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REVIEW OF IMPLEMENTATION OF THE 2018 FRAMEWORK FOR ENHANCED FUND ENGAGEMENT ON GOVERNANCE—BACKGROUND PAPERS

EXECUTIVE SUMMARY

This background note provides a set of short papers with additional information to support the discussion and analysis in the Review of the Implementation of the 2018 Framework for Enhanced Fund Engagement on Governance (the “main paper”). It presents additional analysis on the following topics:

- **Section I: Experiences with Governance Diagnostic Assessments.** Takes stock of the experiences with governance diagnostic assessments since 2018 highlighting their scope, functions, and engagement with the authorities and other stakeholders.
- **Section II: Mitigating Corruption Risks in Emergency Spending: Lessons Learned from the IMF’s Experience During the COVID-19 Pandemic.** Reflects on the IMF approach to governance safeguards in emergency financing during the COVID-19 pandemic and identifies preliminary lessons learnt, including to inform future emergency financing response.
- **Section III: Role of Supreme Audit Institutions to Address Corruption Risk.** Reviews Supreme Audit Institutions’ increased focus on issues relating to corruption, before providing an overview of experience in the Fund’s engagement with SAIs, and elaborating three core principles to inform IMF staff work going forward.
- **Section IV: Transnational Aspects of Corruption.** Briefs about the existing framework for combating the transnational aspects of corruption, takes stock of the coverage in IMF Article IV Staff Reports since April 2018 and discusses lessons learnt, and proposes sustaining and deepening the coverage in Staff Reports going forward.

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Glossary

AEs	Advanced Economies
AFR	African Department
AML	Anti-Money Laundering
APD	Asia & Pacific Department
BOP	Balance-of-Payments
CD	Capacity Development
CFT	Combating the Financing of Terrorism
CSOs	Civil Society Organizations
EMs	Emerging Markets
EMDEs	Emerging Markets and Development Economies
ESG	Environmental, Social and Governance
EUR	European Department
FAD	Fiscal Affairs Department
FATF	Financial Action Task Force
FCS	Fragile and Conflict-affected States
FDs	Functional Departments
GAC	Governance and Anti-Corruption
IDB	Inter-American Development Bank
IFIs	International Financial Institutes
IMF	International Monetary Fund
INTOSAI	International Organization of Supreme Audit Institutions
LICs	Low Income Countries
LOI	Letter of Intent
MCD	Middle East & Central Asia Department
MONA	Monitoring of Fund Arrangements
ML	Money Laundering
NGOs	Non-Governmental Organizations
OCCRP	The Organized Crime and Corruption Reporting Project
OECD	Organization for Economic Co-operation and Development
PIMA	Public Investment Management Assessment

PFM	Public Financial Management
RCF	Rapid Credit Facility
RFI	Rapid Financing Instrument
RST	Resilience and Sustainability Trust
SAIs	Supreme Audit Institutions
SOEs	State Owned Enterprises
TI	Transparency International
UCT	Upper Credit Tranche
UNCAC	United Nations Convention Against Corruption
UNDP	United Nations Development Programme
UNODC	United Nations Office on Drugs and Crime
WB	The World Bank
WGB	Working Group on Bribery
WEO	World Economic Outlook
WGI	World Governance Indicator
WHD	Western Hemisphere Department

EXPERIENCES WITH GOVERNANCE DIAGNOSTIC ASSESSMENTS¹

This background paper takes stock of the experiences with governance diagnostic assessments since 2018. In response to requests by country authorities, teams consisting of staff from relevant functional departments² have completed 15 diagnostic assessments, for the most part in a Fund-supported program context. In close collaboration with government counterparts, these diagnostics are designed to assess the severity of corruption and identify the governance weaknesses and corruption vulnerabilities across six core state functions provided by the 2018 Framework. As a forward-looking exercise, they recommend concrete structural reform measures to advance governance, integrity, and the rule of law, and produce a public report. Depending on the circumstances, each diagnostic takes up to twelve months. As an evolving tool, assessments have reflected strong commonality in coverage, as well as substantial variation in structure, size, number of recommendations, and follow-up. Findings of the diagnostics have regularly informed Fund-supported programs, including through conditionality, surveillance in the context of Article IV missions, capacity development work, and authorities' reforms efforts.

A. Overview of Governance Diagnostic Assessments

1. Since the adoption of the Framework for Enhanced Fund Engagement on Governance in 2018, 15 governance diagnostics have been completed, with six more assessments underway.³ The diagnostics are undertaken in response to requests from the authorities. While the number of requests decreased during the COVID-19 pandemic, some diagnostics have been conducted during the COVID-19 travel ban. The Sudan and Mali diagnostics were undertaken in a full remote mode, while the exercises in Zambia and Mauritania were hybrid. Governance diagnostics are designed to provide a holistic analysis and strategic recommendations for improving integrity and governance in a member country. The assessments examine the severity of corruption in a country, which informs the identification and analysis of governance weaknesses associated with corruption vulnerabilities across the six core state functions covered by the 2018 Framework: (i) fiscal governance; (ii) rule of law (contract enforcement and protection of property rights); (iii) market regulation; (iv) central bank governance and operation; (v) financial sector oversight; and (vi) AML/CFT. They also assess the effectiveness of anti-corruption legal and institutional frameworks. The governance diagnostic report that is produced is part of a longer process of engagement on

¹ Prepared by Tina Burjalani, Ron Snipeliski and Joel Turkewitz (all LEG), Veronique Salins and Olivier Basdevant (both FAD).

² Governance diagnostic missions are a cross-department exercise (co-led by LEG and FAD), with participation of MCM and FIN in most missions. Other international institutions have also participated in some missions.

³ The first comprehensive diagnostic assessment of governance and corruption took place in 2014 for Ukraine, prior to the adoption of 2018 Framework. See "Government of Ukraine Report on Diagnostic Study of Governance Issues Pertaining to Corruption, the Business Climate and the Effectiveness of the Judiciary", July 11, 2014.

governance and anticorruption reform that is shaped by the issues present in a particular jurisdiction and tailored to the country program. To ensure effective implementation of recommendations, country teams need to appropriately follow up, including incorporate key recommendations in program or surveillance work, monitor an action plan included in Government reform programs, and if needed, arrange for follow up TA requested by authorities.

2. The majority of countries which requested a governance diagnostic were LIC and FCS (Table 1). Out of the 21 countries for which diagnostics have been or are being delivered, 10 are FCS. As mentioned in the IMF Strategy for FCS (adopted in March 2022), these diagnostics will inform more in-depth analysis on corruption and governance issues in surveillance, where needed. Governance diagnostics have been concentrated in countries with severe and systematic corruption issues. The participating countries are spread across different income levels (covering both low-income and middle-income countries) and generally perform poorly on control of corruption indicators.

3. Ten out of the 15 completed reports have been published, with the approval of participating authorities (Table 1). Publication of the report is encouraged, as transparency on the findings and recommendations is an important contribution to good governance. Authorities have published the report on their own web sites in number of cases, demonstrating strong ownership of the report and their active engagement defining future actions. As a good practice of ownership, some diagnostic reports were published as the authorities' report prepared in collaboration with IMF.

Table 1. Governance Diagnostic Assessments Since 2018

Year	EM (excl. FCS)	LIC (excl. FCS)	FCS
2018			Republic of Congo (published)
2019	Equatorial Guinea (published) Peru		Mozambique (published)
2020		Honduras	Dem. Rep. of Congo (published) Guinea-Bissau (published) Zimbabwe
2021		Moldova (published)	Central African Rep. (published) Mali Sudan
2022	Paraguay (published)	Zambia (published)	
2023	Sri Lanka (planned) Tunisia (ongoing)	Benin (published) Mauritania (near completion) The Gambia (ongoing)	Lebanon (ongoing) Cameroon (ongoing)

Source: IMF staff, as of March 1, 2023.

4. The severity of corruption has been assessed based on candid analysis of relevant sectors, combined with information obtained through third-party indicators. 13 out of 15 completed diagnostics used third-party indicators in assessing severity of corruption. Some recent exercises, including Zambia, included an external political scientist in the team to provide a deeper and broader understanding of the nature of corruption, changes in corruption patterns and trends, and experience with past efforts to address corruption and improve governance.

5. Diagnostics consistently assess corruption risks as part of analyzing the effectiveness of AML, rule of law (especially in relation to the integrity of the judiciary), fiscal governance and financial sector oversight frameworks. Diagnostics also consider the soundness and alignment of the legal and organizational arrangements for fighting corruption with international standards and good practice, and the appropriateness of the anti-corruption strategy in light of the corruption risks that are present.

6. All diagnostic reports provide time-bound policy recommendations to mitigate governance weaknesses and corruption vulnerabilities. Corresponding with the breadth of coverage of key state functions in the diagnostics, 57 percent of recommendations focused on fiscal governance, followed by recommendations on strengthening the overall anti-corruption frameworks (14 percent), rule of law (including effectiveness and integrity of the justice sector— 10 percent), AML (8 percent), financial sector oversight (4 percent) and market regulation and central bank governance and operations (3 percent each). The small number of recommendations relating to market regulation reflect somewhat inconsistent coverage of this element of the framework. Also, financial sector oversight and central bank governance and operations were not covered in earlier diagnostics.

7. Recommendations are generally tailored to recipient countries' specificities and capacity (See Table 2 for some examples). The number of recommendations varies, largely depending on the scope of the diagnostic (i.e., extent of coverage of key state functions) as well as the context and capacity of the state to implement comprehensive reforms. Given the close association with corruption vulnerabilities, fiscal governance sections of diagnostics, for instance, typically include fiscal transparency, public financial management (in some cases with specific discussions on public procurement, PPP framework and/or public investment management), SOE oversight, revenue administration, and/or natural resource management. When relevant, they also discuss fiscal decentralization or overarching issues such as digitization or human resources management. While all recommendations are time-bound, most reports provide sequencing by identifying a limited number of priority measures in each area.

Table 2. Reform Recommendations from Governance Diagnostic Assessments

Area	Specific reform recommendations (selective)
Anti-Corruption framework	<ul style="list-style-type: none"> • Adoption of anti-corruption law in line with UNCAC standards (short-term RoC; high-priority Equatorial Guinea) • Introduce transparent and participatory appointment rules for key anti-corruption officials (medium-term, Zambia) • Strengthen asset declarations legal framework (short-term, CAR, short/medium-term Zambia)
Fiscal Governance (public financial management, tax administration and customs operation)	<ul style="list-style-type: none"> • Undertake a comprehensive inventory of extrabudgetary operations (short-term, Guinea-Bissau). • Extend the coverage of the General Treasury Account to all central government operations (medium-term, DRC). • Publish quarterly an online list of names of all de jure or de facto exemptions with the revenue losses they generate in the government coffers (short-term, CAR)
Rule of law	<ul style="list-style-type: none"> • Clarify powers and responsibilities of the judicial inspectorate and improve operating procedures (short-term, Moldova) • Establish a publicly accessible central repository of updated laws and regulation (immediate, DRC) • Develop detailed procedures and fair and uniform criteria for alienation of State land, with clearly defined roles and responsibilities of central and local authorities. Provide capacity building and resources to local authorities to ensure proper implementation of land alienation rules (short-term, Zambia)
Market regulation	<ul style="list-style-type: none"> • Post all legislation, decrees, and regulations online (short-term, Guinea-Bissau). • Ensure full operationalization and sustainability of the one-stop shop and for bureaus to become financially autonomous (short-term, DRC). • Unify licensing for economic activity under a single entity (high-priority, Mozambique)
Central bank governance and operations	<ul style="list-style-type: none"> • Strengthen the NBM's governance and independence, including the operational independence of its prudential supervisory function through amendment to the NBM Law (medium-term, Moldova).
Financial sector oversight	<ul style="list-style-type: none"> • Enhance the governance of the Bank of Zambia in its role as banking supervisor (medium-term, Zambia) • Set out detailed requirements to avoid conflicts of interest for members of the Management or Executive Boards and all staff members of the National Bank of Moldova. Equity ownership of any supervised institution must be prohibited (short-term, Moldova) • Implement upgraded regulations on banks' governance, internal controls and risk management (immediate, DRC).
AML/CFT	<ul style="list-style-type: none"> • Strengthen supervision of preventive AML/CFT measures related to politically exposed persons (short-term, Guinea-Bissau) • Amend the AML/CFT Law and related regulations to ensure compliance with the FATF standard (immediate, DRC) • Enhance the use of financial intelligence related to corruption in investigation (Equatorial Guinea, CAR)

Sources: Governance Diagnostic Reports for Moldova, Guinea-Bissau, DRC, CAR, RoC, Mozambique, Equatorial Guinea Zambia and Mali

B. Impact of Governance Diagnostics

8. Governance diagnostics have informed IMF engagement with the membership.

Recommendations that derive from the governance diagnostics have regularly featured in subsequent surveillance and Fund-supported programs. Recommendations have been reflected in program conditionality to support the implementation of key governance reforms (most often on fiscal governance and anti-corruption framework), in a transparent and accountable manner, and have informed the dialogue with country officials on strategic directions for improving governance, integrity, and the rule of law during the program period. For instance,

- In Equatorial Guinea, the diagnostic recommendations were basis for 3 Prior Actions, 5 Structural Benchmarks and 28 MEFP commitments undertaken by the authorities.
- In Guinea Bissau, the diagnostic recommendations resulted in 11 Structural Benchmarks in the ECF and continue to be reflected in the IMF's dialogue with country officials.
- In Moldova, diagnostic recommendations on rule of law and anti-corruption institutions were prominently featured in the subsequent program.

In some cases, however, such engagement was interrupted when a program went off track, or due to an abrupt change in government (e.g., military coups in Sudan and Mali). Overall, governance diagnostics inform longer term engagement on governance and corruption with country authorities. To illustrate this long term impact of diagnostic reports, it is useful to refer to the first governance diagnostic supported by IMF staff and published by Ukraine's authorities in 2014, which has been a precursor for the diagnostic reports discussed in this paper. Box 1 below summarizes the experience with the implementation of anti-corruption recommendations over many years after the publication of the report.

Box 1. Outcomes of Ukraine's 2014 Governance and Corruption Diagnostic

In 2014, with staff support, Ukraine's authorities published a diagnostic report analyzing key corruption vulnerabilities and outlining a roadmap for anti-corruption reforms. Following the "Maidan" Revolution, the new government had identified governance and anti-corruption as a top priority. The report, published as a policy commitment under the IMF-supported program, highlighted the pervasiveness and oppressive nature of corruption in the country. Powerful blocks of political and economic elites were seen as entrenched throughout public institutions and the economy (i.e., state capture). The state agencies responsible for enforcing anti-corruption frameworks (e.g., police, prosecutor general's office, and judiciary) were viewed as the most corrupt public institutions, which had abused their powers to benefit the elites. The report notably concluded that, while formal frameworks were overall aligned with international standards, their implementation to high-level corrupt officials was lacking. A credible threat of consequences for corrupt acts had to be enforced, particularly by establishing independent enforcement agencies to hold public officials accountable and prevent them to benefit from the proceeds of corruption.

Informed by the diagnostic report, Ukraine has achieved significant progress in operationalizing a robust anti-corruption infrastructure. Under the IMF-supported programs and with support from capacity development providers, the pillars of the new anti-corruption infrastructure were established in succession: investigation (the National Anti-Corruption Bureau in 2015); prosecution (the Specialized Anti-Corruption Prosecutor's Office in 2017), and adjudication (the High Anti-Corruption Court in 2019). Members of parliament, ministers and judges have since been subject to corruption investigations, prosecutions, and convictions, including by relying on the implementation of other reforms contemplated in the diagnostic report such as asset declarations, the criminalization of illicit enrichment, and AML tools. These agencies have continued to operate despite the war demonstrating sustainability of the reform efforts. With time, judicial corruption became a critical issue, as vested interests were seen as misusing the judicial system to reverse reforms. The authorities subsequently engaged, in the context of the Fund-supported program, in targeted reforms to strengthen the rule of law and enhance the independence, integrity and accountability of judges, specifically by improving procedures for competitive selection for the members of the judicial self-governance body.

9. Diagnostic recommendations have informed the Fund’s CD, but the integration can be improved. The follow-up on the diagnostic for the Republic of Congo is among the good practices, as the authorities adopted a new comprehensive anti-corruption law and implementing regulations on conflict of interest, along with the law on asset declarations for public officials with IMF’s technical assistance. CD on anti-corruption law and AML systems were provided to Equatorial Guinea and Paraguay respectively.

C. Engagement with Stakeholders

10. Governance diagnostic missions have been a catalyst of governance-related actions by various stakeholders. All diagnostic exercises sought close engagement with other stakeholders, such as civil society and international partners, to collaborate on governance reforms. IMF teams usually meet with bilateral and multilateral donors, and other development partners (UNODC, UNDP, EU, FCDO, GIZ, USAID, SIDA) during or before the missions to seek their perspectives. In some cases, experts from the World Bank (Peru, Sudan, Zimbabwe) or the IDB (Paraguay) participated in the assessments, which helped ensure fuller collaboration. Further, representatives of civil society (e.g., NGOs, academics, association of lawyers, business associations) were also consulted.

11. In some countries, governance diagnostic reports were used by the authorities and donors to prepare a comprehensive governance strategy. In the Central African Republic (CAR), for instance, the IMF, the World Bank and the United Nations Office on Drugs and Crime supported the authorities in developing an action plan to combat corruption and improve governance. Mission teams found the engagement with other international organizations and civil society as essential to refine the scope of the diagnostics and benefited from these stakeholders’ experience and expertise. Conducting governance diagnostic was helpful to both donors and authorities as it raised awareness on some critical governance challenges at the government level.

D. Lessons Learned from the Experiences with Governance Diagnostic Assessments

12. Governance Diagnostic Assessments have guided subsequent IMF actions, including surveillance, and governance-related program conditions. The exercise has regularly helped to shape the core of the Fund’s engagement, influencing the substance, sequencing, and prioritization of the Fund’s program of work. They are an important part of the long-term engagement on governance and anti-corruption. Country-tailored recommendations from many assessments have influenced government actions and have been reflected in the adoption and implementation of reform measures. Continued follow-up on the diagnostic recommendations, including through targeted CD, would strengthen the implementation.

13. Continued focus is needed to tailor each exercise to country circumstances, while establishing greater structural and analytical consistency. A single template for all diagnostic

assessments would not appear appropriate in light of the specific risks and vulnerabilities faced by each assessed country, but there exists space for greater consistency in the content, approach to analysis of governance weaknesses and corruption vulnerabilities in key state functions, processes, reports, and the manner in which they are integrated into follow-on actions. Drawn from good practices in most recent diagnostic assessments, the value of the effort and the follow-up would be enhanced by (i) consistent in-depth discussion of the severity of corruption, including analysis of corrupt practices and networks, (ii) increased focus on governance weaknesses that create corruption risks, (iii) dedicated section on anti-corruption reforms, and (iv) identification of limited number of actionable priority recommendations.

14. In line with the 2022 Fund policy on engagement with Fragile and Conflict-Affected States, a careful balance needs to be sought between fragility/political economy constraints and the need for tackling governance weaknesses and corruption vulnerabilities. Fragile states are often associated with systemic corruption, which creates and exacerbates governance weaknesses. Governance diagnostics in such jurisdictions require careful consideration of the stability of the local environment, adjusting reform timelines in line with operative conditions, while ensuring adequate leverage from development partners to amplify the impact. At the same time, governance diagnostics can prove to be particularly useful in informing the Fund's engagement in FCS context.

15. Analysis of the severity of corruption, and corruption risks in the six state functions should more closely guide the formulation of recommendations, to effectively inform subsequent work by Area departments. Where corruption risks are deemed high and widespread, a deeper understanding of the nature and severity of corruption and identifying the most macro-critically relevant corruption vulnerabilities should facilitate the selection of issues to be addressed and the adoption of a holistic and integrated approach to the analysis. In this regard, having an in-depth discussion of corruption networks and the political economy helps set the stage of the analysis and recommendations for each state function.

16. Requests for governance diagnostics should be carefully sequenced with other CD activities. One way to foster synergy between traditional CD and governance diagnostics, is to use diagnostic reports as a strategic basis for CD engagement with member countries on key state functions.