackle corruption. However, donors have also come to recognise that action is required on multiple fronts to tackle corruption. Some donors have responded to the challenges of improving governance in Cambodia by focusing the budget support instrument around a limited number of critical governance reforms to PFM, private sector development and natural resources – areas where there is a measure of country leadership.

In *Indonesia*, although there has been significant progress in governance reform in several areas (*e.g.* constitutional reforms and decentralisation), general assessment work by donors has highlighted that justice sector and civil service reforms outside the Ministry of Finance and KPK have been slow. Leakages of revenues from oil and forestry sectors are significant. Anti-corruption efforts are limited outside the capital. KPK and other government agencies in the business of fighting corruption have limited capacity outside Jakarta despite the fact that financial powers have been substantially decentralised. Horizontal accountability is limited also, due to a weak Parliament and a dysfunctional judiciary. Election finance and political party reforms are also needed to tackle some important causes of corruption.

With the demise of the CGI, and because government has lacked capacity to put together an overall governance strategy to which donors could align, donors' responses to the situation tend to be *ad hoc*. Nonetheless, donors are providing niche support to specific areas that may address causes of corruption and may be sensitive for government

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38 He had been convicted of drug trafficking in the United States.

to address. For example, efforts are under way to establish the Extractive Industries Transparency Initiative (EITI) in Indonesia to enhance transparency in the management of oil, gas and mining. WB and DFID are working jointly on a scoping study to help government determine how to engage. Meanwhile the Netherlands is supporting dialogue among political parties on party reform through an arm's-length relationship with the Netherlands Institute for Multi-Party Democracy.

3. Responses to allegations or evidence of corruption emerging in sectors or donor-controlled projects or programmes

During the *reformasi* period in *Indonesia*, civil society and many new leaders viewed the larger donors and financial institutions as complicit in the corruption that prevailed during the Soeharto years. Attention was focused on corruption in donor-funded projects – for example, a leaked WB staff memorandum estimated that 20-30% of WB funds did not reach beneficiaries. Donors realised they needed to take and be seen to take corruption risk in their projects more seriously. They responded in several ways: with programmatic responses, reassessment of fiduciary risk[39] and necessary safeguards, and increasing governance advisory capacity to their offices. They revisited their country partnership strategies to strengthen support for governance and anti-corruption reforms, notably regarding citizen participation and oversight, and to better manage fiduciary and reputational risk.

For example, the World Bank stopped all new operations for one year and revisited its country strategy, resulting in a greater focus on community-led development programmes, and an effort to shift accountability from state to citizens rather than to donors in all programmes. More emphasis was given to greater information and transparency to facilitate civil society oversight. A review of WB projects highlighted collusion, poor contract management, delays and poor quality in audits. The WB responded (according to its standard procedures) by demanding repayment from the borrower. Meanwhile the ADB strengthened fiduciary oversight, and other donors managed risk largely by directly implementing their own programmes (Japan) or relying on the international financial institutions (IFIs) or UNDP to manage their programmes.

In *Mozambique* in 2005, there was an allegation that money had been diverted from an education sector project in the province of Zambezia, funded by the Danish government, through Danida. A joint steering committee – comprising the Ministry of Education, the Internal Audit function of the Ministry of Finance, the Auditor General and the Danish Embassy – was set up to deal with this case, and hired an audit firm to carry out a forensic audit. The audit was delayed, and meanwhile the story appeared in the press in Denmark. The Danish Ministry of Development urged the Danish Embassy to take action. The Embassy responded by freezing all funding to the new activities of the education sector, and reviewing all projects in which it was involved with other development partners. It also introduced a new disbursement modality of quarterly tranches, to be accounted for before a further disbursement was made. The Danish Embassy also froze 75% of its contribution to general budget support pending reimbursement of funds diverted. There was further bilateral political dialogue between the Danish Development Minister and the Mozambican Prime Minister on a visit to Denmark, leading to a commitment by the government of Mozambique to resolve the issue. Once funds were repaid (GBP 2.4 million, representing the leakage and undocumented funds), Danish general budget support and funding to the sector resumed.

Other donors had been informally briefed prior to the Danish decision to freeze general budget support, but there was no formal consultation or agreement with them. At the 2006 mid-year review donors made statements similar to previous joint reviews concerning limited progress with implementation of the A-CS and in support of other prevention measures. Other donors raised concerns informally about Denmark's response of freezing budget support without a formal agreement with donors and considered that Denmark, to some extent, had not operated within the parameters of the Memorandum of Understanding.[40] The MoU does accord donors the right unilaterally or jointly to withhold disbursements or claim repayment in the event of misuse or fraud, but it requires consultation with the budget support group before any individual donor suspends budget support (Mokoro, 2008). In this instance Denmark followed its

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39 Although only a very limited number of donors were providing budget support.

40 In general an MoU is not a legally binding document. However, there are bilateral agreements between donor government and recipient government that cover circumstances in which donors may exercise unilateral discretion to suspend aid, investigate, and require funds to be repaid.

corporate policy on the appropriate response of investigation and seeking reimbursement, and exercised its right to withhold disbursements in light of its bilateral agreement with the government of Mozambique.

With Uganda there is an example of a similar situation with different responses. In 2004, an external audit[41] of Swedish support to the water sector showed serious deficiencies in reporting and financial management, and indicated that SIDA funds had been mismanaged. SIDA and two other donors funding the sector then required the Directorate for Water Development to commission a more in-depth audit, although the auditors were impeded from doing their work and the findings were not considered sufficiently robust to justify repayment. A further audit meanwhile found mismanagement in other donor support to the sector. The weight of evidence from the different audits combined to present a persuasive picture of corruption in the sector.

Donors responded in different ways. While SIDA suspended disbursements, other donors increased their contributions – out of concern to minimise impact on service users, and as they were under pressure from their headquarters to meet spending commitments. In accordance with corporate policy, SIDA demanded repayment of mismanaged funds and that sanctions required under Ugandan procedures be applied. Donors could not agree on a joint statement for the annual sector review and there was intense discussion between bilateral donors at the political level. In order to resolve this discord, a wide range of multilateral and bilateral donors agreed to convene a two-day retreat on corruption. This led to agreement on a common approach that included priorities for programming to tackle corruption in the sector, for future information sharing about disbursements and for monitoring. Anti-corruption figured more prominently in the design of the next phase of sector support.

In *Afghanistan*, approximately two-thirds of the USD 3 billion in aid is off-budget. Although allegations have not been substantiated, there are perceptions[42] of corruption in the "external budget" controlled by donors. Many Afghans consider high pay for consultants and advisors and high overheads for NGOs to be a form of corruption (WB, ADB, DFID, UNDP, UNODC, 2007; IWA, 2008). The Afghan government is also concerned about value for money in aid resources channelled outside the budget (WB/ARTF, 2008). CSOs have called for the government to establish a "double compact" with citizens and the international community against corruption and weak accountability in development aid. A group of donors committed to a donor transparency and integrity initiative have also called for payments to consultants and expatriate government officials to be made more transparent. At the Paris Conference in June 2008, donors responded by committing to increase aid effectiveness, including providing more transparent and accountable assistance.

4. Responses to allegations of diversion of funds from government systems in countries where donors are providing general budget support

A succession of events in the 1990s put corruption at the top of the agenda in donor-government dialogue in *Mozambique*. Particular focus was on scandals in the country's banking system following privatisation of two state-owned banks that were technically bankrupt. The government remained a shareholder. Continued poor management, including discretionary lending to people with links to the ruling élite, put recoverability of the banks' loan books at risk and endangered the Mozambican financial system in 2000. The government intervened to recapitalise the Banco Austral, one of the two banks. Subsequent leaks indicated that donor funds had allegedly been used to fund privatisation. A journalist, Carlos Cardoso, followed the story[43] closely but was killed in November 2000. Moreover, in an attempt to recover other non-performing loans to the Banco Austral, the government appointed a respected Central Bank economist, Siba-Siba Macuacua, who published a list of debtors in the newspaper. He was also killed, in August 2001. An independent researcher subsequently published research criticising donors' lenience with respect to these allegations of corruption (Hanlon, 2002). A group of donors subsequently commissioned an independent audit of government loans that had allegedly been used to fund the privatisation. The report highlighted non-repayment of loans and poor government controls.

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41 The audit was undertaken as part of standard procedures required by HQ.

42 A recent survey found that 64% of respondents thought that there is corruption in aid; of those, 60% estimated that 40% of aid money is lost in corruption (IWA, 2008).

43 Cardoso questioned a loan from an import support mechanism funded by donors, made to a businessman who purchased one of the banks.

After the death of Macuacua, the seven donors who were providing general budget support (GBS) had high-level meetings with government to obtain a better understanding of the government's position on the issue of Banco Austral. Since the government was not signalling its position clearly, at the end of the 2002 Joint Review the GBS donors decided to withhold budget support. The GoM tried to negotiate with other donors not involved in GBS to contain the GBS group approach. It became clear to the donors that to be effective in dealing with sensitive situations like the Banco Austral case, they needed to adopt more co-ordinated responses as well as dialogue mechanisms (including with the government). Subsequent discussions led to the decision to design a mechanism for more co-ordinated responses, and this contributed significantly to the design of the current aid architecture in Mozambique *(Box 2)*.

Under the new framework, the forensic audit of the Banco Austral was included in the PAF as a performance indicator and monitored in joint annual and mid-year reviews. After many delays the audit was completed in January 2006 and sent to the Attorney General's Office for judicial follow-up, but is has never been published. The issue was withdrawn from the PAF but is still monitored through political dialogue. However, other reforms relating to state withdrawal from banks and improved regulation were included in the PAF.

Box 2.   **Architecture for performance monitoring and responses involving aid –**
The case of Mozambique

The Memorandum of Understanding comprises a common performance assessment framework (PAF) composed of GoM priorities and targets in the areas of governance, financial system reform, and priority sectors for poverty reduction. The PAF orients dialogue on priorities and performance between GoM and Programme Aid Partners (PAPs). It also includes targets and indicators in the above-mentioned areas for the succeeding two years. Assessment of government performance is carried out in the annual joint reviews, normally in March/April, covering the activities of the previous year. For this exercise the GoM has to provide all relevant documents and information, such as budgets, plans and execution reports, taking into account the agreed indicators. Donors provide information on resource commitments, the schedule for disbursement and information on the assessment of their performance, taking into account indicators related to harmonisation, alignment and aid predictability.

Section 3 of the GoM-PAPs MoU defines as the underlying principles of governance for the provision of budget support "the GoM's [performance] commitments to peace and to promoting free, credible and democratic political processes, independence of the judiciary, rule of law, human rights, good governance and probity in public life, including the fight against corruption (with reference to commitments in the constitution, NEPAD and international agreements)". Assessment of performance regarding these principles is also part of the agreed PAF indicators – mainly under the governance pillar, which also includes justice sector and anti-corruption activities.

In principle, the violation of an underlying principle is considered to be beyond issues about underperformance as measured against indicators expressed in the PAF matrix. It is "dealt with through consultation and dialogue between PAPs and GoM at the appropriate level for decision-making, at any moment one of the signatories thinks this to be appropriate" (not just within the standard joint review timetable) and the violation may trigger an appropriate response.

The general response mechanism, which is described in Section 7 of the MoU, explicitly links commitments and disbursements for the coming year to past GoM performance as measured through the PAF matrix. The mechanism states that "PAPs may choose between making a single response based on the joint view of performance or a split response, with one part (fixed portion) being based on the joint view of performance and the other part (variable portion) being linked to specific, transparent commitments drawn from the PAF and agreed with GoM".

PAPs with a single response mechanism use the annual reviews to make decisions on the subsequent year's funding within four weeks after the annual review. These commitments are confirmed by 31 August (the mid-year review). Any change between the initial commitment and its confirmation in August can occur only if an underlying principle is violated.

In the case of PAPs with a split response mechanism, the fixed portion is committed as above. The indicative commitments of the variable portion are made within four weeks after the end of the annual review and also confirmed by 31 August. Changes may occur only on the basis of additional information about GoM performance on specific indicators, until the moment of the mid-year review (in August). Again, once commitments are made disbursements can only be changed when there has been a violation of an underlying principle.

Regarding corruption specifically, the MoU states that "in the case of serious deviation or misuse of state budget funds or acts of large-scale corruption by members or structures of GoM, GoM commits to make all due efforts to recover funds thus misused or misappropriated and take appropriate measures. PAPs reserve the right to unilaterally or jointly withhold disbursements or claim repayment in full or in part of funds in the case of misuse or fraud".

The European Commission, Sweden and Switzerland use a split response mechanism. These donors have also fixed and variable portions.

Bilateral agreements have precedence over the MoU (article 2). However, PAPs are required to adjust their agreements in order not to include in "their bilateral agreements any additional conditions or administrative and reporting requirements to those agreed upon in the MoU". In cases where PAPs have specific conditions or administrative or reporting requirements in their bilateral agreements, these are specified in the MoU, more specifically in its Annex 10.

In general terms, these are the parameters guiding the relationship between government and donors, and consequently should be used in responding to corruption situations.

In Mozambique and other budget support contexts reviewed for this study, donors often respond to reports of leakage in line with their corporate policies. This response often entails donors awaiting the outcome of partner government investigation of the leakage and seeking partner government action against the alleged perpetrators. Informally there may be differences among donors over whether to delay or suspend disbursements, and some donors tend to be concerned that this may cause a "domino effect" that reduces overall aid flows and predictability. These discussions tend to intensify and become formal opportunities for joint response approaches – such as the annual joint review of performance, where donors are required to state their disbursements for the subsequent period based on performance. Bilateral political dialogue is often used by individual donors to encourage partner governments to take demonstrable action. Action by partner governments, for example the completion of investigations and arrest of alleged perpetrators of corruption, may be considered by donors as a sign of commitment to address the leakage, allowing disbursements to resume or continue. It is often more challenging for donors to assess overall progress in tackling corruption or the causes and government response to leakage where technical dialogue on corruption is not well connected to the high-level budget support discussions or political dialogue.

In the Uganda water sector case described in the previous section, corruption arising in the sector and donor responses did not affect higher-level budget support or technical discussions on governance and corruption. During this period in Uganda, higher-level dialogue was focused on broader issues of political governance around presidential terms and elections. There was already intense negotiation between donors and government at this higher level about corruption where the focus was on officials' asset declarations.

ANALYSIS OF THE CASE STUDIES

Part II analyses how donors have actually responded in practice to corruption. Part III then summarises the lessons learned from how donors have responded historically and offers recommendations to make responses more effective.

1. Predictability and the protection of development outcomes

Aid architecture requires flexibility to ensure that individual donors can manage fiduciary and reputational risk. Where emphasis is on maintaining the aid partnership, this can limit scope for delivering strong joint messages on corruption.

Principles of aid effectiveness, as embodied in the Paris Declaration 2005 and the Accra Agenda for Action 2008, have been an opportunity and incentive for more joined-up donor responses. Donors sometimes respond to evidence of corruption or deteriorating trends in governance by reducing or reallocating aid. This has the potential to affect donors' commitments to providing particular volumes of aid in a certain way, or time disbursements predictably. The case studies and key informant interviews showed that this possibility was an incentive for donors to ensure that responses to corruption minimise disruption to aid volumes, timing and development dialogue.

This concern for predictability is reinforced by incentives to protect perceived development outcomes. In Mozambique, for example, many donors draw on evidence of improved poverty outcomes to argue that aid volumes and budget support are making an important contribution. Donors in country also feel pressure, including from headquarters, their domestic and international audiences and peers, to portray Mozambique and a number of other multi-donor budget support countries in Africa as relative success stories in terms of poverty reduction and donor co-ordination. The reputational risk associated with leakages from government systems is intensified because all budget support donors are affected. Concerns to reduce development[44] and reputational risk are an incentive for donors to ensure that their responses are joined up in a way that maintains aid flows. When donor country offices face pressure from headquarters to respond to corruption by changing aid disbursements, it is easier to defend spending programmes if they can argue to headquarters that other donors are maintaining a similar response, which is then "joint".

Donors often face a trade-off between ensuring predictability and managing fiduciary risk. When a corruption situation arises, corporate policies or political pressure from parliaments in some donors' home countries may lead them, either individually or in groups, to make a different trade-off. This can be a constraint to joint responses. When individual donors respond, for example by freezing disbursements pending investigation and reimbursement of funds, other donors may compensate or put pressure on the donor not to change disbursements, resulting in mixed messages (as happened in the Uganda water sector case). In highly aid-dependent multi-donor budget support contexts, there are sometimes concerns about a "domino effect" if one influential donor or a critical mass of donors changes disbursements. However there are ways in which individual donors, who are required to respond to domestic parliamentary pressures, can however, do so in a way that would minimise the risk of a domino effect and joint response which would undermine predictability. Donors may minimise this risk to predictability either informally or formally. An example of the informal approach to minimise risk would be Danida freezing budget support in Mozambique while awaiting the outcome of the Zambezia education case, but consulting and keeping other donors informed first. A more formal approach to minimising the risk to predictability (Mozambique, Cambodia) is to adapt the aid architecture specifically to accommodate mixed responses.

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44 In this section, development risk is seen as the risks of not achieving development goals and losing support among donors' domestic constituencies for development work and spending. Reputational risk is seen as the risk that donors are perceived not to be working successfully to achieve development outcomes.

On the one hand, many agreements[45] with partner countries reflect donor policies (MinBuza, 2006; DFID, HMT, FCO 2005; Danida, 2003) that emphasise predictability and lessons on conditionality in line with the Paris Declaration and Accra Agenda for Action. Thus these policies and agreements now set out in advance that corruption[46] may represent a fundamental breach of the partnership. It is formally established in such agreements that this should lead to a graduated response of dialogue and consultations before progressing, if the breach is not addressed, to responses involving delays, reallocation or ultimately suspension of aid disbursements.

On the other hand, aid architecture (in Mozambique and Cambodia, for example) often explicitly provides for individual donors to respond unilaterally to a common set of performance indicators in a pre-agreed fashion, without interrupting overall aid flows. The basis for such a response, procedures for consultation and signalling are clearly set out and agreed in advance with government and other donors, to enhance predictability. In Mozambique some donors (particularly from Northern Europe) face their own domestic parliamentary pressure to respond to corruption by adjusting aid flows. After the 2008 joint review in Mozambique, most donors maintained their level of funding; Sweden and Switzerland announced a reduction of the variable portion of 2009 budget support[47] because of what they perceived as a poor performance as gauged in governance indicators and lack of progress in political dialogue on governance. This follows the procedure established by the MoU.

The emphasis placed by the aid effectiveness agenda on predictability and ownership may nonetheless limit the extent to which donors can deliver strong messages on tackling corruption in the shorter term. In order to manage fiduciary risk effectively, donors also seek tools that can encourage partner governments to address corruption while maintaining predictability and strengthening partner government systems. Different approaches to tackling corruption, which may be regarded as alternatives or complements to modifying aid disbursements, are explored in Section 4.2 below.

2. Co-ordination of dialogue and aid delivery

The dialogue and monitoring structures established around the most significant financial flows from donor governments to partner countries tend to be where important dialogue takes place concerning governance and corruption. In Mozambique and Cambodia, the architecture established for dialogue on and monitoring of budget support provides an important platform for donors to respond to corruption, for example at the annual joint review. In Indonesia, high-level government dialogue currently takes place between the Ministry of Finance and the three remaining large creditors of development policy loans (WB, Japan and ADB) that are monitoring reforms in PFM, customs and tax, although corruption is not a central focus.

When one or a number of donors have a separate dialogue with government, it can be a constraint on joint responses and may generate mixed messages if the donors in question take a different stance with respect to corruption. Until recently, the United States – which does not use government systems to channel aid – often maintained political dialogue on anti-corruption with the government of Afghanistan through bilateral channels, although there is now evidence of greater co-ordination. When budget support donors suspended funding in Mozambique in 2002, that government held separate discussions with non-budget support donors in an attempt to contain budget support donors' stance. That was a catalyst for government and donors agreeing on the need for greater donor co-ordination,[48] and the establishment of mechanisms for future responses and the basis for monitoring performance. This architecture[49] also provides space for non-budget support donors, for example as observers, to ensure that information flows effectively and donor responses can be more consistent with each other, even if they are not identical.

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45 For example MoUs, joint financing agreements.

46 Interpretation of evidence of corruption and the way it represents a fundamental breach can, however, be problematic. See Part III Lesson 4.2.

47 At the time of writing, donors did not believe this would have a "domino effect". For example, Sweden has indicated that Mozambique will continue being the main recipient of Swedish ODA, and a new five-year programme is being prepared.

48 A need made even greater as additional donors were becoming active in providing budget support: numbers rose from six in 2000, to ten in 2002 to nineteen today.

49 Known as the G19: it includes 16 bilaterals and 3 multilaterals as well as non-Budget Support observers.

The emergence of non-traditional donors, such as China,[50] India, Japan and the Arab states, all with different policy objectives and views on co-ordination, is a constraint to joint responses involving traditional and non-traditional donors. It has been argued (Centre for Chinese Studies, 2007; Davies *et al.*, 2008) that the Chinese approach has been well received by heads of state in Africa, for example, as an alternative to the West; that increases these leaders' potential leverage. Moreover, China has generally established its own bilateral relations and funding channels with partner governments rather than participating in joint donor initiatives.[51] In the case of Afghanistan, the study found that India and Japan have pursued a largely bilateral approach in their development assistance. India, with its large-capacity development support, has considerable direct influence in specific ministries or public agencies in Afghanistan. However, it appears that India and Japan have not been present in dialogue on anti-corruption. In Cambodia, the fragmented nature of the administration and the arrival of new donors, including China, India, Korea, Singapore, the Czech Republic and Qatar, will continue to pose co-ordination challenges. In some contexts the way in which non-traditional donors have drawn the attention of partner governments has also been an incentive for OECD donors to co-ordinate with each other in order to maintain dialogue with recipient governments.[52]

In Mozambique there is also a separate EC-government political dialogue mechanism based on the Cotonou Agreement,[53] apart from political dialogue among heads of mission within the budget support framework. This also presents an opportunity for EC countries that are not part of the budget support and observers' framework. Southern European donors appear to find these discussions more useful than budget support discussions at the joint review. Additional dialogue mechanisms may also be an opportunity for different donors and political counterparts to raise similar points in different types of meetings and discussions with partner governments.

A sense of crisis or increasing corruption may be an incentive to improve donor co-ordination and joined-up dialogue with government on corruption. In Afghanistan, signs of a deteriorating corruption situation from surveys and anecdotal evidence incited a group of donors to begin meeting to co-ordinate policy work at the technical level from 2006 on-wards; more donors have joined the group recently. Corruption has increasingly been acknowledged as a key threat to security, state building and counter-narcotics. In Indonesia there was a critical juncture after the fall of Soeharto, when donor support was required for technical assistance and limited budget support but more importantly, to provide a signal to investors of official international support for the new government. Thus an aid co-ordination mechanism was set up in 2001 and was centred around an annual CGI meeting. Bilateral donors saw this as an opportunity to discuss governance issues, but over time government interlocutors became increasingly sceptical of the value of meetings that ultimately did not generate additional aid flows. In 2005, with stability restored and the government-led reform programme well established, government took over chairmanship of the CGI and in 2007 closed it down without donor resistance.[54]

When different parts of a single donor government carry out separate dialogue with government at different levels, that too can be a constraint to joined-up responses to corruption and lead to mixed messages. In Afghanistan, political and technical dialogue on corruption within donor governments has sometimes been disconnected. Increased evidence of corruption has led some donors to conclude that greater political dialogue and focus on this issue is required, but anti-corruption issues are often dealt with by more technical divisions of donor agencies in-country as a development issue. Meanwhile their political colleagues have often been careful to avoid the appearance of political interference.

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50 In 2006 China's African policy paper reiterated its long-standing declared policy of non-interference in internal affairs and respect for national sovereignty (Centre for Chinese Studies (CCS), 2007).

51 The 2007 MOU for transport and energy infrastructure projects in Africa with the WB is an exception; see Davies *et al.*, 2008.

52 Some OECD donors interviewed for this study (in 2008) expressed concern that the presence of non-traditional donors weakens their influence, a concern echoing those in interviews carried out for CCS in 2007.

53 The Cotonou Agreement, or the ACP-EC Partnership Agreement, is a global cooperation agreement between the members of the African, Caribbean and Pacific Group of States and the European Community and its Member States signed on 23 June 2000. The agreement was concluded for a twenty-year period from March 2000 to February 2020.

54 The WB Country Director's press statement said, "[t]he old CGI model – whereby government presented a financing gap, and donors pledged funds to fill it – is no longer relevant to a strong country like Indonesia … Of course it is valuable to maintain a dialogue with the international community on issues relating to access to technology, ideas, capital and trade" (Lateef, 2008). Reference was not made to governance as an issue for dialogue.

Higher-level dialogue mechanisms, for example round budget support as described above, are underpinned by ongoing technical working groups. These represent an opportunity to prepare joint donor messages in high-level meetings such as annual joint reviews of performance, and to reach a common understanding of priority areas for reform. Often there are thematic groups where donors and other stakeholders are co-ordinated round particular areas of governance relevant to tackling corruption. However, where there is no specific formal working group within the aid architecture, mandated to consider corruption or drawing together issues from other thematic groups, this also is a constraint on joined-up responses. In Mozambique, until recently, donors supporting justice reform focused on the judicial system, and donors supporting public sector reform or PFM focus on reforms in these areas that can reduce opportunities for corruption. The technical dialogue in this setting was weak as there was no formal mechanism to monitor cross-cutting measures (although an informal anti-corruption donor group had been established). These circumstances can stimulate an individual donor to respond to corruption based on its own understanding of a particular reform area or its own corporate policies, without wider consultation. From 2007 one donor consistently called on others to identify a shortlist of priority areas for dialogue with government including encouraging sector working groups to engage with the five sectoral anti-corruption action plans. This coordination led to a commitment from government on three priority areas at the 2008 joint annual review, although with limited sector support. With leadership from a couple of donors, the informal "governance platform" group in Mozambique also developed by 2008 into a technical group looking across different service delivery sectors with the aim to present some key expectations to government. In Afghanistan, governance and corruption are discussed in a fragmented way among different working groups of donors and government. There was a cross-cutting thematic group, but the counterpart government institutions had little capacity and no political support making it difficult for donors to engage with a government focal point to deliver a joint response.

However constraints can arise where the quality of dialogue deteriorates. In Mozambique, donors who recently reduced a variable tranche of budget support cited the lack of systematic technical dialogue and deteriorating political dialogue as contributing factors.

3. Government leadership and ownership

Leadership from and ownership by partner governments when it comes to measures to improve governance and fight corruption provide an opportunity for donors to harmonise and align their support for government anti-corruption efforts. This lead may take the form of high-level political support for a reform programme, for example when President Yudhoyono moved quickly after the 2004 election in Indonesia to announce a series of governance and anti-corruption measures. Donors have subsequently co-ordinated their support to governance and anti-corruption work around individual state agencies leading different parts of the reform programme; examples include the anti-corruption commission, KPK, the Supreme Court and Attorney General's Office.

However where the government does not address some significant causes of corruption or effectively lead some reform programmes, this can be a constraint to joined-up donor responses. As outlined above, the Indonesian government ended the CGI arrangement in 2007 and only the major three creditors maintain high-level policy dialogue on governance and corruption issues. This dialogue is restricted to the areas where they have comparative advantage and are supporting reforms: PFM, customs and tax, which nonetheless are important means to address corruption and improve accountability. Government has lacked the capacity to put together an overall governance strategy to which donors could align. Donors' engagement tends to be ad hoc with individual government agencies. Nonetheless, some individual donors have taken the initiative to support reforms in key areas that remain to be addressed, such as political party reform and natural resources.

Donor reliance on formal strategies to tackle governance and corruption that are not owned by governments can also be a constraint to joint responses. Governments have often prepared a formal anti-corruption strategy, frequently under pressure from donors. This may represent an opportunity for donors to harmonise and align their support but, as in Mozambique and Afghanistan, they have often perceived that partner governments lack commitment or the capacity to implement such strategies. If donors disagree as to the reason for non-implementation of

anti-corruption strategies, this can be another constraint. For example, in the Ugandan water sector, some donors perceived that government counterparts were keen to sign up to any action plan that ensured resumed disbursements, but were not committed to reform as they did not own the process. Also in Uganda, donors could not agree on common messages to express concerns about corruption at the water sector annual review.

Taking a more realistic view of the political room for manoeuvre available to governments can provide an opportunity for more joint responses. A group of donors in Cambodia have adapted their approach to support a limited number of reforms with government ownership. The budget support policy matrix includes "critical benchmarks" and "milestones" drawn from the government-owned National Strategic Development Plan. These focus on three areas: PFM, private-sector development, and natural resource management. In adopting this approach, donors took the realistic view that setbacks in reform are inevitable. They viewed the budget support instrument and its associated conditionality not as a way of breaking through resistance to reform, but as a way to sustain complex reform processes to which the government is already committed.

Where government does not provide leadership to the reform process, that can produce the incentive for donors informally to co-ordinate technical dialogue among themselves. For example, in 2006 in Afghanistan, faced with increasing evidence of rampant corruption, an informal donor group on anti-corruption was established by nine donors, including UN agencies, bilaterals and multilaterals. Since then, as donor co-ordination has become more established in Afghanistan and evidence of corruption and its destabilising potential has increased, more donors have joined the group. The work of this group has included co-ordinating their agencies' inputs on anti-corruption into national policy dialogue[55] and producing a discussion paper on anti-corruption reform (WB, ADB, DFID, UNDP, UNODC, 2007). Corporate commitments made by donor headquarters to implement the Paris Declaration were an incentive to co-ordination. However, where influential donors do not join the co-ordination mechanisms,[56] that is a constraint on collective public messages. In Mozambique, in the absence of a formal working group within the budget support aid architecture, donors have also created an informal anti-corruption group led by DFID, to exchange ideas and experiences and influence policy dialogue between donors and government.

Understanding local priorities may represent an opportunity to tackle corruption. Cambodia's government, like Soeharto's in Indonesia in the 1980s, has acted to tackle corruption when it appeared to affect growth and the government's legitimacy adversely. Indonesia's current President, Mr. Yudhoyono, and his economic team have a strong commitment to growth and FDI. They recognise that investor confidence is closely linked to progress in reducing the cost of doing business and improving the investment climate. Meanwhile in Cambodia, international garment investors have lobbied successfully to reduce customs corruption which was eroding profitability.

4. Convergence of some donor policies on governance and corruption

On paper, many donors' corporate policies now recognise corruption as a symptom of weak governance. However, differences in practice tend to represent a constraint to joint responses, as discussed below.

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55 The national policy dialogue took place in formal aid co-ordination structures between government and donors. In 2006 the Afghanistan Compact established a Joint Coordination and Monitoring Board (government, donors, security sector) to oversee and report on progress quarterly. There is also a consultative group and working groups structure where donors and government institutions identify priorities and assess progress.

56 For example, the United States in Afghanistan until recently.

4.1 Multiple assessments [57] of governance and corruption

Separate assessments of governance and corruption by different donors can constitute a constraint to joint responses. In Mozambique, although budget support donors have a common PAF, they supplement this with individual assessments carried out in line with corporate policies and material from local assessments. In Mozambique, successive joint reviews in 2006 and 2007, based on indicators in the PAF, concluded that efforts to tackle corruption are ineffective and donors responded jointly by expressing their concern in formal statements about this at the joint review. However, in 2006 the WB CPIA ratings for Mozambique fell due to a new assessment methodology, resulting in a cut in funding of USD 10 million. In the same year the EC increased funding based on its own positive assessment of governance. Separate qualitative assessments that seek to explore the political economy of corruption can also prove a constraint. Several donors now have their own established methodologies for qualitative assessment, for example Sweden's power analysis, DFID's drivers of change and the Netherlands SGACA, although their findings are shared informally.

Standardised assessment methodologies agreed in advance with other donors and government and owned by governments are sometimes an opportunity for joined-up responses. Performance assessment frameworks based on pre-agreed indicators and benchmarks such as those in Cambodia and Mozambique are an example. PEFA assessments, which have been used in Mozambique and Afghanistan, are also an opportunity for donors jointly to assess progress with PFM and agree on appropriate programmatic responses or adjustments to measures to manage fiduciary risk. By contrast in Indonesia, the three major creditors were unable to use the PEFA assessment as a basis for their support, as the assessment was not fully owned by government.

4.2 Understanding of governance and corruption

Where donor staff lack technical expertise or capacity to understand the causes of corruption and identify appropriate engagement and benchmarks to monitor progress, this can be a constraint to joined-up responses. Often, more generalist governance advisers participate in technical discussions on corruption, and that can make it more difficult for donor representatives to reach a common understanding. For example, in Afghanistan after the election of President Karzai in 2004, donors had small embassies or country offices that had only recently (re)opened and were seriously understaffed. High staff turnover and competing demands on staff time have impeded a deeper understanding of country dynamics and development of institutional memory. Indonesia's return to middle-income status has resulted in many donors reducing staff for governance work. Certain technical skills are necessary to identify the cause and effect of reforms with respect to corruption and so determine whether a response is appropriate. For example, one outcome of successful public financial reforms can be greater transparency so that, paradoxically, more evidence of leakages emerges. Evidence of the advance of reform could have the perverse result that donors believe corruption has increased, unless they have the technical capacity to analyse the information properly.

The skills base of donors' staff may also affect their choice or understanding of corruption indicators, for example leading to over-reliance on well-known international cross-country indicators such as the TI CPI rather than less aggregated, more local, detailed or sectoral indicators if these exist. Donor reliance on the CPI can often provoke criticism from partner governments, as has been the case in Mozambique and Tanzania. In Indonesia, by contrast, the government itself has used the CPI as an indicator.

Donor policies with respect to governance[58] and corruption are constantly evolving, and variations in approaches may arise among different donors operating in the same country context. For example, following widespread consultations on its governance and corruption policy, the World Bank found "the message that perhaps came out most strongly was not 'whether' but 'how' the WBG can stay engaged in countries with weak governance… and a high incidence of corruption, by continuing to provide financial and technical support" (WB, 2007a). In contrast USAID policy states

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57 Recent research has indicated that it is important for donors to identify a clear purpose to drive the choice of assessment tools and processes, including separating governance assessments used for the agency's internal purposes from those intended to influence partner country processes. However, relying on various types of assessments, e.g. indicator-based marking and political economy-informed, approaches, could be usefully combined to ensure that assessments are sensitive to context-specific constraints and opportunities (OECD DAC GOVNET, 2009b).

58 sSee for example a selection of governance definitions used by aid agencies (OECD DAC GOVNET, 2009b).

that where political will is lacking and grand corruption prevalent, emphasis should be placed on diplomatic pressure and donor co-ordination rather than extensive programming to reform state bureaucracies. It argues that "high-level diplomacy, including aid and trade conditionalities, visa policies, denial of safe havens, implementation of global and regional conventions, and public and private policy messages can create powerful incentives for reform." Pursuing technical or bureaucratic reforms in these environments risks "being politically manipulated by corrupt elites or used as window dressing". Support for civil society and public education "may not constitute sufficient levers for altering corrupt elites' incentive structures" (USAID, 2005).

Different donors prioritising different approaches to tackling corruption can be a constraint to joined-up responses. This affects the way donors select reform programmes to support and monitor, and the performance indicators to which they respond. Some donors or divisions of donor agencies prioritise a more preventive approach, while others prioritise enforcement. This may reflect prior and joint analysis of priority areas in line with government and local analysis, but sometimes the emphasis chosen may reflect the influence of different HQ departments or the skills base and priorities of donor staff in country. It can sometimes be difficult to reach agreement among donors on a range of complementary approaches.

For example, emphasis is often placed on justice sector reform, with prosecutions expected to reduce impunity and the numbers of prosecutions taken as an indicator of commitment and impact when tackling corruption. In Afghanistan, UNODC, the United States and the United Kingdom have placed importance in providing technical advisers and mentors to the justice sector and Attorney General's Office as part of overall approaches that emphasise both enforcement and prevention. Among the UN agencies, UNODC is by definition more focused on law enforcement – UNDP pursues a more preventive governance approach. The United Kingdom has pursued both avenues. The United States placed great emphasis on justice reform, with those advisors advocating law enforcement to counter corruption; other USAID officials pursued preventive approaches, although they were not always present in co-ordination. In Indonesia, a successful record of prosecutions by the anti-corruption commission, KPK, is a sign of progress in tackling corruption. In Mozambique, evidence of lack of progress in justice sector reform was one of the factors that led two donors to reduce their variable tranche of budget support for 2008.

On the other hand, different approaches may provide opportunities for donors to consider alternative responses. Lessons learned about conditionality and the emphasis placed on predictability by the Paris Declaration and the AAA have perhaps limited the tools available for donors to convey strong messages on corruption to partner governments. At the same time, anti-corruption policies have begun to focus increasingly on measures to address the global incentive environment[59] to complement other efforts to improve governance. Proponents of these initiatives believe they have considerable potential to deter corruption. For example, the WB-UNODC-sponsored Stolen Asset Recovery Initiative (StAR) argues that "a StAR program that transmits the signal that there is no safe haven for stolen assets will embody a powerful deterrent effect". Referring to the types of money-laundering techniques used by corrupt public officials, StAR argues, "this narrow spectrum … suggests that concentrating efforts on monitoring a specific set of transactions and related institutions might have a significant deterrent effect on corruption leaders" (WB, 2007b). Nonetheless, these are relatively new approaches and their effectiveness has yet to be evaluated.

Literature and some key informant interviews suggest that donors have begun to respond across borders and link responses in country to responses at home – for example, by freezing assets[60] in a donor's home country or a third country, where those assets were obtained through corruption in country. In some circumstances donor countries have worked together, for example to refuse or withdraw visas from members of partner governments facing allegations of corruption. The use of international tools was not a primary focus of this research and little reference was made by interviewees in the country case studies to such approaches apart from the case study of Indonesia, which has requested World Bank assistance to access StAR. The limited reference to such initiatives emerging from these case

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59 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.

60 For an example of UK action in this area, see http://www.dfid.gov.uk/pubs/files/combating-corruption-action-progress.pdf.

studies suggests that international measures such as asset-freezing and mutual legal assistance are at an early stage of adoption by field staff. It also appears that such approaches are often considered more the responsibility of political counterparts than development agencies.

The UN Convention against Corruption (UNCAC) has been seen by donors (at least at headquarters) as a new opportunity to address corruption. It has the potential to act as a framework around which donors could co-ordinate support and monitor progress once adopted by partner governments. In Indonesia for example, as a sign of *reformasi* commitment to bring Indonesian laws gradually towards international standards, UNCAC was signed in December 2003 and ratified in December 2006. The Partnership for Governance Reform has subsequently supported gap analysis of compliance with UNCAC and the drafting of an anti-corruption bill to improve compliance by civil society in partnership with the anti-corruption commission (KPK).

Elsewhere however, there is scepticism among some donors about the genuine traction of UNCAC where governments are less committed to tackling corruption. These doubts may limit the extent to which it can be used as a basis for a response that is not only well co-ordinated but also effective in tackling corruption. In Afghanistan for example, the government signed UNCAC in 2004. During the preparation of the 2006 Afghanistan Compact, some donors advocated inclusion of concrete anti-corruption benchmarks, although government resisted this. A benchmark relating to ratification of UNCAC, introduction of new legislation and a monitoring mechanism was seen as a softer compromise that could accommodate resistance from the government and the concerns of some donors who were less inclined to push for tangible action. There is thus a risk that where governments are not committed to tackling corruption, some measures such as establishment of an anti-corruption commission or introduction of UNCAC, can be seen as an easy benchmark for compliance, while the political limits to implementation go unaddressed. In Cambodia and Mozambique some donors and civil society commentators were also privately sceptical about the usefulness of UNCAC, which would require passage and implementation of legislation in order to be enforceable in country. Passage and enforcement would be at best a lengthy process requiring the co-operation of weak state-based institutions for accountability, such as the legislature and judiciary. Attempts to pass anti-corruption legislation in Cambodia had already proved very challenging, leading some donors to prioritise other reforms.

Many donors have adopted a definition of corruption similar to "the misuse of entrusted power for private gain"[61] and tend to use that as a basis for policy and interventions. However, such phrasing may differ from the way government interlocutors and citizens in recipient countries define corrupt behaviour.[62] Donors may then differ as to the extent their responses take account of local demand for changes in behaviour. In Indonesia, survey data indicate that people are generally intolerant of high-level corruption in government but tolerant of smaller payments to cut through red tape or accelerate access to services.[63] In Afghanistan, bureaucrats or MPs may feel compelled by informal socio-cultural norms to favour their kin, and low-level corruption is widely tolerated. In Afghan eyes, high international salaries for technical advisors and some Afghan officials, and perceived wastage and leakages in off-budget aid, constitute a form of corruption.

Scant information on progress and the impact of governance and anti-corruption reforms can constrain joint responses. Measuring corruption is intrinsically difficult and tends to rely on perception-based data. This creates uncertainty as to whether reforms are having an impact. For example, despite nearly a decade of sustained donor support to a range of government-led governance reforms with potential to tackle corruption in Indonesia, indicators covering the period up to 2007[64] did not suggest a significant impact on corruption outcomes except for broad improvements in

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61 This is the definition adopted by Transparency International. For examples of similar definitions used by donor agencies see Mokoro, 2008.

62 The UN Convention against Corruption (UNCAC) notably avoids defining corruption and provides examples of corrupt practices (Arts. 15-22).

63 Individuals may also be tolerant of speed money in individual transactions without associating this with perverse incentives and wider networks of patronage that it can encourage across government bureaucracies.

64 Indonesia's absolute scores improved in perception-based surveys on corruption between 2003 and 2007, but at a 90% confidence level it is not possible to say whether corruption lessened in this period (Kaufmann, et al., 2008). Indonesia's scores on corruption in the CPIA index also remain low, just above the IDA borrowers' average, and it gets an overall "weak" rating in the 2006 Global Integrity Indicators Scorecard. That year's Scorecard gives strong ratings for KPK, civil society and judicial accountability. Investment climate surveys show significant improvement in local firms' perception of the severity of corruption, and a substantial decline in the cost of bribes as a share of production costs.

the investment climate. However, Indonesia's TI Corruption Perception Index[65] score rose in 2008 to show distinct improvement over 2003, even allowing for margins of error.[66] But Indonesians are less optimistic about where corruption is headed: in 2005, shortly after President Yudhoyono was elected on an anti-corruption platform in Indonesia, 63% of Indonesians thought corruption would decrease in the following three years; by 2007 Indonesians only 22% felt corruption would decrease.[67] Nonetheless there are signs that the anti-corruption commission's prosecutions have reduced impunity.

Lack of information and uncertainty can lead some donors to conclude that action is not being taken to tackle corruption, or that the action taken is not having an impact. Lack of information, about implementation and the impact of sectoral anti-corruption plans in Mozambique, despite donor efforts to engage with service delivery sectors, was one factor causing some donors to reduce or not increase budget support in 2008. The need to monitor and demonstrate results can sometimes induce donors to seek easily measurable indicators. Sometimes these would be a strong indicator of impact (*e.g.* the number of textbooks reaching schools), but on other occasions less so (*e.g.* the passage of anti-corruption legislation).

5. Donor countries' strategic priorities

As mentioned above, donors often share a common concern to manage development and fiduciary risk. However, where different donors accord greater priority to different types of risk, this can be a constraint to joined-up responses. Donors tend to judge situations on a case-by-case basis. However, among some donor countries – particularly in Northern Europe – pressure from domestic parliaments to manage fiduciary risk is often a trigger to respond to reports of leakage, deteriorating governance assessments or poor performance against governance indicators.

Where some donor countries prioritise strategic goals other than tackling corruption, this too can prove a constraint. In Afghanistan the immediate priority after the fall of the Taliban in 2001 and during the subsequent political transition was to ensure security and re-establish state administration and capacity for service delivery. This was accompanied by unconditional support from the international community for the government of President Karzai and large volumes of aid. Those large inflows of foreign assistance into weak systems and existing systems of patronage helped to increase corruption.

Donor countries keep their strategic goals under regular review and may change the nature of their engagement when new evidence of deteriorating governance emerges. In Afghanistan donors initially focused urgently on stabilisation and reconstruction. Military and foreign policy objectives have continued to crowd out other concerns. However, in the light of evidence of increased corruption, some donors and multilaterals have since 2006 begun to question whether the priority accorded security and stability has been at the expense of effectively managing fiduciary and development risk. More recently, stronger public messages on these issues have been delivered by even the most influential donors.

Another constraint can arise where donors are under corporate pressure from headquarters and parliaments to scale up aid. In some northern European countries, parliaments especially hold donor governments to account for managing fiduciary risk as well as meeting commitments to deliver increased aid. In a number of budget support contexts in Africa, some donors felt it was difficult to respond to corruption by reducing or delaying disbursements, partly because of this "pressure to spend". The Ugandan water sector provides an example: while at one stage Sweden responded to evidence of corruption by suspending disbursements, other donors were concerned this might limit achievement of their spending plans and increased spending to compensate. This resulted in mixed messages to government partners. In Mozambique it is evident that some southern European countries accord high priority to meeting international targets to increase aid. This can make them less likely to respond to evidence of deteriorating governance by reducing aid, and more likely to use other forms of response, such as political dialogue.

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65 See discussion of the use of TI CPI in Part I. In Indonesia the government uses the CPI to measure its own progress.

66 Indonesia's TI CPI score rose from 1.9 in 2003 to 2.6 in 2008. With margins of error in 2008 ranging between 2.3 and 2.9, Indonesia's 2008 score at any point in that range was higher than in 2003.

67 Transparency International's Corruption Barometer.

6. Strengthening vertical accountability

Many donors' policies have converged round the conviction that strengthening partner governments' accountability to their citizens is an important means to improve governance and reduce corruption. Where partner governments' commitment to tackling corruption is weak, and there is little or no evidence of formal or state-based reforms having an impact on corruption, donors have an even stronger incentive to strengthen the "demand side" for greater transparency.

Donors have an opportunity jointly to analyse the type of support that may be needed to strengthen vertical account-ability, for example working to strengthen political competition or advocating freedom of information. Some donors may have comparative advantage that enables them to provide technical support or allows them political freedom to work in sensitive areas, such as political party reform. In Indonesia for example, the Netherlands is supporting political party reform through an arm's-length relationship with the Netherlands Institute for Multi-Party Democracy – and, together with AusAID, is strengthening Parliament to better perform its role. A joined-up approach does not require all donors to work on the same areas, providing the overall effort is informed by a common analysis of priorities.

Again in Indonesia, until recently significant and co-ordinated support to civil society was routed through the Partnership for Governance Reform in Indonesia (PGRI). This gave donors an opportunity to support an Indonesian-led approach and support civil society at arm's length with core funding. That support, combined with other direct support to NGOs, has facilitated continued civil society pressure to maintain reform momentum.[68]

> **Box 3. The Partnership for Governance Reform in Indonesia**
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> The PGRI was established in March 2000. A governing board was formed with representation from different stakeholders (the three branches of government, civil society, academia, the private sector, the media and the principal donors). The presence of influential ministers on the board gave the PGRI status and influence in advocating reforms in the early years of *reformasi*. In the anti-corruption area, for instance, the Partnership was an early contributor to the dialogue that led to reforms. Its initial surveys[69] helped lay the foundations for a subsequent nationwide dialogue on corruption under its auspices, and helped convince Indonesian policy makers about the extent of public anger about corruption.[70]
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> The advantage of this approach was that the PGRI was an Indonesian-owned entity with strong support from the government. It also enabled donors to support NGOs through an intermediary rather than providing direct support, given the tendency for such a relationship both to affect the efficacy of the NGO (being seen as driven by donors) and to shift NGO accountability away from Indonesian constituencies to donors.

Co-ordinated support to civil society is more effective if it is informed by a shared assessment of governance challenges and the role of civil society. In Afghanistan, civil society has been involved irregularly in consultations on the ANDS and in the working group structure underpinning the JCMB. But generally, CSOs have not been considered by the government or donors as relevant actors at the policy level, and much less as potential partners. CSOs' effectiveness in holding government to account is also limited by their weak capacity and limited funding. In Mozambique donors have sometimes acted as a hub, encouraging the inclusion of civil society in the thematic working groups that carry out ongoing performance monitoring of the multi-donor budget support mechanism. Such approaches may encourage gradual government acceptance of civil society as interlocutors. They may go some way toward mitigating the tendency of some partner governments to be more accountable to donors where

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68 "[P]erhaps the most significant contribution that PGRI has made has been helping to grow the network of reform interested NGOs, which have kept up the pressure for reforms 'from below' and can help to ensure that the reform process becomes irreversible" (Lankester, 2007).

69 The PGRI's 2001 anti-corruption survey of households, civil servants and business enterprises was the first of its kind in Indonesia (PGRI, 2001). In its study *The Poor Speak Up* (Hardjono and Teggemann, 2002), poor people spoke about their day-to-day encounters with corruption.

70 The survey revealed that four-fifths of respondents felt that corrupt officials needed to be jailed and their assets seized. A significant majority also favoured corrupt officials being publicly shamed.

aid flows are high, complicating efforts to build greater accountability from state to citizens.[71] Support from donors for research, policy participation and advocacy may mitigate some of the risks faced by CSOs. For example, in Afghanistan, advocacy, specifically for sensitive political issues like corruption, continues to be perceived as dangerous; most CSOs engage very cautiously in advocacy-related activities, if at all. Some prefer to maintain a profile closer to research institutions, limiting their role to making information and analysis available. On the other hand, the Indonesia case study highlighted the risk that donor involvement with civil society may distort civil society priorities by providing funding primarily for donors' preferred activities, indicating the need to provide more sustained and less earmarked support.

While donors recognise the importance of parliament's role in strengthening horizontal and vertical accountability, efforts to strengthen it have often had limited success, leading some donors to conclude that such efforts are not worthwhile. Parliamentarians' political loyalties impede effective interventions. Loyalty to or interference from the executive may undermine parliament's accountability role. For example, in Mozambique the legislature has been historically dominated by the ruling party; it faces serious capacity constraints that limit its ability to perform its over-sight roles. This in turn limits horizontal and vertical accountability. Not only has it proved difficult for donor-supported reform programmes to have an impact, but the weakness of the legislative oversight function has reinforced the accountability of government to donors. In Afghanistan, the National Assembly has started asserting its role of oversight of executive power. It rejected some presidential nominees for Cabinet, and for the chief and judges of the Supreme Court. In response, members of the executive refused to appear before the National Assembly to answer questions of different committees. President Karzai does not count on a stable majority in the National Assembly, and there are allegations of corrupt practices by the executive to obtain legislative majorities (Ruttig, 2008).

For parliament to act as a channel of vertical accountability, it must also respond to the citizens it represents. However, in Mozambique for example, there is a weak relation between the legislators and their constituencies. In Afghanistan the National Assembly, parliamentarians and individuals are not generally trusted by citizens (WB, 2008).

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71 In Mozambique, for example, it has been argued that donors continue to crowd out national policy processes and confuse the space for accountability between government and citizens (DFID, 2008).

LESSONS LEARNED AND RECOMMENDATIONS

Responses to corruption and poor governance are part of an ongoing engagement with development in partner countries. Responses occur at different stages in the programming cycle; a corruption situation may result in review and revision of the overall strategy for engagement with a partner country, or specific strategies relating to governance and corruption. Responses involve stakeholders – in partner countries, in donors' home constituencies and internationally. To be effective, they need to involve advance and continued analysis, connected political and technical dialogue, prior agreement on performance monitoring frameworks, and discussion of a range of disbursement arrangements. Confrontation with partner governments rarely ensures lasting improvements in governance and reduced corruption, but may send a strong signal. Measures to strengthen transparency and accountability to citizens in developing countries are an essential component of effective responses, but often take time to demonstrate impact on corruption. By further linking national and international anti-corruption efforts, donors may provide additional incentives for partner governments to take action against corruption.

1. Assessment and analysis [72]

The relevance and effectiveness of responses must be seen in the light of the governance, politics and accountability of each context. Obtaining an understanding of these is an important first step to improving the effectiveness of responses.

There are often multiple governance and corruption assessments available, including local sources. *The key to using these effectively[73] is to ensure that information is shared; that different types of analysis are viewed together to form a comprehensive picture; and that the material is then used collectively, rather than as a trigger for unilateral responses.* If donors take time together to obtain a shared understanding of the political and economic dynamics of a country, this can help to identify causes of corruption, its different forms and impact, and any local demand for improvements in accountability and transparency as a basis for designing and prioritising effective responses at all stages of the aid planning and delivery cycle.

The quality of analysis is improved where donors have appropriate technical capacity, where multidisciplinary inputs are encouraged, and where different parts of donor governments are involved. Different donors may have technical expertise and interest in different areas.

Often it is difficult to measure or identify the impact of reform. Lack of such information is not usually an appropriate rationale for responses that affect aid disbursements and development dialogue. PEFA is a standardised assessment tool that has proved valuable for measuring intermediate outcomes of PFM reform. It is more effective where government is involved in the process of assessment and recognises the value of using the scorecard as a way of measuring its progress over time.

Advance analysis of the political economy of partner countries is also effective in helping donors manage reputational risk and ensure continued support from donors' domestic constituencies for development goals. Such analysis can:

- Identify opportunities or blockages to reform that may arise from the nature of a country's political economy and timing in the political cycle.

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72 See also OECD DAC GOVNET, 2009b.

73 OECD DAC GOVNET, 2009b highlights how different governance assessment methodologies explicitly or implicitly measure or assess standards against one of five governance perspectives. It argues that the choice of assessment tool is then likely to point to a certain type of agenda. For example, if assessment is against standards of new public management governance, then the result will point to an agenda of change towards these standards. If power and political economy are assessed, the result will point to an agenda working to influence or acknowledge politics and power.

- Identify critical junctures[74] when particular types of response may be needed.
- Take account of longer-term consequences of immediate reactions.
- Predict the likely positions, when a response is required, of different stakeholders. Different donor countries sometimes have other strategic goals of their engagement. Donors may not all prioritise development, reputational and fiduciary risk to the same extent in a given context.

Although donors now have well-established methodologies for analysing the dynamics of the political economy and neopatrimonial networks in a given context, it is still challenging to incorporate these into technical and programmatic approaches to governance reform. Donors are challenged to find compelling evidence of interventions that are effective in different contexts given a range of informal rules and norms. One implication is that building rules-based governance is a lengthy process with many setbacks.

Experience suggests that there are also risks associated with such approaches. For example, by taking a longer-term view of change and attempting better to understand underlying institutional incentives driving corrupt behaviour, donors may be perceived to condone it (Mathisen, n.d.; Unsworth, 2007). Providing large aid volumes into corrupt and entrenched patronage systems can both sustain and strengthen them (Cammack, 2007). 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 also important to keep the trajectory of reform and appropriateness of responses under regular review.

Recommendations

1. Jointly analyse assessments.[75] Reach a shared understanding, including local perspectives on governance and how it is evolving. Harmonise support for assessments by local analysts, including support to build capacity if required.[76] Work with government and civil society.[77]

2. Assess gaps in donors' skills in order to enhance technical work. Agree how to fill these based on each donor's comparative advantage. Consider joint support for improved technical capacity among donors. Respond to requests for technical inputs from partners.

3. Involve partner country governments in the development of tools.[78] Agree in advance how qualitative assessments will be shared and used to monitor performance.

4. Take early action collectively to consider risks of corruption, even in political transitions and post-conflict contexts. Include consideration of the risks and consequences associated with providing large aid volumes where systems and capacity are weak and patronage networks are entrenched.

5. Look ahead and consider future scenarios that might require management of reputational or development risk. Use this as a basis for agreeing in advance how best to manage these risks when evidence of corruption arises or performance deteriorates. Identify options for early action to minimise risk to development outcomes.

6. Identify in advance the impact of donor practices on corruption and commitment to reform, so as to minimise approaches that impede greater transparency and accountability.

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74 For example, when priority is given to humanitarian and reconstruction needs in post-conflict contexts, basic measures to introduce systems to prevent and sanction corruption may not be prioritised while large amounts of aid are being provided to re-establish systems of administration and service delivery. This can facilitate the evolution of established patterns of patronage and rent-seeking into rampant corruption.

75 At the very least this entails donors sharing with each other the assessment material they have to reach a shared understanding of the governance and corruption challenges. Depending on the purpose of the assessment there may be advantages in further harmonisation, for example if the primary purpose of assessments is to engage domestic stakeholders, stimulate dialogue and promote governance reform. However, if donor assessments are mainly intended to serve internal purposes, the costs of harmonisation may outweigh benefits (OECD DAC GOVNET, 2009b).

76 This can ensure coverage, diversity and pluralism (OECD, 2009a).

77 The OECD DAC Guiding Principles suggest it is important to draw on and align with domestic or peer-based assessments and involve partner country stakeholders in tool development, as this will benefit realism and legitimacy (OECD, 2009a).

78 The importance of involving government was highlighted when a PEFA assessment was carried out in the Indonesia case for this study.

2. Donor co-ordination for supporting and monitoring relevant reforms

Where government owns and/or leads the approach to tackling corruption, this is a strong basis for donors to support governance and anti-corruption reforms and monitor progress. Where there is government commitment to reform but limited technical capacity to develop and implement appropriate approaches, donors can work together to provide technical support as requested by government[79] for priorities that could improve transparency and accountability. An imperfect approach that is owned by government has greater prospects of success and is likely to be more politically viable than one that donors like for technical or policy reasons but that lacks government ownership. It is worthwhile for donors to continue harmonising analysis, support to reform and monitoring, even where government is leading reform but not co-ordinating donors. This ensures donors are better prepared if a response is required or government commitment weakens.

There may be scope for donors to ensure that critical areas are not overlooked in a government-led strategy or, separately, support reforms to address these areas. For example, it may be easier for donors to support reforms in areas that are politically sensitive for government to address. Sustained support is required to ensure governance outcomes. When donors' strategic priorities change – for example if a recipient country "graduates" from LIC to MIC status based on income criteria – sustained support is still required for institution building. Donors can jointly review the technical skills they require to provide appropriate support to reform, and how they can combine or share resources to provide this.

Where there is limited government commitment to reforms to improve accountability and transparency, donors need to resist the temptation to rely on formal plans or fund consultancies to write strategies. Confrontation with government may not lead to greater commitment or action; it may also undermine dialogue necessary to encourage development outcomes. In such contexts, there may still be scope for donors to co-ordinate and agree on approaches to support. This could involve agreeing with government on a limited number of concrete benchmarks supported by reformers, which allow progress against vested interests opposed to reform. Informal donor co-ordination can help donors identify areas where there may be some government support for reform, and ways to improve transparency and accountability. This includes working in sectors.

Even where donors are harmonised round a common performance assessment framework, there may be occasions when additional or non-predicted evidence of corruption comes to light. Where donors agree together at the outset of joint programming how they will share information with each other and government, and which type of responses according to their bilateral agreements or joint MoUs are likely to be triggered, this can ensure responses are predictable while allowing individual donors flexibility.

Donors' corporate policies on governance appear to have been converging, for example recognising that corruption is a symptom of weak governance. In practice individual donors may give greater relative weight to fiduciary or development risk when a corruption situation arises.

Several thematic working groups may exist related to different public sector and governance reform programmes that address corruption. It is still important to have a single forum in which donors, ideally with government and other stakeholders, can view reform programmes from a multidisciplinary perspective. This ensures that separate dialogue with government concerning the different reform programmes is connected, and an overall picture of the trajectory of reform is obtained. Often reforms are interconnected, and lack of progress in one area may be attributable to blockages elsewhere. Donors need to understand these linkages when monitoring performance indicators and before deciding on responses. Where recipient governments provide only a formal or incomplete lead, this can still be a basis for donors to meet regularly to share analysis and monitor progress across different reform programmes addressing corruption.

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79 The AAA 2008 states that "capacity development is the responsibility of developing countries, with donors playing a supportive role … Donors' support for capacity development will be demand-driven and designed to support country ownership" (AAA 14, 14 b).

Where recipient governments are not committed to reforms to improve governance and tackle corruption and do not provide a lead, it is still important for donors to co-ordinate analysis, support to reform opportunities and monitoring, for example in an informal donor group. For more effective responses, more influential donors may need to take the lead in making space for other donors and encouraging discussion of alternative effective responses.

Recommendations

1. Co-ordinate donor support to reform round government-led and -owned approaches, where they exist. Encourage governments to take their aid co-ordination functions seriously. Ensure donors jointly have the shared technical expertise in country to support reform processes.

2. Work with government, parliament and non-state actors to develop a shared position on how corruption should be addressed in a particular context, using this shared approach as a framework. Co-ordinate efforts to provide technical support where requested by government to identify priorities and related reforms. Strategically select reform areas to support and monitor.

3. Avoid confrontation over performance where this may undermine dialogue about development and jeopardise development outcomes (but see comparative advantage in Section 3 below). Work to strengthen parliaments and civil society to demand improvements. Support and monitor a range of reforms, and take advantage of opportunities when they arise.

4. Agree in advance with other donors on how and when to consult with each other and government if performance deteriorates or stagnates, or new evidence appears. Agree with other donors and government what kind of responses (dialogue, aid disbursements, modalities) might follow.

5. Establish a formal, multi-disciplinary, cross-cutting working group on governance and anti-corruption as one of the working groups monitoring government performance in CG architecture and preparing for high-level meetings. Encourage inclusion of other stakeholders *(see Section 7)*. Where a formal group is not possible, establish an informal donor group.

3. Dialogue

Separate dialogue mechanisms can lead to mixed messages. Different donors and donor governments have comparative advantage in political and technical dialogue. An individual or critical mass of donors may be better equipped to convey different types of messages through different channels. Some division of labour according to comparative advantage has the potential to make the overall response more effective if a coherent approach is agreed in advance.

There are regular opportunities to raise issues of governance and corruption in the calendar of donor-government meetings established around key aid instruments. Instruments such as budget support provide a high-level platform for discussion, agreement and monitoring of reform with government. Donor concerns to manage fiduciary and development risk focus attention on progress with reform. Where efforts are made to include other donors in these discussions, communication improves among donors and between donors and government. This can promote transparency, help avoid mixed messages, and ensure predictability in aid flows and responses.

Quality of dialogue is a key determinant of effectiveness, one that can be enhanced by advance preparation and regular contact between the parties, for example in ongoing working groups. Where quality deteriorates, some donors may wish to pursue less joined-up responses. On the other hand, concerns to maintain a united public front and protect engagement from reputational risk can dilute the effectiveness of public messages in moving the governance and anti-corruption agenda forward.

Responses tend to be more effective where donors co-ordinate technical dialogue and use this knowledge to inform political dialogue, both among donors and between donors and government. This approach facilitates consistent messages and makes best use of different opportunities for dialogue with government. Partner governments may support reforms based on priorities other than governance and anti-corruption, for example awareness of international reputation or a desire to generate growth. These can open opportunities for dialogue where there is a mutual interest in reform that may also improve governance and address corruption.

Mixed messages can also absorb scarce government time, due to the transaction costs and the capacity required to attend to different donors. It can cause confusion over sequencing and priorities for reform.

Civil society participation can make donor and government commitments more transparent, helping to lock in reform and ensure greater accountability for delivery. Often civil society has participated in working groups that monitor performance, but not in higher-level dialogue on policy or where decisions are made.

Recommendations

1. Co-ordinate donor support to reform round government-led and -owned approaches, where they exist. Encourage governments to take their aid co-ordination functions seriously. Ensure donors jointly have the shared technical expertise in country to support reform processes.

2. Work with government, parliament and non-state actors to develop a shared position on how corruption should be addressed in a particular context, using this shared approach as a framework. Co-ordinate efforts to provide technical support where requested by government to identify priorities and related reforms. Strategically select reform areas to support and monitor.

3. Avoid confrontation over performance where this may undermine dialogue about development and jeopardise development outcomes (but see comparative advantage in Section 3 below). Work to strengthen parliaments and civil society to demand improvements. Support and monitor a range of reforms, and take advantage of opportunities when they arise.

4. Agree in advance with other donors on how and when to consult with each other and government if performance deteriorates or stagnates, or new evidence appears. Agree with other donors and government what kind of responses (dialogue, aid disbursements, modalities) might follow.

5. Establish a formal, multi-disciplinary, cross-cutting working group on governance and anti-corruption as one of the working groups monitoring government performance in CG architecture and preparing for high-level meetings. Encourage inclusion of other stakeholders *(see Section 7)*. Where a formal group is not possible, establish an informal donor group.

6. Identify the comparative advantage of different donors and donor governments. Use this to improve the quality of technical and political dialogue with government concerning governance and corruption. Agree division of labour in different dialogue forums in advance, considering sectors as well.

7. Ensure that architecture around key aid instruments provides space for other donors[80] to participate and share information. Donors involved in key aid instruments should bring in other donors.

8. Link technical and political dialogue mechanisms to ensure that technical understanding informs all levels of political dialogue in country, at headquarters and internationally, as well as dialogue among different parts of donor and recipient governments. Identify government reform priorities as a basis for constructive dialogue.

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80 For example, mechanisms to include non-budget support donors where co-ordination and dialogue mechanisms are structured primarily round budget support.

4. Responses affecting aid modalities and the timing of disbursements

When donors respond to increased fiduciary risk by introducing additional funding safeguards, the response will be most effective if safeguards are not introduced in an *ad hoc* way, but as part of an approach that strengthens government systems.

Aid architecture and performance indicators are more effective if they provide sufficient flexibility for different donors to respond in ways that meet domestic accountability demands, while maintaining pressure on recipient governments to improve governance and maximise predictability of disbursements. Advance agreement on consultation procedures among donors and with government, calendars for commitment and disbursement decisions, use of fixed and variable tranches, and alignment of donors behind a common performance framework can all help achieve this. Donors are then locked into responding in a coherent and co-ordinated way.

Recommendations

1. Collectively agree and set out in advance with government the criteria for assessing progress in addressing governance and reducing corruption. Set out in advance the way aid modalities will be affected in different situations. When a situation arises, signal and consult in accordance with these agreements. Delay, reduce or reallocate disbursements according to these agreements to ensure predictability.

2. Take a longer-term view of the trajectory of governance change and reform. Avoid short-term reactions that can undermine development dialogue and longer-term goals. Meanwhile support the enabling environment for improved governance, for example by providing sustained support to improve transparency and accountability.

3. Establish additional safeguards and measures if necessary to manage fiduciary risk, but only in ways that strengthen rather than undermine country systems and procedures.[81]

5. International action

Lessons learned about conditionality and the emphasis placed on predictability by the Paris Declaration and AAA may be perceived as limiting the range of tools available for donors to convey strong messages on corruption to partner governments. At the same time, anti-corruption policies have begun to focus increasingly on the global incentive environment.[82] Donors may be able to influence action in third countries by working together internation-ally, for example to reduce opportunities for money laundering or co-ordinate extradition proceedings for individuals accused of corruption. While some donor headquarters have embraced these approaches, and several international initiatives[83] have been launched, many members of donor field staff have scarcely begun to try out these tools. Often they lack technical expertise in these areas, or see them as the domain of political counterparts.

Donor responses are sometimes motivated by information exchange between headquarters, and responses to corruption are often triggered by pressure from parliaments in donors' home countries. Donor governments often respond defensively by emphasising measures to manage fiduciary risk, and seek examples of short-term results in tackling corruption to present to their home constituencies. It may be useful for donors in country to agree on a common communication strategy putting forward their choice of responses, based on assessment of trade-offs and long-term trajectories of reform. This can be used in different donors' home countries and internationally to foster debate about corruption and aid effectiveness.

Although donors have similar corporate policies on managing fiduciary risk and addressing corruption, interpretation in country tends to vary.

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81 Accra Agenda for Action (AAA) 2008 15 b).

82 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 a description of these approaches see OECD, 2007.

83 For example The Stolen Asset Recovery Initiative (StAR) – see WB, 2007b and the International Centre for Asset Recovery (ICAR), www.assetrecovery.org.

Recommendations

1. Agree in advance among donor headquarters on procedures for consultation and information sharing about performance monitoring and responses to corruption.

2. Incorporate the recommendations from this research into individual donors' policies. Encourage donors to report internationally on adherence to them.

3. Agree on a common communication strategy as to choice of responses, based on assessment of trade-offs and long-term trajectories of governance and reform. Use in dialogue with parliaments and media[84] in donors' home countries and internationally.

4. Influential donors should take the lead in consulting with and co-ordinating other donors. Donors should identify opportunities to work with the influential donors among them via their headquarters or in international meetings as well as in country.

5. Collaborate with other donor countries, including in third countries, to facilitate international action against corruption.

6. Consider with other donors and political counterparts how to use international initiatives such as asset freezing, anti-money laundering and anti-bribery measures as alternative tools to deter corruption in partner countries. Link corporate policy and knowledge at headquarters with action in the field. Mainstream knowledge of international initiatives in order to tackle corruption and increase donor field staff skills in this area.

7. Research the impact of international initiatives on corruption and explore their effectiveness as an alternative or complement to existing tools.

6. Credibility and transparency

Donor responses are likely to carry more weight where they are matched by evidence of donors' own efforts to address corruption. Responses to corruption in country can also be more effective if they are complemented by donor action at home.

Where donors identify corruption in projects or programmes they control, it is advisable to be transparent about the process being followed to investigate and sanction, so long as this does not prejudice the investigation itself. It is important to maintain communication with other donors and government as investigations progress. Whether decisions to investigate are taken at donor headquarters or in country, an understanding of the political implications for recipient governments is important if there is to be effective co-operation. Transparency of procedures for investigating and seeking redress for leakages can build accountability and credibility.

Recommendations

1. Be transparent about how leakages and investigations in donor-controlled programmes are managed.

2. Commit to publishing conditions, the rationale for responses and the responses themselves, and to acting in a co-ordinated fashion that will not undermine development outcomes. Facilitate monitoring of these commitments by parliaments and civil society in country and/or peer review. Where use of country systems is not feasible, state the rationale for this and regularly review this position.[85] State clearly the circumstances under which country systems can be used.

3. Ensure that the proceeds of corruption are not laundered through donor country financial systems, and that their companies do not bribe or make illicit use of natural resources. Work across donor governments to introduce and apply legal frameworks in donor countries to ensure that companies are sanctioned for such action.

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84 A similar approach is discussed in Booth, 2008, specifically with respect to educating parliaments and the public aid modalities and development.
85 AAA 2008 15 b).

7. Building accountability from state to citizens and strengthening demand for improved governance

Anti-corruption reforms supported by donors have often prioritised improving state-based, formal and horizontal accountability. In aid-dependent contexts, particularly when existing checks and balances are weak, there are strong incentives for government to be accountable primarily to donors. This is sometimes reinforced by pressure on donors from their domestic constituencies with regard to how aid is spent. To strengthen accountability further from state to citizens in partner countries, donors need to provide greater support toward strengthening parliaments and civil society, and improving political competition.

Donors' efforts to improve accountability of recipient governments to their citizens have often failed or had limited impact (at least in the short term), as they have concentrated on strengthening or introducing formal institutions without sufficient understanding of the incentives of the political actors and officials within these institutions or of whether these are likely to encourage or block reform.

Where partner governments' commitment to tackle corruption is limited, it is even more important for donors to nurture demand from citizens for improved governance. By supporting capacity development and making space for civil society to produce surveys about corruption, donors can contribute to shifting attitudes and lessening tolerance of corrupt practices. This can create demand for reform among society and donors.

These relationships need to be handled with care, to ensure donors do not crowd out efforts to strengthen vertical accountability. On the other hand, donor support may be the only means by which civil society can resist threats, challenge existing patronage networks, build capacity, participate in policy debates and monitoring of reform, and carry out advocacy as a means to improve governance and reduce corruption. It is important for donors to support private sector interest groups that are lobbying for increased transparency or accountability.

Even where partner governments are committed to reform, donors often act as a hub, connecting government and civil society. Partnership among stakeholders is more effective in raising sensitive issues. Donor influence can also ensure that civil society is included in reform-monitoring mechanisms such as joint reviews. This may facilitate gradual acceptance by government of civil society as participant and interlocutor.

There are important opportunities to support improved accountability at sub-national levels, by making space and building capacity for local communities to observe procurement, monitor budgets and implementation, and service delivery.

Strengthening civil society requires sustained support. Civil society institutions may take time to develop sound internal management and governance practices. Sustained support is necessary to protect space for participation and influence and maintain momentum for reform.

Recommendations

1. Foster improvements in accountability from state to citizens, for example by providing sustained support to parliaments, and to non-state actors including civil society, media, research institutes and the private sector.[86]

2. Increase the space and capacity for civil society to participate in discussions with government on policy and monitoring of reform.[87]

3. Provide opportunities and strengthen capacity for communities and citizens to hold government and donors to account for budgeting, implementation and service delivery at national and sub-national levels.

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86 See AAA 13 b).

87 See AAA 13 a)-b).

ANNEX: PRINCIPLES ON WHICH A DRAFT CODE OF CONDUCT FOR EFFECTIVE COLLECTIVE RESPONSES TO CORRUPTION COULD BE BASED [88]

Introduction

Responses to corruption and poor governance are part of an ongoing engagement with development in partner countries. Responses occur at different stages in the programming cycle; a corruption situation may result in review and revision of the overall strategy for engagement with a partner country, or specific strategies relating to governance and corruption. Responses involve stakeholders – in partner countries, in donors' home constituencies and internationally. To be effective, they need to involve advance and continued analysis, connected political and technical dialogue, prior agreement on performance monitoring frameworks, and discussion of a range of disbursement arrangements. Confrontation with partner governments rarely ensures lasting improvements in governance and reduced corruption, but may send a strong signal. Building rules-based governance is a lengthy process with many setbacks, and donors are at an early stage in understanding these dynamics. Measures to strengthen transparency and accountability to citizens in developing countries are an essential component of effective responses, but often take time to demonstrate impact on corruption. There is scope to make more effective use of tools to tackle global incentives to corruption.

1. Prepare collectively in advance for responses.

- Reach a shared understanding with other donors and political counterparts of governance and politics and how they are evolving over time in each country context. Jointly analyse information, harmonising assessments where there is clear added value (OECD DAC GOVNET, 2009a). Include local citizens' perspectives on corrupt practices and reform priorities. Work with and strengthen the assessment capacity of partner governments and civil society.

- Agree in advance with other donors, parts of donor governments and international counterparts on the types of responses available. The options might include: intensified or alternative dialogue mechanisms, timing of aid disbursements, changed modalities, additional safeguards, and targeted political measures such as travel restrictions, among others.

- Consider the likely and longer-term impact of different responses on fiduciary, development and reputational risk.

- Review and update these assessments regularly.

2. Follow the government lead where this exists. Otherwise foster this lead, promote accountability and co-ordinate donors.

- Co-ordinate donor support to reform around government-led and -owned approaches, where they exist. Encourage governments to co-ordinate donors.

- Work with government and non-state actors to develop a shared position on how corruption should be addressed in a particular context, using this shared approach as a framework. Co-ordinate efforts to provide any technical support as requested by government and develop a division of labour among donors to meet this demand.

- Maintain regular informal consultations among donors even where government does not lead or co-ordinate donors. Look to influential donors to take a lead on co-ordination if government does not, and proactively include other donors, including non-traditional actors.

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88 These principles draw on findings from the case studies and prior work carried out by the OECD DAC, for example the OECD Policy Paper and Principles "Setting an Agenda for Collective Action". In environments of weak ownership and/or capacity to tackle corruption, lessons can also be learned from approaches to delivering effective aid in fragile states. In the short term, there is an expectation that some progress will be made toward achieving a long-term vision of building legitimate, effective and resilient state – for this dialogue and harmonisation with other donors is essential and engagement of a range of national actors. It is recommended that donors conduct joint assessments of governance and capacity and examine the causes of fragility before agreeing a set of realistic state-building objectives, and work on flexible funding modalities (AAA 2008).

3. Agree in advance on a graduated response if performance stagnates or deteriorates.

- Collectively agree and set out in advance with partner governments the criteria for assessing progress in addressing governance and reducing corruption. Draw a limited set of mutually agreed conditions from partner countries' own policies where possible.[89] This may include a set of agreed indicators that can serve as benchmarks. Encourage inclusion of civil society in monitoring of performance.

- Use government systems as the first option but where this is not feasible, state the rationale and regularly review the position.[90] State clearly circumstances under which country systems can be used.

- Agree in advance with other donors and government how and when to consult with each other if performance deteriorates or stagnates or new evidence of corruption emerges.

- Analyse jointly with government and civil society the causes of deteriorating performance; where causes are technical (*e.g.* capacity), review appropriate support to governance and anti-corruption reform or, where deterioration is due to reduced or absent commitment, agree with other donors a graduated response, which might include the following individual or simultaneous measures:

  - intensify development and/or political dialogue
  - explore international, regional and third party avenues for dialogue.

  Where aid is channelled through country systems, also:

  - Signal reductions in variable tranches of aid, and then reduce these as signalled.
  - Introduce additional fiduciary safeguards, but only in ways that strengthen rather than undermine country systems and procedures.[91]
  - As a last resort, change aid modality away from use of government systems.

- Incorporate the stages of response and range of possible responses in bilateral and multi-donor aid agreements.

- Consider applying targeted restrictions to public officials accused of corruption *e.g.* travel restraints. Take steps in donors' own countries to track, freeze and recover illegally acquired assets.[92]

4. Act predictably in relation to other donors; encourage other donors to respond collectively to the extent possible, but allow flexibility for individual donors.

- Respond as previously agreed with other donors and government. When a situation arises, signal and consult in accordance with these agreements. Keep other donors and government informed from an early stage about intended responses.

- Encourage as many donors as possible to join a common response and avoid mixed messages. Encourage influential donors to take the lead in responding. As a minimum, foster a critical mass of donors with a common response while allowing individual donors flexibility.

5. Maintain dialogue at different levels and focus on long-term development objectives.

- Ensure separate channels of dialogue are connected within each donor government and with partner governments – for example, at different levels of aid architecture, technical and political channels, and trade, security and development channels. Establish a cross-cutting, multidisciplinary working group on governance and anti-corruption – ideally formally within aid architecture, but at a minimum informally.

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89 See AAA 25 and 25 a).

90 AAA 2008 15 a)-b).

91 AAA 2008 15 b).

92 AAA 2008 24 d).

- Assess gaps in donors' skills in order to enhance technical work and improve dialogue. Consider joint use of technical capacity among donors and make best use of each donor's comparative advantage.

- Make use of individual donors' comparative advantage in dialogue with government to move negotiations forward. Agree division of labour in advance but consider jointly when different styles of dialogue and meetings may lead to greater commitment, sustained improvement in performance or, on the other hand, may be counterproductive by reducing influence over development outcomes.

- Where partner government commitment to some reforms is limited, focus support and monitoring on areas where there may be scope for change. Strengthen the enabling environment for improved governance though greater accountability, transparency and participation including at sub-national levels and in sectors. Support and monitor a range of governance reforms so that when one avenue is blocked, others may be prioritised.

- Provide sustained support among different donors for institution building in partner countries, even if other geopolitical or funding priorities shift.

6. Foster accountability and transparency in country and internationally.

- Deepen efforts to improve vertical accountability from state to citizens, for example through parliaments and political competition, as well as continuing support to strengthen horizontal checks and balances within the state.

- Make space for civil society to participate in government-donor dialogue, monitoring and policy discussion. Provide sustained support for the participation of – and capacity building by – civil society, including the private sector, media and research institutes.

- Publish conditions, the rationale for responses and the responses themselves. Facilitate monitoring of these commitments to predictability by parliaments and civil society in country and/or through peer review.

- Encourage and support partner government efforts to publish information that will facilitate greater account-ability to citizens.

- Publish applicable policies, results of investigations, and action taken when corruption arises in donor-controlled programmes.

7. Act internationally but link international action to anti-corruption work in partner countries

- Agree in advance between donor headquarters on procedures for consultation, information sharing about performance monitoring, and responses to corruption.

- Collaborate with other donors in international forums and third countries to facilitate cross-border action against corruption.

- Mainstream among donor staff, partner governments and in-country programmes knowledge of international initiatives to address global incentives to corruption.

- Encourage consideration of and take steps at home, where possible, to combat corruption by individuals or corporations and track, freeze and recover illegally acquired assets.[93] Work with other parts of donor governments to achieve objectives. Provide technical assistance on demand to strengthen partner countries' capacity in these areas and skill up donor field staff to support this.

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93 AAA 2008 24 d).

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