RECASTING GOVERNANCE FOR THE XXI CENTURY

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I. INTRODUCTION -- *Barking at the wrong tree*

It has become almost trite to invoke the realities of globalization. And yet, it is remarkable to observe the difficulties and dislocations the world is facing to cope with the implications of such major paradigm shift – from the fall of centrally planned economies in the former Soviet block; the increased mobility of goods, services, funds and people across borders; to the consequent diminishing relevance of the nation-state and Governments, the declining importance of countries unable to adapt their institutions and economies to the more flexible conditions around the world, and the associated shift of the center of gravity from the Mediterranean and the Atlantic towards the Pacific rim.

Nowhere is the disconnect between reality and past frames of reference more evident than in the political and governance debate. While much of the literature still harps on the North-South, East-West, Left-Right (rather than on the Height-Depth) divide, in practice, societies that have generated rapid development have left behind such battles in favor of more empirical, cooperating and adaptive policies aimed at moving with and creating, rather than resisting the tide.

By the same token, a multitude of international conventions, principles, standards and pacts, built essentially on obsolete institutions, too inflexible to deal with a more dynamic, agile and creative world, is unable to engage the forces unleashed by the swift technological change. And while this is producing unprecedented development, it is also facilitating corruption, money laundering, trafficking of human and financial resources at unprecedented levels, which institutions and politicians so eloquently (and ineffectively) condemn. Contrary to popular belief, the greatest problems are not centered on how to stop and control these dangerous side effects, but in the failure to understand the forces at work. In fact, many of the “solutions” being promoted are based on strengthening controls and monitoring vehicles that don’t have remotely the agility of today’s economic forces, thereby barking at the wrong tree, for lack of proper diagnoses of the problems to be resolved.

Of course, even the most serious persons are sometimes overcome by the fascination of mere forms, and manage to convince themselves that they are doing something if they hold impressive international meetings with a mass of documents, conferences at which facts are recorded, decisions taken, proclamations and press releases issued. The ceremony of such gatherings is capable of losing itself in this sort of thing just as much as government officials, NGOs and others who get blinded by the panoply of journalistic reports, funding for all kinds of “follow-up”, and so much activity busily engaged in doing nothing that is of any practicality. If anything, this points towards confusion between being active and doing something with impact on the ground.

There is thus a need to guard any serious discussion against the army of ideologists, propagandists, public relation officials, interpreters and apologists, who essentially sandbag the issues, embellish the system as it exists and create artistic monuments to rhetorical ideas espoused in such gatherings. They tend to increase confidence and optimism of those who benefit under existing conditions. More seriously though, they leave institutions, policies and other vehicles of action hopelessly behind the curve, and a far cry from what is needed to deal with the emerging conditions.

Sooner or later, these approaches will run out of ammunition, and at the end of the day, the best antidote will require more than exhortation. To alter the situation, and open minds to the implications of the changing world around us, we must understand first the change that is taking place. This paper tries to tease out the different elements that explain societal conflicts, whether war or corruption, and the underlying governance and institutional issues – and accordingly the possible ways towards reforms that respond better to the issues that must be confronted.

II. <u>THE ISSUE</u> – *Fighting yesterday's battles in a changing world.*

Much of current day debate, both academic and the media, tends to focus on the resource dimension of and leadership perpetuating corruption, dysfunctional societies and even armed conflict. If only one could get rid of troublesome leaders or curtail resources flows to them – so the argument goes – one could severe the ties that sustain such state of affairs, and bring about an end of corruption and various manifestation of conflicts. If life were that simple, surely we would have had a more peaceful and better operating world long time ago. The sheer stubbornness, longevity and intractability of so many conflicts, even in the face of such pellucid and blazingly simple suggestions, are clear indications that we must have a better understanding of the underlying forces and incentives that fuel such confrontations, and thus better grounded strategies for dealing with the issue.

Of course, this should not be interpreted as a suggestion that controlling the resource flows should not play a role in conflict resolutions and the battle against corruption. But, one has to be keenly aware of the weaknesses of institutions (not to speak of the agility and resourcefulness of money launders, terrorists, combatants and other such players) and limitations of trying to solve such problems through the money flows -- or "the supply side", so to say. Accordingly, this note, while concentrating on "the demand side" (i.e. the part that generates the funding requirements of conflicts), takes the view that once one understands the nature of the problem, one can devise and respond through appropriate policies and actions on both the supply *and* demand side of the problem -- just as one can only clap with two hands.

The following thus attempts to sketch out: (i) the particular *"nexus issues"* that makes countries vulnerable to conflicts; (ii) some of the *"supply side"* responses currently in place and their basic limitations; (iii) key underlying causes for dysfunctional societies that create conditions for corruption and other societal conflicts, including armed confrontation (i.e. the *"demand side"* of the problems) and, what can be done about them; and (iv) the bringing together of supply- and demand-side responses to the issues at hand.

Having said that, we must disabuse anyone from thinking that there are quick fixes, standard solutions, one-size-fit-all approaches. There is no such thing: every country, crisis or conflict is absolutely situation-specific. That being said, while each conflict has its own particularities that need to be understood, there are nonetheless some common patterns that tend to magnify (or attenuate) conflicts. They give some valuable hints – just that: hints – of where solutions can be found.

III. THE MISSING LINK – *You can't fish with a tennis racket*.

A heavy concentration of conflicts is concentrated in the poorest regions of the world. There is by now a growing recognition that strategies must be put in place to address the conflicts themselves, but also the need to pre-empt the factors that contribute to them. In many countries embroiled in such conflicts there is a fundamental problem of failed governance. Conflicts (both civil wars and between neighboring countries) are oftentimes motivated and sustained by the economic self-interest of belligerents, who find conflicts a viable means of accessing wealth or sustaining conflicts.

Where institutional and associated governance structures are weak, leaders can easily remain in power (be it in government or rebel/guerrilla movements) through patronage, oftentimes of the military or armed groups, while they may wage war on their real or imagined enemies. Such strategies require funds – money to buy arms and bribe allies to secure loyalty. Consistent with these developments, all surveys on international corruption rank the arms and extractive industries as being some of the major sources of international bribery.

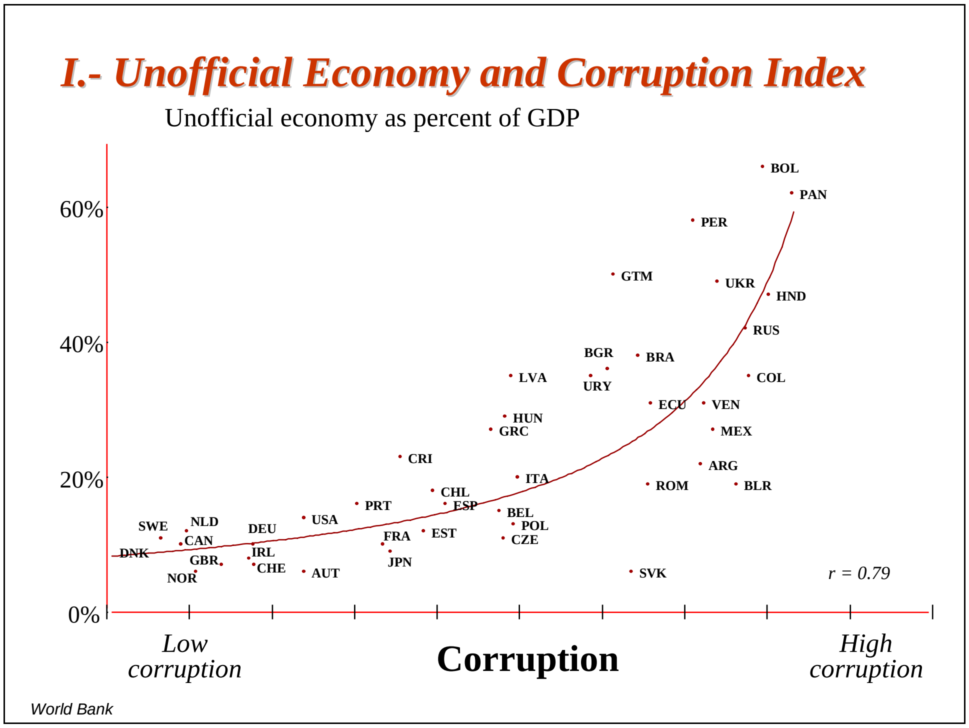
Under the circumstances, it is no accident that a great many conflicts take place in poor, yet resource-rich countries. Inevitably, global companies with activities in countries with conflicts are seen to be complicit with their leaders and the provision of the funding that support their administrations, or rebel groups, as the case may be. If such revenues were "controlled and tracked", they would not help fuel conflicts. Moreover, it they were effectively and transparently managed, they could contribute significantly to successful growth and poverty reduction, and thus reduce an important source of grievance and conflict. However, all too often, the State, rebel groups or other institutions with access to these resources are unaccountable to the ordinary citizens and the payments become vehicles for embezzlement, fraud and corruption. As a result, such countries tend to perform poorly in terms of economic development and governance indicators.

Tempting as it may be to pinpoint to the above-mentioned governance-natural resources-corruption-conflict nexus, in actual fact it begs the question in which direction these factors work; which is the cause and which the effect – and ultimately where to put the emphasis or sequence for corrective action: on governance? the money flows and corruption? the conflict per se?

A few hints give us some pointers. The post-conflict proceedings of a number of enquiry committees, such as the Chilean and Peruvian Truth and Reconciliation Commissions, when interviewing insurgents, combatants, soldiers and their families have hit on a a variety of factors – which had little to do with money or access to resources, which have triggered and fueled incredibly violent conflicts. In Peru (where 30,000 people lost their lives, 5,000 disappeared and half a million were displaced) and in Chile (with more that 3,000 deaths and disappearances) the fights were driven by serious political impasse, great disparities of opportunities and associated ideological motivations leading people to take up arms to alter the established order by violent means.[1] In Peru, more than in Chile, they concentrated their activities in the poorest regions of the country, and sustained their fight through kidnappings of peasants, terror and even enslavement. In both cases, they were ultimately overwhelmed by military might and confrontation, leading (mainly in Chile) to institutional and policy reforms that set the country on a radically different path from the past, recasting of policies and institutions, new political leadership and, ultimately, economic development. Perhaps inevitably, this approach while focusing almost single mindedly on "demand side" issues of the type mentioned on section V below, eventually led to the formation of more nuanced approaches combining legal proceedings, mutual recognition and compensation, and social inclusionary policies aimed at healing the wounds of the abrupt an bloody termination of conflicts.

Surely, the Chilean and to a lesser extent Peruvian situation, where the weight of the Government and its military could unilaterally "impose" at least a semblance of modus vivendi, is not replicable in many cases where there are weak States, more vulnerable to the development of alternative sources of power. Even so, it took Peru and Chile the better part of the first ten years of Fujimori and five of Pinochet's regimes, respectively to overcome the violent conflicts. In Colombia, on the other hand, the stalemate between Government and insurgents is running over fifty years, with some 100,000 people having been killed, 2 million displaced and living a the fringe of society, and another million having left the country since 1980, with no clear end in sight. Whereas rebellious groups in the three countries had their origin in social, economic and ideological grievances, over the years, in the case of Colombia, armed groups (both guerrilla and paramilitary) have increasingly relied on drug cartels, which fuel the conflict by financing the armed groups in exchange for protection of their business – in essence challenging the State and substituting it by providing basic services, including administering extralegal justice, education and social services. With an efficient economic base grounded on drug trade, and other inhumane methods such as extortion, kidnapping and forced contributions, they are in fact in war with the civilian population, the State and the rule of law.[2]

Moreover, in weaker States, mainly in Africa, these problems manifest themselves in more problematic ways. Where governments have been captured by particular interest groups, for their benefit, increased corruption tend to "crowds out" the economy into the informal sector (Graph I). This provindes every incentive for people to go underground to make a living, thereby "hollowing out" the States by de facto replacement "shadow states". This in effect leads to privatizing public benefits for for the leaders for patronage of those who support them – either financially or militarily.

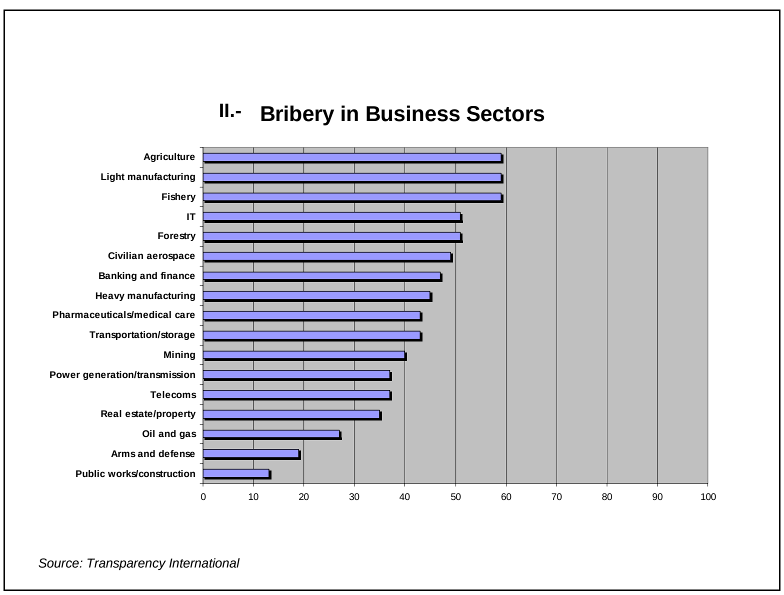


Clearly, this is a recipy for corrupt, unaccountable and thus unresponsive governments, which tend to cling to power through repression. Sooner or latter, this leads to conflicts that cannot be controlled. Put in another way, unlike interstate conflicts, which often mobilizes national unity and strengthens societal cohesiveness, violent conflict within a state can be caused by and/or weakens its social fabric. In the end, as evidenced in much of Africa, sustained conflicts divide the population by undermining interpersonal and communal trust, destroying the norms and values that underlie cooperation and collective action for the common good, and increasing the likelihood of communal strife.

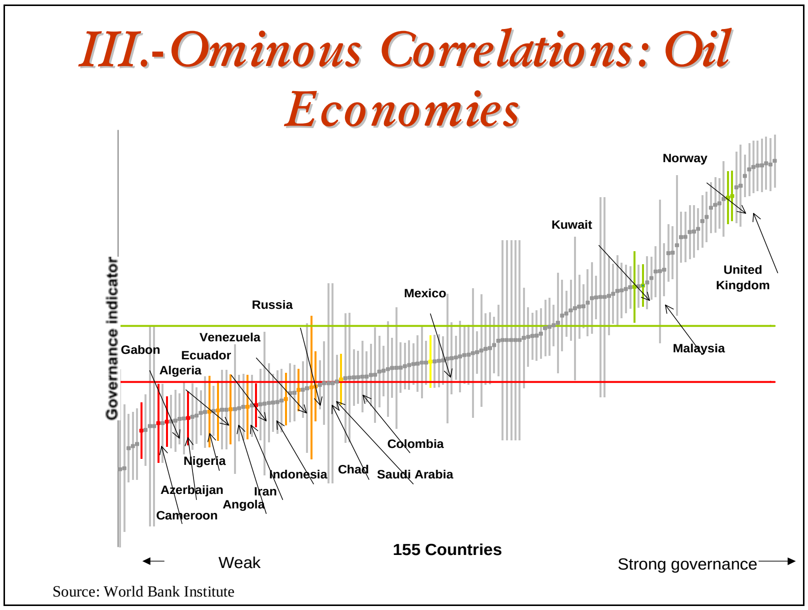
As a result, relations start to develop predominantly based on kinship, ethnicity, religion, or social strata, largely as protectionist, defense mechanisms that form a safety net for basic survival. While surely these conflicts oftentimes are driven by other causes – from raw power, ambitions of warlords, simple prejudice and other such factors, the above discussion points towards some economic dimensions of conflict and illustrate how issues of management and governance affect social cohesion. If not property addressed, they can magnify or even drive people into violent conflict with several conditioning factors, such as inequality, indignity and exclusion.

In all, what needs stressing is that often overlooked are the governance elements triggering or sustaining such conflicts: to one extent or another – from Chile and Peru, in one extreme, to perhaps Rwanda or the Congos, in the other - governments with sectarian policies or run for private benefits, create conditions for societies, political movements, clans, or families having to fare for themselves to procure "public goods" (such as support of the weak, education, etc.) - - the exact obverse of a functional society. More often than not, this state of affaires damages the values and social relations that bond communities together, as well as the bridges between civil society and the State, which impedes the ability of either communal groups or the State to recover after hostilities cease.

A few indicators provide strong hints on what generates such behaviors. Transparency International's Bribers Payers Index (BPI), which ranks the leading exporting countries and sectors in terms of the degree to which their companies are perceived to be paying bribes abroad, indicates that corruption is widely seen as playing a significant role in international trade. The data provides a disturbing picture of the degree to which leading exporting countries are perceived to be using corrupt practices – buying business for them, getting laws regulations issued for their benefit, supporting regimes to serve their interests, and ultimately undermining the solidity of host Governments. Specifically, business-executives and professionals in leading emerging market countries see international bribe paying to be greatest in the public works and construction sectors, followed by the arms industry (Graph II).



Particularly disturbing, however, is the high corruption associated with extractive industries – the economic bedrock for many developing countries. Take the case, for instance, of petroleum (the third highest bribing sector) where countries like Nigeria, Indonesia, Algeria export anywhere between US $2 to 35 billion, depending on oil output volumes and prices - - and yet their performance in terms of GDP growth, human resource development and governance is significantly lower than countries in the same income per capita levels.[3] It should thus not be surprising that petroleum-producing countries tend to fall in the lower percentile categories of governance ratings, where corruption figures high (Graph III):



More importantly, it is striking to see the heavy concentration of countries plagued with internal conflicts that fall in the higher end of corruption perception indicators – and in the lower end of governance ratings.

Moreover, the secondary effects, in downstream petroleum activities (transportation, refinery, inland distribution), are equally devastating though much more widespread. Petroleum products play a pivotal role in Sub-Saharan Africa's economic development. Their purchase absorbs 20-35 percent of export ratings for the bulk of the countries in the region, and generates approximately 40 percent of tax revenues (and even higher shares at current price levels) – thus constituting the single largest item in the balance of payments and fiscal revenues for most countries in this region. The amount of disappearing resources from petroleum trade is more than 50% higher than the whole of World Bank Group net disbursements to Sub-Saharan Africa put together[4] and thus ought to be much higher in the policy agenda of countries and international development agencies. In fact, some 65% of such "losses" occur as a result of discretionary decisions, where local authorities are involved (i.e. requiring no investments of any sort), and the bulk occurs in lower-income countries (Graphs IV and V) – depriving them from financial resources for development and increasing the prospects for grievance and tensions.

IV.- Potential Savings

V.-Government Involvement and Levels of Inefficiency

The issue is by no means restricted to petroleum. The nature of diamonds and this industry's operations create opportunities for illicit trade. Diamonds are a high-value commodity easily concealed and transported, are mined in remote areas worldwide, and are virtually untraceable to their original source. These factors allow diamonds to be used in lieu of currency in arms deals, money laundering, and other crimes. Further, the diamond industry lacks transparency, which limits information about diamond transactions. As a result, "conflict diamonds" are used by rebel movements mostly in Africa to finance their military activities, including attempts to undermine or overthrow legitimate governments. These conflicts have created severe humanitarian crises in countries such as Sierra Leone, Angola, and the Democratic Republic of the Congo.

The same problem can arise even in trade of bulkier commodities, such as in the forestry industry, where illegal logging is estimated to easily range between over 40% of countries' production (in Colombia) all the way up to 90% in Cambodia, with many countries ranging in between, like Myanmar (80%), Indonesia (50%), Brazil (85%). Examples of illegal practices in the forestry sector include: unlawful occupation of forest land by rural families or corporations, international trade in protected species, logging outside concession boundaries, logging in protected areas, under-grading and misclassifying species, timber smuggling, transfer pricing in timber trade, timber processing without a license, etc.

In sum, poverty, inequality, misuse of the government apparatus through widespread corruption are often-times the grievances that trigger conflict – even armed ones. But these problems get particularly exacerbated by the specific pathologies of rent-seeking and corruption that affect weak States that are highly dependent upon natural resource exports. While corruption has deeper economic and political causes than the distortions of natural resource dependence, weak public administrations, and its attendant absence of rule of law, combined with natural resource dependence have been associated with particularly virulent and intractable forms of systemic corruption.

Accordingly much greater attention is needed in addressing: (i) the specific institutional, legal, and other governance factors that permit and perpetuate this kind of behavior; and (ii) the way natural resource dependence exacerbate corruption. In general, when resources come from the sun and the earth, rather than hard toil, the temptation is great to manage the surpluses as if they were the product of loot. As long resources are plentiful or there is even a moderately functioning State, peace can be "bought" through massive subsidies (such as in Argentina or even Nigeria). But while this may not be a long-term sustainable situation, the nature of natural resource dependency creates particularly difficult barriers to reform, by generating an entitlement mindset in the population while freeing States from the need to tax their citizens, thereby removing an important incentive for accountability and transparency, be it private or public. It is in this crucible that one has to find the way to diffuse the entangled interests that generate conflicts.

IV. **CURTAILING THE "SUPPLY SIDE"** - *Emptying the ocean with a teaspoon.*

A view has emerged over recent years that one must tighten up controls of money flows, which generate corruption and sustain conflicts. There is no shortage of such initiatives.

At the ***Governments*** levels, a number of initiatives have been taken that reflect a measure of awareness and goodwill:

- Twenty-five countries signed the landmark *Inter-American Convention Against Corruption* in March 1996, two years after the issue of corruption was put on the agenda of the Summit of the Americas by the leaders of the Western Hemisphere. The Convention requires countries that have not already done so to criminalize transnational bribery and all illicit enrichment. Other provisions include building commitments to provide greater mutual assistance laws and to establish a framework for cooperation on extradition. In addition, the Convention encourages countries to adopt a wide range of laws and regulations to prevent corruption. These measures include conflict of interest rules, disclosure of assets of high public officials and their families, establishment of national organizations for the oversight of such laws, protection of whistleblowers, and open government procurement. Implementation, however, has been poor, and a peer review system was set up only in 2003, which may well end up covering all countries in two or three years time.

- Similarly, in late 1997, thirty-four countries signed the *OECD Convention on Bribery of Foreign Public Officials in International Business Transactions*. The purpose of the Convention is to criminalize corruption of foreign officials and to end the tax deductibility of bribes, thereby removing the associated fiscal incentives. This is a good first step forward, and one that provides a sound, though more focused, framework for an international anti-bribery system. But the level of awareness among the business community of the existence of such laws remains exceedingly low[5], which may explain the seemingly little impact of the precursor of this Convention – the Foreign Corrupt Practices Act in the USA.

- Other Conventions, such as the *United Nations Convention against Corruption*, have been adopted and are similarly aimed at advancing the same cause, with varying degrees of advancement (though hardly discerning enforcement).
- Multilateral development banks have similarly begun to play their role in their respective areas of expertise and responsibility. The *IMF* has started to restrict its operations in countries where the level of corruption is deemed to negatively affect in a material way their economic performance. To the IMF Code of Good Practice on Fiscal Transparency and associated reports provides on the other hand a solid set of standards for fiscal transparency, and does not involve itself with the vehicles to publish, disseminate, and create constituencies for such data to be used in countries for accountability purposes.

- The *World Bank* has initiated a more comprehensive program. It introduced sanctions on firms and governments engaged in corrupt practices. Under this arrangement, it bans firms that offer bribes from future Bank financed procurement worldwide. It would also cancel loans to governments whose officials solicited bribes. So far, some 260 firms and individuals (mostly medium and small ones) of 24 (mostly of developing) countries have been debarred since 1998, and no loans have been hitherto cancelled on these grounds.

At the ***Sectoral*** level, various Global Business Codes have been developed, including: International Chamber of Commerce (ICC) Rules; Pacific Basin Economic Council (PBEC) Charter; and the TI Business Principles for Countering Bribery. Most of them are at the principles formulation stage, with voluntary implementation by members, without independent verification arrangements – and thus are difficult to evaluate in terms of their actual implementation, impact or results. Special initiatives meriting particular highlighting are:

- The *Wolfsberg Anti-Money Laundering Group* is strengthening "know-your customer self-regulations" of major banks[6] but in practice money laundering takes place in poorly regulated jurisdictions, and other financial intermediaries like money houses, insurance institutions and the like. For the present, money-laundering and anti-corruption arrangements among countries are in their infancy, their reach of institutions still limited and largely untested, and enforcement arrangements too cumbersome to make much of a dent in the problem. A broader effort aimed at establishing an anti-money laundering effort of universal application is under way through the *Financial Action Task Force on Money Laundering*[7].

- Similarly, the *Kimberley Process Certification Scheme*, which went into effect on January 1, 2003 after some two years of negotiations aims at certificating diamonds trade among some 40 countries to prevent the flow to violent insurgencies. Legislation is also being developed to address U.S. consistency with the Kimberley Process. The United States General Accounting Office (GAO) was asked to assess the challenges associated with deterring trade in conflict diamonds. GAO's assessment of the Kimberley Process plans for international diamond certification scheme found it incorporated some elements of accountability. However, GAO noted that the scheme is not based on a risk assessment, and some activities experts deem high risks are subject only to "recommended" controls. Also, the period after rough diamonds enters the first foreign port until the final point of sale is covered by a system of voluntary industry participation and self-regulated monitoring and enforcement[8]. With no powers to compel compliance by either the diamond industry or governments, the agreement relies essentially on faith. These and other shortcomings provide significant challenges in creating an effective scheme to deter trade in conflict diamonds

- Other efforts, like the *Mining, Minerals and Sustainable Development* (MMSD)[9], have so far been rather conceptual, with little in the way of concrete, on-the-ground application. In response to these concerns, ICMM (the mining association for sustainable development) which received the mandate to follow-up on the MMSD work is developing a more concrete action plans with suitable verification arrangements. The *Extractive Industries Transparency Initiative*, while focused on resource revenues, have so far concentrated on awareness raising of the importance of disclosing tax and other payments to host countries and getting them to adopt frameworks to track tax payments of the industries concerned. On the other hand, it does not address either the downstream resource deflections referred to above or the overwhelming effect such resources have on economic management in host countries, with their consequent governance and anti-corruption implications. They have been successfully addressed in some economies not covered by the initiative, such as Chile, Botswana, Norway or Alaska. This broadening of focus is essential, by preventing moneys from being siphoned subsequent to disclosure and collection; by the manner they are being managed, saved or disposed.
- In forestry, work is only commencing among a group of interested companies and NGOs through *Forestry Integrity Network* to size up the problems and possible actions for the future. A group of donors has recently approved a research proposal aimed at improving forest governance and containing corruption. The project will involve a Forestry Integrity Network in monitoring corruption in target countries and organizing regional workshops to identify best practices and possibilities for their replication.

Finally, on the ***Private Sector,*** there are differences of opinion about the value of corporate anti-corruption programs and associated codes of conduct. Given the many parties involved, the "going alone" practices have proven to be particularly difficult, if not ineffective judging by the widespread corruption in countries and sectors where companies with such codes operate. Many in the business community believe that self-regulation, through for instance *Business Principles for Countering Bribery* is the right solution and that it is preferable to government regulation. Others argue that self-regulation is a sham and only government action can be expected to curb corruption. When seen, however, as a component of a comprehensive anti-corruption program, they could provide a stimulus to more business-like and effective economic activity. Internal reviews of several companies' programs tend to agree that they are not a substitute for government policies and regulations: both are needed and each reinforces the other, and coalition-building approaches with relevant constituencies have tended to be more effective.

A "best practices" study undertaken by Transparency International USA of anti-corruption programs used by major American companies[10] stressed that whether a code of conduct is only a piece of paper or it controls corporate behavior, depends on the compliance program the company uses. These include: (i) unequivocal commitment by top management, including hands of top-management involvement in policy formulation, articulation and implementation, (ii) clear policy statements that the company prohibits employees and third parties representing the company from offering anything of value, directly or indirectly, to government official to influence or reward an action; (iii) detailed guidelines regarding gifts and entertainment, and strict enforcement and compliance programs with applicable laws and regulations regarding corporate political contributions and their disclosure; and (iv) the existence of a system of internal controls and record keeping that ensures that company books accurately reflect its transactions, overseen by an audit committee, composed of outside directors and associated internal reporting.

The sheer absence of visible, discernible improvements and abatement of conflicts despite this flurry of activity should be a warning that something important is missing. Under the circumstances, proposals for cutting or controlling flows of resources require the burden of proof – rather than benefit of doubt, at least when applied across the board, with little adaptation to individual country circumstances.

V. TACKLING THE DEMAND SIDE – *Better vaguely right than definitely wrong.*

Governance dysfunction and attendant corruption occurs when economic opportunities for it prevail and political will to combat it is lacking. In a way, corruption is a symptom of fundamental economic and political problems. Addressing them effectively therefore requires dealing with the underlying economic, political, and institutional causes.

This requires looking at the demand side (i.e. the “receiving hand”), where empirical evidence strongly suggests the following striking patters[11]:

- Corruption tends to be high, the weaker the *rule of law* and the institutions that impart justice in the countries concerned. Almost by definition, this makes zones of conflict easy prey for corruption.
- Similarly, the more societies are pluralistic and thus open to scrutiny, the lower the levels of corruption. The empirical evidence suggests that countries with the strongest *civil liberties* tend to have, government investments with high returns the greater their public accountability, and that there is an interrelationship among civil liberty, civil strife and public performance[12].
- It also stands to reason that the higher the *professional levels in civil service*, or the sheer existence of a credible public administration (a particular neuralgic issue in zones of conflict), the lower are the perceived levels of corruption.
- Conversely, more often than not, at the root of the problems, one can find excessive *discretionary powers* of leaders and administrations -- as the old saying goes: “power corrupts, absolute power corrups absolutly.”

The foregoing essentially points towards corruption as being an entrenched symptom of misgovernance often reflected in patronage, red tape, ineffective revenue generating and public service agencies -- and under extreme conditions, a source of conflicts. At the same time, corruption, and its attendant breakdown in societal governance, can be reversed by dealing with the underlying public-private sector interface. When officials in charge of public resources are accountable to their citizens, decision-making can become participatory. In turn, a participatory process can be the cornerstone to reform “sick” institutions and improve the welfare of citizenry. In the end, corruption is an entry point to deeper public/private interface reforms.

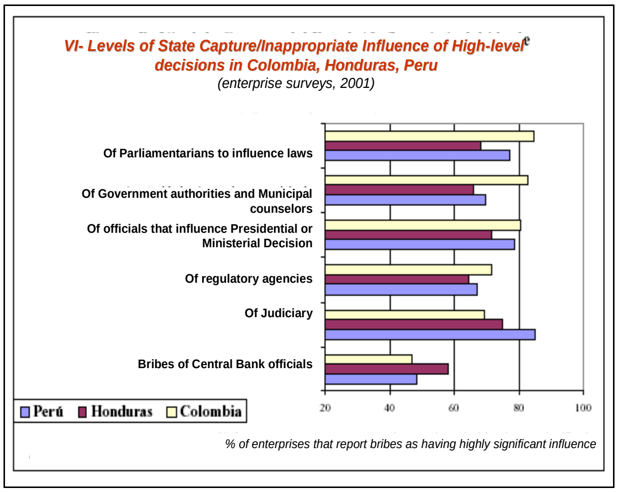
The main message to be drawn from the previous discussion is that the fight against corruption and its ramifications in conflict should not begin or end with fulmination about ethics or the need for a new set of attitudes. Instead, it should dispassionately look for ways to reduce monopoly power, limit and clarify discretion, and increase transparency, all the while taking account of the costs, both direct and indirect, of these ways. After all, the above suggest that corruption is a crime of calculation, not of passion. People will tend to engage in corruption when the risks are low, the penalties mild, and the rewards great.

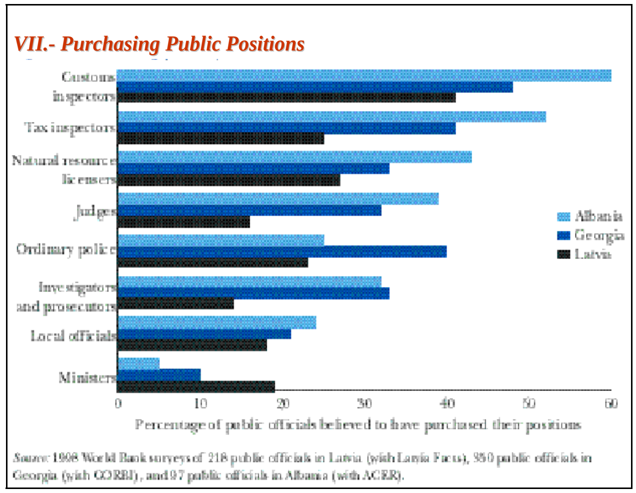
The secret of successful reform should thus focus on changing policies and systems, rather that hunting for isolated culprits, adding new laws and regulations, or calling for a moral renovation. When public officials are paid meager salaries and offered no rewards for exceptional performance, and when penalties against the corrupt are rare and mild, we can expect corruption to flourish. Based on the empirical evidence noted above, successful reforms aim at changing in habits and attitudes by addressing these systemic problems, and acting on the following five “levers” for reforms:

- ***Empowering*** and enabling ***civil society*** that protects the rights of individuals and of groups while holding state institutions accountable to the rule of law that: (a) ensure freedom and dissemination of information; (b) provide for publicly driven hearing or similar arrangements for drafting laws, regulations or other vehicles of governmental acts; (c) develop media, civil society organizations, etc. to engage citizenry and level the playing field between government and the private sectors; and (d) build checks and balances to ensure: independent and effective judiciary, decentralization with accountability, and support civil society oversight arrangements.
- ***Depoliticizing public administration*** and public finance through setting up the rudiments of: (a) meritrocratic civil service; (b) transparent, monetized public sector with adequate remuneration; and (c) associated accountability in expenditures -- by setting up independent treasury, audit, procurement functions and processes, and performance-based management processes.
- ***Establishing accountability of political process and finance*** through: (a) disclosure of parliamentary or equivalent legislature votes; (b) transparency in party financing; (c) asset declaration, conflict of interest rules and/or similar actions to build transparency of associated sections of political processes, (c) disclosure, accounting/audit and other transparent governance arrangements for private enterprises.
- ***Building up mediating mechanisms***, requiring as limited institutional-intensive arrangements as possible to facilitate an enabling environment for the development of movements and entrepreneurs, however fledging, though competition and entry through: (a) competitive restructuring of monopolies; (b) regulatory simplification; and (c) reducing discretionary powers of public authorities.
- ***Supporting*** local efforts through ***global institutions***, by building up: (a) the transparency of their transactions, including their tax and royalty payments, imports and exports; (b) establishing business standards, associated internal control and enforcement arrangements; (c) debarring jurisdictions or countries, enterprises or individual engaged in corrupt practices; (d) strengthening money flow and trade oversight verification and self-regulation.

But here is where the commonalities end, and where the crucial country- and situation–specific situations begin. After all, there is one thing that is common to all countries: they are all different. The above-mentioned “levers of change” are the same for nearly every situation, but they can take you only so far, and play themselves out differently in every particular situation. To carry out effective reform programs one has to start by: (i) understanding and diagnosing how the specific corrupt system works in the particular country or regional context through surveys, workshops with key players, to pinpoint specific vulnerable areas that need corrective action; (ii) overcoming political and bureaucratic resistance, and garnering support by focusing on early wins, building alliances with relevant parties, to gain broad support and momentum for the needed reforms, etc.; and (iii) crafting a sequenced plan of action to heal corrupted systems, break the culture of cynicism, and build political momentum and transformation of government, civil society and enterprise sectors.

Graphs VI and VII illustrate, for example the extent and different focus of government capture in some countries, suggesting that in places like Colombia action needs to concentrate on elected offices like Parliament, the Executive and Municipalities, where as in Honduras or Peru attention needs to be drilled down on the Judiciary and its associated bodies to build up rule of law.





In countries emerging from strong and sustained civil strife, the institutional dysfunction is inevitably more widespread and thus require actions on a broader array of "levers of change", ranging from the government apparatus (executive, legislative judiciary) to independent oversight and watchdog bodies, civil society, media, etc. This requires an internally driven and homegrown process of renovation such as the one outlined by a broad group of civil society, government and private sector representatives in the Democratic Republic of Congo in September 2002, which came up with a series of actions, vehicles for implementation and constraints to overcome to raise awareness, reform public sector institutions, and develop necessary alliances.[13]

VI. MEETING SUPPLY AND DEMAND – *Focusing where the rubber hits the road.*

The above-mentioned initiatives should be seen as a beginning for addressing challenging governance demands in the new century. Quite apart of the specific constraints mentioned before, those initiatives that are more advanced tend to put the emphasis on issues of enforcement, greater transparency and controlling funds. So far, these efforts have three major shortcomings:

- *First*, with no local grounding, such efforts lack indigenous constituencies and thus that can only survive through continuing conditionality, institutional compulsion and increased dependency – a poor substitute for homegrown efforts that can assure sustainability.
- *Second,* for the most part, they tend to rely on: (a) gathering of information and evaluation that are scarce and expensive, which inhibits internal and external controls, (b) weak information-processing skills at both the individual and institutional levels; (c) weak incentives in the sense that good performance goes relatively unrewarded and bad performance based on self-regulation rather than independent or countervailing institutions tending to avoid “rocking the boat”; and (d) dependence on oligopolistic players who, left to their own devices, many collude to avoid confrontation.
- *Third,* while such controlling efforts have their place, the inherent inefficiency of government and international agencies, obsolete tools, inadequate legal environments, and ineffective doctrines of today's institutions limit the effectiveness of such approaches.

Accordingly, even after accounting for the imprecise nature of corruption and governance indicators, particularly their large margins of error, we would be hard put to establish tangible improvements of significance. Greater efforts are needed to “demand side” and home grown actions that can make governance improvements more sustainable and agile to meet changing conditions.

In those countries that have been able to combat corruption, and its attendant breakdown in societal governance, they have done so by dealing with the underlying public-private sector interface. When officials in charge of public resources became accountable to their citizens, decision-making has become participatory. In turn, a participatory process can be the cornerstone to reform “sick” institutions and improve the welfare of citizenry. In the end, corruption is an entry point to deeper public/private interface reforms, which aim at changing in habits and attitudes by addressing these systemic problems.

In the same way as poor governance issues can be the trigger, if not the actual cause, of many conflicts, strong societies with inclusionary institutions and social policies as manifested in conflict-mediating institutions, such as efficient and non-corrupt bureaucracy, are more likely to be able to prevent or withstand the socioeconomic and political shocks associated with internal conflicts.

The critical importance of well-performing public institutions and good governance for internal peace, development and poverty reduction has come to the forefront in the 1990s. Just as it was increasingly recognized in the 1980s that individual, targeted actions are less likely to succeed in a distorted policy environment, so it has become obvious that neither good policies nor good single-purpose actions or investments are likely to emerge and be sustainable in an environment with dysfunctional institutions and poor governance.

Of all institutions, the World Bank (and subsequently other multilateral development banks) has perhaps been the most open in recognizing this paradigm shift and responding with by a more comprehensive focus to development, including a broader approach to combating corruption.[14] At the same time, it is also clear that building or reforming public institutions is a complex task, both technically and politically. "First-generation" reforms, such as trade liberalization, could often be undertaken through the actions of a relatively small number policymakers and public managers. Institutional reform, however, typically involves fundamental changes in the "rules of the game" for a large number of civil servants and private citizens. Such changes are likely to require long-term and widespread commitment, in-depth knowledge, and extensive support and assistance, and above all, tailor-made solutions – not best-practices, but better-fit solutions. Even when reviewing the experience with individual tools, a survey of civil society monitoring practices of public procurement showed that the way to manage and apply them need strong adaptation to respond to local capabilities, institutional and policy contexts.[15]

While the broadening of *World Bank and other development institutions*'actions is a welcome shift, one must be aware of their fundamental constraints. First, the Bank (as other intergovernmental institutions) still has a technocratic and State-driven approach to problem-solving, with limited appreciation of the role of civil society, transparency, scrutiny, contestation, and the way of holding accountable countries' Administrations. As a result, mediating and empowering organizations, the institution of proper oversight arrangements with stakeholders' inputs, checks and balances play only a marginal, if not perfunctory role in the arsenal of Bank interventions.

Second, as to vehicles of assistance, the Bank has still essentially an outmoded, largely project-based, approach to providing assistance. This has served the Bank through much of its existence. However, with the rapid surge of private capital and human resources flows, with their attendant transfer of knowledge and technology, information market access and finance, the Bank has great difficulties to "compete", replicate or supplement the performance of the new players in the field. Accordingly, the unbundled approach the Bank uses in the delivery of services (through economic, sector/policy, project work) more often than not produces serious discontinuities and poor follow-up, with the result that the institution has great difficulties in "walking the talk" and delivering on what it recommends. This needs a profound recasting of its delivery instruments and perhaps internal organization.

Similarly, the beginnings of welcome shift in the *Extractive Industries Transparency Initiative*, which is evolving to introduce much needed demand-side concerns captured in part by Caspian Sea Revenue Watch.[16] The study recognized that, even as important is information about what the government receives for oil or other natural resources, so is an understanding of how this compares with what other countries are receiving , and how the government use the funds it receives from the sale of natural resources. Unfortunately, these efforts still are still overly driven by donors and their conditionality, whose record has been spotty at best.

That being said, the basic principles one can derived from more successful cases, to enhance the chances for success are:

- ***Checks and Balances***. One of the principal reasons for creating natural resources funds and/or developing special oversight on the generation and management of extractive sector activities is to help governments resist temptations to spend everything, at the expense of future generations. A separation of oversight powers creates layers of supervision into such resources and minimizes opportunities for their diversion.
- ***Transparency.*** Natural resources funds, or for that matter any forms of surplus management arrangements that operate behind a veil of secrecy are more likely to be diverted from their original goals. An aggressive disclosure minimizes opportunities for abuse – just as the proverb states, *sunlight is the best disinfectant*, and produces a sense of ownership with its consequent accountability.
- ***Public involvement.*** The more engaged a citizenry is in the fate of its country's resource revenues, the less likely it is that a government will risk public ire by tampering with such resources. With public involvement, the public expenditure management can serve effectively as a compact between governments and citizens.
- ***Depolitization.*** The more technical and non-discretionary the rules of surplus and public sector expenditures are (such as the establishment of thresholds for resource use or savings), state-of-the-art expertise to establish and guide public expenditure and saving policies.
- ***Integration.*** The more attuned resource uses are to the country's absorptive capacity (to avoid "Dutch Disease", or just plain transfer of corruption to difficult to track activities, or simple resource misallocations) the better the chance for a good and generally acceptable resource use.

In sum, control of money and trade flows that sustain conflicts, are complex, costly to monitor and to punish. In the end, the solutions have to be grounded on institutions that are accountable in the countries concerned, are compatible with the institutional capabilities, and are driven by commitments in countries resulting from incentives, rather than mere bureaucratic compulsion of donors or well meaning advocacy groups. Above all, no international tracking of resources or agreement is bound to succeed unless it is associated with a build-up of and adaptation to local capacity for public administration, budget monitoring and educated, well grounded policy debate that can provide the scrutiny required for accountable administrations.

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