How does political finance regulation influence control of corruption?

Improving good governance in Latin America

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1. Introduction 6

2. Literature Review 8

From Corruption to Control of Corruption 8

The Definition of Political Finance 11

The Link between Political Finance and Corruption 12

Political Finance and Corruption in Latin America 20

Public Expenditure and its Relation with Corruption 22

Judicial Independence: A Precondition for Control of Corruption? 23

3. Methodology 26

4. Results 29

The state of Political Finance Regulation in the world 29

Political Finance Regulation and Control of Corruption in Latin America 33

Panel regression model of Latin America 39

Variable description 40

Simple regression model 40

Multivariate regression model 41

How to improve control of corruption in Latin America? 44

5. Studies of Argentina, Chile and Mexico 46

Argentina 46

The Corruption Context 46

Argentina’s performance within Latin America 47

The strategy to improve control of corruption in Argentina 51

Judicial Independence 53

Public Investment Control 56

Political Finance Regulation 58

Chile 61

From colonialism to dictatorship 61

Transition to democracy 64

Party finance and corruption 67

Party finance regulation and the improvement of the control of corruption in Chile 68

The probity agenda promoted by Bachelet’s administration 73

Public funding contributions to political parties 73

Bans and limits on private income and limits on spending 74

Oversight and sanctions 75

Integral ecosystem of reforms 76

Mexico 77

Corruption in Mexico 78

Political Finance 81

Judicial Independence 83

Public Investment 84

Improving control of corruption 85

6. Conclusion 90

References 91

Figure I. Equilibrium Model (based on Mungiu-Pippidi's (2015)) 25

Figure II. Worldwide levels of PFR 2015 (Source: own calculations) 30

Figure III. PFR Index times series by regions, 1996-2015: America, Europa, Africa, Oceania, and Asia (Source: own calculations) 31

Figure IV. PFR and WB Control of Corruption Index time series, 1996-2015 (Source: own calculations) 32

Figure V. PFR Sub-Index level in 1996 and 2015 by region. BLPI: Bans and limits on private income, PF: Public funding, RS: Regulation on spending, OS: Oversight and sanctions (source: own calculations) 33

Figure VI. PFR Index in LA 2015 (Source: own calculations) 34

Figure VII. PFR Sub-index time series in 1996 and 2015 for Latin America. BLPI: Bans and limits on private income, PF: Public funding, RS: Regulation on spending, OS: Oversight and sanctions (Source: own calculations) 35

Figure VIII. PFR Index level in 2006 and 2015, Latin America (Source: own calculations) 36

Figure IX. Mean PFR Index and World Bank Control of Corruption time series in 2006-2015, Latin America (Source: own calculations) 37

Figure X. PFR Index and World Bank Control of Corruption change in 2006-2015, Latin America (Source: own calculations) 38

Figure XI. CoC, PFR and WEF Judicial Independence 2006 and 2015 (Source: own calculations) 39

Figure XII. Marginal Effects of PFR on CoC for different levels of JI (Source: own calculations) 43

Figure XIII. Marginal Effects of PI on CoC for different levels of JI (Source: own calculations) 43

Figure XIV. Predicted vs. Actual CoC. Equilibrium Models 2014 & 2006-2014. (Source: own calculations) 44

Figure XV. Argentina CoC, 2006-2015 (Source: own calculations) 48

Figure XVI. Argentina PFR Index, 2006-2015 (Source: own calculations) 49

Figure XVII. Argentina PFR Subcategories (Source: own calculations) 49

Figure XVIII. Argentina Judicial Independence, 2006-2015 50

Figure XIX. Argentina Public Investment, 2006-2015 51

Figure XX. Equilibrium Model for Argentina and Achievers 52

Figure XXI. Argentina PFR sub-indexes and Achievers 59

Figure XXII. Chile CoC Indicator, 2006-2015 69

Figure XXIII. Chile PFR Sub-indexes and Latin American Mean 70

Figure XXIV. Chile CoC Indicator, 2006-2015 70

Figure XXV. Chile Judicial Independence, 2006-2015 71

Figure XXVI. Chile Public Investment, 2006-2015 71

Figure XXVII. Chile Equilibrium Model 72

Figure XXVIII. Mexico CoC, 2006-2015 79

Figure XXIX. Mexico PFR Index, 1996-2015 82

Figure XXX. Mexico Judicial Independence, 2006-2015 83

Figure XXXI. Mexico Public Investment, 2006-2015 85

Figure XXXII. Mexico Equilibrium Model 86

# 1. Executive Summary

This thesis tackles the question of how political finance regulation affects control of corruption in Latin America from a quantitative angle and, afterwards, it examines how to improve good governance in Argentina, Chile and Mexico.

We present a Political Finance Regulation Index with panel data from 180 countries over 20 years (1996-2015). This index was developed using the IDEA Political Finance Database, and once created, was applied to assess the relationship between political finance regulation and control of corruption.

In order to do this, we use the equilibrium model of control of corruption developed by Mungiu-Pippidi (2015). We also included judicial independence and public investment, considered as a constraint and an opportunity to corrupt, respectively. Lastly, we used control variables for level of development.

Results show that, in Latin America, increases in political finance regulation are related with a deterioration of control of corruption. This relationship is statistically significant in the panel estimations. Inversely, the negative relationship between regulation and control of corruption becomes positive in countries with high levels of judicial independence. In a similar way, increases in opportunities to corrupt, represented by levels of public investment, have a significant and negative effect in control of corruption.

The second part of the thesis presents the qualitative analysis of Argentina, Chile and Mexico. Using the quantitative framework provided by the aforementioned results, each case takes into account the local context in order to develop measures to improve control of corruption.

Argentina and Mexico should focus on enhancing judicial independence and reducing the margin of discretion of public investment. Instead, Chile’s study emphasises the need of sophisticating its political finance regulation, specifically in the realm of oversight bodies and sanctions.

# 2. Introduction

Honest political parties play a vital role in strengthening democracies, functioning as a bridge between citizens and their governments. However, corrupt parties can seriously damage a democracy by undermining public trust, increasing voters’ disillusionment and even leading to authoritarian regimes. (Blechinger, 2002) This is why the corruption of political parties is one of the most critical threats to democracies, especially for young ones.

Today, a relative majority of countries are organized around regular elections and people are involved in public affairs more than ever. Yet, corruption is expanding among new democracies instead of decreasing. (Mungiu-Pippidi, 2015)

Latin America is a perfect example of this situation. Even though democracies in the region experienced an important consolidation in the last decades, corruption scandals related to the influence of money in politics seem to have increased. Issues such as the illicit funding of candidates and parties by criminal organizations, as well as the misuse of public resources by parties in government, have been gaining traction in the public agenda.

This thesis will focus on understanding how political finance regulations have influenced control of corruption. In other words, it will seek to identify if political finance regulation has been an effective constraint of corruption in Latin America. By developing a Political Finance Regulation (PFR) Index*,* this study aims to identify how different levels and types of party finance regulation interact with control of corruption in the region.

Furthermore, as literature states that political corruption is a multidimensional problem and we present corruption with an equilibrium model, we use public investment as a measure of opportunities for corruption. Using data from capital expenditures from Latin American countries, we will consider how control of corruption interacts with both political finance regulation and discretionary public investment in the region. Public investment and political finance regulation will be analysed in conjunction with judicial independence, another fundamental variable for control of corruption.

Taking into account the results quantitative analysis of the first part of this thesis, the second part is comprised of a deeper analysis of changes in control of corruption, political finance regulation, judicial independence and public investment in three countries: Argentina, Chile and Mexico, as well as the exploration of measures to improve control of corruption in the three countries.

# 3. Literature Review

## From Corruption to Control of Corruption

Corruption is not harmless and has indisputable negative consequences for societies. It leads to massive brain drain and produces disincentives for hard work and integrity. It also affects fair competition and gender equality, in addition to distorting public spending and equal access to public jobs. (Mungiu-Pippidi, 2015)

Notwithstanding the importance of the concept, the definition of corruption represents a challenge. According to Mungiu-Pippidi (2015, p. 3), there seems to be an agreement around the idea that “corruption involves some undue private profit (for someone) due to the abuse of an entrusted public authority”.

Indeed, since 2005, the United Nations Convention Against Corruption (UNCAC) provided a frame for the idea of corruption. Even though this international instrument does not offer a clear definition of corruption, the Convention states in its first article that one of its purposes is “[t]o promote integrity, accountability and proper management of public affairs and public property.” (UNCAC, Art. 1.c)

Moreover, the first preventive measure of the Convention states that: “Each State Party shall, in accordance with the fundamental principles of its legal system, develop and implement or maintain effective, coordinated anti-corruption policies that promote the participation of society and reflect the principles of the rule of law, proper management of public affairs and public property, integrity, transparency and accountability.” (UNCAC, Art. 5.1)

According to Mungiu-Pippidi (2015), the classic definition of corruption made by Nye in 1967, as a “behaviour which deviates from the formal duties of a public role because of private-regarding (personal, close family, private clique) pecuniary or status gains; or violates rules against the exercise of certain types of private-regarding influence)” (p. 11) highlights the connection between the public and the private spheres. However, this definition does not consider situations where “laws and policies themselves are corrupt and seek to create legal privileges for those connected with the source of authority granting the privilege”. (p. 11)

Furthermore, there are three main characteristics of the idea of corruption. First, fraudulent behaviours between private actors are normally defined as fraud, staying out the realm of corruption. Second, the notion of abuse of public authority is assumed to avoid cases where private parties can damage public interest or trust. Third, corruption exceeds the notion of deviation from the norm, since the idea of public interest of this definition implies a high level of relativism and has mutated over the years and cultures. (Mungiu-Pippidi, 2015)

Based on these characteristics, it is noted that agreeing on a unique and universal definition of corruption is complicated, since it is a phenomenon affected by many disciplines. Moreover, in societies without ethical universalism, which is the equal treatment of all members of society by government when implementing laws and policies, the different kinds of corruption can be immeasurable due to the prevalence of groups taking advantage of public resources. (Mungiu-Pippidi, 2015)

In a theoretical-practical approach, the author turns the focus from the idea of corruption to control of corruption, defined as “a given society´s capacity to constrain the use of public authority to generate private rents detrimental to overall social welfare”. (Mungiu Pippidi, 2015, p. 18)

Then, the key question is how a certain society can constrain the missuses of public resources by an individual or a group in their own and private benefit, and guarantee that the state serves the social wellbeing. Thus, Mungiu-Pippidi (2015) addresses the issue of corruption, not from an individual perspective, but from a societal one. The difference is that while the former would be aimed at the undue profits made by individuals due to the abuse of public authority, the latter sees corruption “as an intrinsic part of certain governance context, a social allocation mode”. (p. 19)

This approach exceeds the notion of corruption as a simple aggregation of individual corrupt acts. Conversely, it is focused on how the work of institutions and the rules of the game determine the allocation of public resources. Mungiu-Pippidi (2015) highlights those countries with the highest levels of control of corruption that managed to institutionalize open and non-discriminative access to their institutions.

Indeed, human agency is indispensable to make progress in governance. It means to move from particularistic societies where states and their institutions are used as instruments for particular private profits, to more ethical universalistic societies, where institutions seek out general welfare. (Mungiu-Pippidi, 2015)

However, when it comes to the question about the right kind of human agency, the answer tends to be contested. Implementing anticorruption laws, liberalizing trade, increasing accountability, are just some of the options normally analysed.

Actually, the answer will depend on the type of control of corruption model that is applied. Mungiu-Pippidi (2015) differentiates between three main models of control of corruption. The first is based on structural factors: traditional factors, like trust, natural resources, and/or geographical and living conditions, as well as modernization conditions like literacy rates, urbanization and life expectancy. The second model, aimed at the promotion of anti-corruption legislation and the adoption of anticorruption tools for domestic implementation such as civil service merit-based recruitment, administrative reforms and independent control agencies, which can include freedom of information legislation, anticorruption agencies and ombudspersons. Finally, a third model of control of corruption is identified: the equilibrium model.

Based on the understanding of corruption as equilibrium between costs and benefits pioneered by Klitgaard (1988) and Huther and Shah (2000), Mungiu-Pippidi (2015) states that “the ideal model to explain control of corruption should be an equilibrium model without a principal-agent perspective” (p. 116), in order to overcome those situations where principals are the ones to be enforced.

The equilibrium model understands control of corruption as the balance between opportunities or resources to corrupt and deterrents or constraints imposed by society as a whole. Indeed, this approach is aimed at the collective capacity to enforce good governance, which means the capacity of a society to reduce particularistic situations and increase ethical universalism among their institutions. (Mungiu-Pippidi, 2015)

Then, the equilibrium model formula of control of corruption developed by Mungiu-Pippidi (2015) is:

“*Control of corruption= Constraints (Legal + Normative) – Opportunities (Power Discretion + Material Resources)”*. (p. 117)

Based on this model, we will seek to address a central issue of particularistic societies and corruption. When ethical universalism is not the norm, private entities usually offer favours to political parties and political candidates, which are expected to be reciprocated once that party/person is in charge of public resources. (Mungiu-Pippidi, 2015, p. 16)

Scholars have analysed a significant dimension of control of corruption related to this problem: political finance regulation. However, it seems that there is not an agreement regarding the impact of this approach on the decrease of corruption. While some specialists and international organisations encourage states to adopt a broader regulatory framework, some research argues that those regulations are limited, since they cannot prevent the influence of money.

The discussion regarding political finance regulation can be tackled from different theoretical angles and regional perspectives. This thesis will focus on understanding how political finance regulations have influenced control of corruption.

## The Definition of Political Finance

Even though political finance usually refers to money flowing in the political process, this thesis will use the definition of political finance as “the (legal and illegal) financing of ongoing political party activities and electoral campaigns (in particular, campaigns by candidates and political parties, but also by third parties).” (IDEA, 2014, p. 2)

Within this context, internal political parties’ behaviour, availability of state resources and private founders´ activities, are some of the elements that comprise the realm of political finance. Regulation of at least some of these matters has been adopted by most states in the last decades. Political finance regulation, then, looks to prevent the missuses of money in politics, as well as to provide the necessary framework to enforce some mandates and sanction those who violates them. (IDEA, 2014, p. 2)

Indeed, political finance regulation is seen as a key variable of more transparent and legitimate democracies. The need to regulate money in politics is usually considered as an indispensable step to diminish the influence of big donors over candidates and parties. The Global Commission on Elections, Democracy and Security, for instance, stated that "the failure to regulate political finance threatens to hollow out democracy and rob it of its unique strengths". (IDEA, 2014, p. IV)

The lack of political finance regulation has been identified as an opportunity for organized crime to influence politics and as a cause of negative economic development. In his foreword for IDEA’s Handbook on Political Finance, former UN Secretary General Kofi Annan called for a better control of political finance, meaning that governments should regulate donations and expenditures effectively, increase transparency of donations, require disclosure of financial sources, adopt sanctions for non-compliance and legislate over effective monitoring and enforcement mechanisms. (IDEA, 2014)

However, there also seems to be a general agreement on the conviction that more regulation does not necessarily mean more transparency or a better balance of power between those with money and citizens in general. Indeed, IDEA concludes that in some situations, depending on the social-political context and/or the aims of the regulation, a high level of regulation may be not desirable. (IDEA, 2014) All in all, this shows an open discussion about the capacity of political finance regulation to influence control of corruption within states.

## The Link between Political Finance and Corruption

The scholar debate about political finance can be traced back decades. The issue was discussed in the 1940s, when specialists could not reach an agreement on how to address limitations to contributions and expenditures of candidates and parties over electoral campaigns in the US. (Overacker, 1941)

To tackle the problem of the power of the purse for the presidential campaign in 1940, the US Congress decided to increase party finance regulations. There were already some limitations to the amount of contributions and total expenditures of candidates and parties since 1911. Nevertheless, through the *Hatch Act II*, Congress also limited the amount of money that an individual could contribute to a national committee and the level of expenditures permitted to these agencies. (Overacker, 1941)

The results of the new legal framework were poor. Its subjects adopted deliberate strategies to circumvent the law without violating its letter; both major US parties decentralized the collection and distribution of funds. Indeed, Overacker (1941) concluded that the endeavour to regulate camping funds was "ambiguous, unworkable, and conducive to unhealthy political practices" (p.724). Based on the evidence, she disputed the advice from other specialists who were in favour of more party finance regulation and subsequently supported the idea of increasing the publicity of party funding instead of passing new legal prohibitions. (Overacker, 1941)

At the beginning of the 1960s, Heidenheimer (1963) went a step further in comparing political finance processes. After recognizing that a high quality comparative study on the topic would require greater amounts of data and more unified concepts, he looked to develop a comparative evaluation of data and information. At that time, he observed two polar models in terms of party finance processes. The first built around mass parties and based on membership fees. The second concerning cadre party, who’s financing relied upon the "whim of a few hidden large-scale contributors and ´interests´". (p.791)

He stated that in the 1960s, most Western parties were turning into mass parties and had started to diversify their sources of financial support, affecting financing patterns. Indeed, throughout his work, Heidenheimer compared party finance processes to identify the existence of a historical evolution. He touched upon the issue of regulation within this realm, but only accessorily. He observed that only a small amount of countries tried to prohibit corporate political donations like the US. Indeed, Heidenheimer concluded that there were tax laws on different countries that had considerable influence on the matter. However, he admitted that the application of regulations deserved much more detailed studies on a comparative level. (Heidenheimer, 1963)

During the 1960s some scholars observed a growing tendency among Western countries regarding party finance. They noted that in a number of countries, political parties abandoned their traditional sources of income from the 19th and 20th centuries and changed towards a public subsidized system. Concerned about this phenomenon, they analysed the importance and effectiveness of political finance over electoral results, mainly focusing on the relationship between economic and political powers. Consequently, they went into the realm of party finance regulation. (Heidenheimer, 1970)

Heidenheimer (1970) also studied the different practices and experiences related to the rising spending and controlling of political funds. The scholar analysed different regulations related to campaign expenditures, like spending limits and expenditure reporting requirements.

Moreover, he underlined the political discussion about Parties Law in Germany, specifically, the critique of the proposal of prohibiting corporate donations to parties and candidates on the basis of the American experience, which proved such these rules could be easily circumvented. Nevertheless, Heidenheimer observed a high correlation between the enforcement level of expenditures disclosure and the degree of public access to that information. (Heidenheimer, 1970)

In the 21st century, still interested in the structure of modern mass parties, Heidenheimer (2007) turned his focus over to the relationship between party finance and political corruption. He argued that for many decades there was a lack of studies on the “linkages between party finance processes and explicitly recognized patterns of political corruption” (p.764), because of the different national ideas about the meaning of political corruption.

After linking a party and campaign expenditure index from the early 1960s and Transparency International’s (TI) Corruption Perceptions Index (CPI) from 1995 to 1997, Heidenheimer found a pretty consistent relationship between both rankings. His study covered nine different countries and, taking into account the 30 years gap between both indexes, he concluded that higher campaign expenditure increased corruption. (Heidenheimer, 2007)

According to Mauro (1998a), government regulations are a key element for corruption. Based on economic research, he states that corruption takes place where rents exist, and since public regulations usually provide discretion to public officials, government restrictions tend to result in rent-seeking behaviour, like in the case of import quotas.

He mentions different situations where government restrictions generate excessive profits increasing corruption likability. Examples are trade constraints, favourite industrial policies, price controls, multiple exchange rate policies, foreign exchange allocation schemes and provision of credit under governmental control. Also, he underlines rent-seeking contexts in the absence of governmental intervention, like the case of natural resources, which generate extraordinary profits, and therefore, increase the incentives to bribe those who allocate extraction rights. (Mauro, 1998a)

Despite the depth of his analysis, Mauro does not mention party finance regulation as a cause of corruption. The fact that this kind of rules seek to restrict politicians instead of empower them may be a central difference with regulations that enable rent-seeking scenarios. Party finance regulation is not mentioned as a tool to fight corruption, at least, in a direct way. Among the different options analysed by the author to reduce corruption, the need of transparency is recurrent; budget transparency, as well as, government expenditures transparency are hopeful alternatives. (Mauro, 1998b) So, depending on how party finance regulation is defined, whether as a rent-seeking generator or a transparency tool, the object of this study can be considered as a corruption opportunity or constraint.

According to Wilcox (2001), there seems to be a general agreement regarding the positive effects of disclosure within the campaign finance system in the US. Indeed, the obligation that candidates, political parties and interest groups reveal their funding sources and how they expend money tends to be accepted as a way to reduce corruption.

Disclosure regulation has its advantages such as the improvement of corruption control and civic accountability. Inversely, overexposure of private donors, small parties’ under-funding and rent seeking are possible disadvantages. (Wilcox, 2001)

After studying the US experience, Wilcox concludes that a good disclosure system would need to define campaign activity broadly in order to avoid circumventions of the rules. It also has to provide the policymaking authority with the ability to adapt to different practices. However, it is important to balance the costs and benefits of the disclosure system, considering the social and political context. (Wilcox 2001, p. 38)

Based on different study cases, Blechinger (2002) underlines the importance of party finance regulation, mainly aimed at campaign finance, as well as intra- and external party anti-corruption laws. Nevertheless, he also notes that for it to be effective it needs to be part of a broader strategy that includes party competition, more transparency, the monitoring of free media, an active civil society and up-to-date citizenry.

On the subject of parties, Hopkin (2004) argues that following the decline in party membership, partially caused by scandals that feed the perception of politicians as corrupt, there has been changes in patterns of party finance, specifically a shift from the mass party model of funding towards elite party and cartel party models. In this sense, party finance is a collective action problem in which rational self-interested group members will free ride and refuse to contribute to the party. He further identifies four post-mass party financial strategies: the clientelistic mass party, the externally financed elite party, the self-financed elite party and the cartel party. He concludes that the mass party model remains closest to the democratic ideal, while the state financed model is a pragmatic response to the decline in party membership.

The level of regulation of the political process may also depend on the democratic context. After analysing party laws of 39 countries, Karvonen (2007) ascertains that party laws regulate political parties differently depending on the democratic status of its countries. In non-democratic states, the establishment tends to use these laws to restrict the freedom of their opponents, while in new democratic states the law counteracts lingering anti-democratic tendencies. Finally, in stable democracies, the law is seen as a prerequisite for regulation of subsidies and political finance. Furthermore, these laws tend to cement the existing party structures.

According to Scarrow (2004), political finance is one of the most problematic regulatory areas of democracies, because it is connected to the aim of guaranteeing a certain minimum level of political equality in a context where wealth is unequally distributed. After analysing party finance reforms in Germany and England, Scarrow noted that scandals had weak consequences in regulatory results, unless one party advances the cause. Also, he showed how parties endorsing reform, did not automatically mean they would adopt it.

Conversely, the deepest effects in party finance reforms were reached thanks to the intervention of non-party regulatory bodies, such as independent commissions appointed by the government, as well as courts of justice, among others. Even in cases of parties willing to compete over party regulation issues, the adoption of self-denying rules may be more successful with external forces suggesting and/or imposing reforms. (Scarrow, 2004)

Based on evidence from 20 years, Scarrow (2007) affirms that campaign spending matters. Even in scenarios ruled by party loyalty and spending centralized in national parties, individual candidates’ spending can improve electoral chances. Moreover, the spending by challengers tends to be more effective than officeholder’s spending. Therefore, attempts to limit the impact of money over politics through regulations can work as a protection to the ruler party or candidate and as a limitation to the challengers.

Rules aimed at increasing transparency of the relation between donors and recipients, like an increase of disclosure or specific prohibitions to donations; tend to have a dual effect. They decrease people´s distrust on candidates and parties, since they appear less responsive to donors’ preferences, but can have the counter-effect of scandalizing former accepted behaviours. (Scarrow, 2007)

According to research from the US, introducing public funding does not guarantee more citizens´ trust in their parties. However, Scarrow (2007) notes a lack of investigations on the issue. He concludes that the comparative studies which address the assumption that politicians in need of funding may pay disproportionate attention to their funders´ will are unlikely to provide a universal solution to the problem.

Pierre et al. (2000) study the consequences of the introduction of public funding to party dynamics. They take the arguments in favour and against the introduction of subsidies to political parties and examine if they are supported by empirical data. On the side of advocacy for state subsidies, they identify the need to maintain parties for their importance to a democratic government, the fact that they can serve as a platform for citizens’ political participation and the rising costs of running a party in a modern democracy. The arguments for removing them are the supposed co-optation of the state by the parties, that they petrify the party system by not allowing entrance to new parties and because they eliminate parties’ interest in sustaining or increasing their membership.

The study finds that petrification of the party system has not taken place in systems with extensive support for parties and that the decline in membership of parties could not be attributable to the introduction of subsidies. Furthermore, it confirms that subsidies don’t have a significant impact on the structure of the party system and that they might provide funds to develop the creation of new parties. (Pierre et al., 2000)

For Pinto-Duschinsky (2002) state funding has not cured the problem of corrupt political funding because “some of the most serious scandals have occurred in countries with generous public subsidies”. (p.78) He states that the failure might be related with the fact that heads of government have a secret slush to use as they see fit; legislatures have similar funds for development projects in their constituencies; public officials are required to donate part of their salaries to parties and the use of state resources for electioneering purposes could be used as an indirect public subsidy.

In the same sense, laws are not respected because of a lack of enforcement and political will. Related to this, he underscores the dangers of assuming that the problems of political financing are amenable to legislative remedies, stressing the need for a focus on enforcement. (Pinto-Duschinsky, 2002)

On the same note, van Biezen and Kopecky (2007) propose an analytical framework that distinguishes between three different dimensions of the party–state linkage: 1) the dependence of parties on the state, 2) the management of parties by the state and 3) the control of the state by parties. They argue that despite regional variations, the widespread availability of public subsidies demonstrates that subventions have become a pervasive phenomenon in contemporary democracies and that the regulation of party activity indicates that parties are more extensively managed by the state. Also, they determine that there is a pervasiveness of party rent seeking, which suggest that parties are in some degree in control of the state and state resources.

Van Biezen (2004) notes that the concern of the impact of money in political finance has acquired an increasing importance due to perceptions of dishonesty of party leaders. The author explores the variation in existing regulatory frameworks and provides a typology of financing regimes, which focuses on the control and transparency of income and expenditures, as well as the availability of direct and indirect public funding. The study uses the Political Finance Database of IDEA to examine structural and institutional explanations for patterns of party regulation. The research found no correlation between the pervasiveness of corruption, the level of economic development or the maturity of the democracy.

Using the CPI of Transparency International, Van Biezen (2004) found no clear relationship between the existence of disclosure rules, the availability of public funding and the level of corruption. Furthermore, the study concluded that countries with higher levels of corruption may be more likely to establish legal norms to control political donations and expenditures, but are not necessarily more inclined to introduce transparency legislation or to concede a greater role to state funding. Contradicting similar research, it suggests that political finance regulations might not be a product of an increase in political scandals.

Casal Bértoa et al. (2014) analysed if public funding and political finance regulations are related to the perception of party corruption. Like most of the scholars who tackle this topic, the authors note a lack of research concerning the influence of political finance regulation on corruption.

Using a dataset developed at Leiden University, with information of political finance aspects in Europe and Latin America, these scholars employ a quantitative approach to verify the assumption that political finance regulation has a positive effect on party corruption trough a comparison of 28 European and 9 Latin American countries. Based on their data, the scholars conclude that more political finance regulation does not mean a lower perception of party corruption. (Casal Bértoa et al., 2014)

The scholars note that political finance regulation does not help to drop the levels of perceived corruption among political parties. According to their study, neither restrictive legal frameworks where the state is the main financial contributor to parties, nor more independent controls, nor higher penalties over illegal funding activities, are correlated to lower levels of party corruption perceptions. Despite the limitations of the study, they conclude the state should not be the only contributor of funding to political parties. (Casal Bértoa et al., 2014)

## Political Finance and Corruption in Latin America

In Latin America, scholars note a gap between the high density and scope of political finance regulations and the role of money in politics. The main underlying problem in the region is not the lack of regulation, but the inability to enforce rules. Some of the issues shared by countries in the subcontinent that contribute to this problem are low levels of transparency of funding, the inexistence of regional standards for political finance, the loopholes or rigidity of regulation, the infiltration of illicit financing and the impossibility to implement the ruling norms effectively due to the absence of strong monitoring and enforcement agencies. (IDEA, 2014)

Political finance issues became central in Latin America after dictatorships came to an end in the late 70´s and democracy emerged as the only legitimate way to reach and keep institutional power. Actually, Casas-Zamora (2016) remarks that today, after a generation of democratic relations, the region is in a much better position to address some key issues to strengthen democracy, like transparency of political finance.

Still, in recent years, the region has faced many political corruption scandals. For instance, the *Petrolão* or *Lava Jato* in Brazil; the *Penta and Soquimich* affairs in Chile; the social security scandal in Honduras (Casas-Zamora, 2016); the *Odebrecht* case in many countries of the region and the *Panama Papers*.

In parallel, and as an answer to these scandals, Latin America has been making regulatory efforts to improve control over money in politics (Casas- Zamora and Zovatto, 2016). The focus has been set on private contributions and corporate donations bans, television advertising restrictions during political campaigns and stronger penalties for political finance violations. Nevertheless, both old and new regulatory frameworks are weakened by grave implementation problems. (Casas-Zamora, 2016)

Chile, El Salvador, Guatemala, Paraguay and Peru passed new political finance regulations between 2012 and 2016. Yet, “these changes have left the crucial question of the enforcement of political finance controls largely unaddressed”. (Casas-Zamora, 2016, p.7)

In the same sense, Posada-Carbó (2008) specifies that democracy in the region is seen to have failed to provide economic and social stability and that the surge of state funding of parties in the region answers to corruption scandals rather than to an interest in a procedural democracy.

The concept of clientelism is also closely related with the study of party finance and corruption in Latin American countries. Clientelism is a “relationship based on political subordination in exchange for material rewards. In systems where this is the norm, the poor are obliged to sacrifice their political rights in exchange of access to redistributive programs.” (Fox 1994, p.153)

Fox (1994) analyses the case of Mexico, in which a trend towards electoral competition did not result in a decrease of clientelistic practices of the government. The author concludes that there needs to be respect for associational autonomy for citizens to organize and not to fall in an asymmetric power relation. He argues that antipoverty programs could be used to perpetuate clientelism.

The lack of effective control mechanisms, social inequality and clientelism are related to the idea that political finance regulation is a second-generation political reform, which needs a number of economic, social and institutional prerequisites in order to succeed. (Casas-Zamora, 2016)

Those interested in improving political finance issues should focus on enhancing political finance regulation, monitoring and enforcement; paying special attention to local level political finance corruption; and, facilitating and simplifying the access to political finance information. Also, promoting a comprehensive regulatory approach that integrates campaign finance, conflicts of interest and lobbying activities rules. (Casas-Zamora, 2016)

## Public Expenditure and its Relation with Corruption

Complementarily, and based on the equilibrium model developed by Mungiu-Pippidi, this study will also focus on a well-known opportunity to corrupt: public investment. According to Tanzi and Davoodi (1997), higher corruption is related to higher public expenditures in big infrastructure projects in developing countries. The main reason behind this idea is that in societies with low control of corruption, politicians may have incentives to increase public capital spending at the expense of lower expenditures on operations and maintenance (public current expenditures) to get larger illegal commissions from the beneficiary private companies.

The influence of corruption over public spending and its effects on growth have been studied for the last years with noteworthy results. For instance, it was revealed that corruption reduces government expenditure on education, since it is an unattractive field for rent-seekers. The assumption is that goods and services that do not require high-technology inputs to be provided by oligopolistic suppliers are less suitable to generate rent-seeking situations. (Mauro, 1998a)

Going deeper into this subject, it was also discovered that corruption could negatively affect growth by increasing public investment and at the same time reduce its productivity. Indeed, the golden rule of promoting public sector investment spending to increase growth has been disputed, especially in countries where corruption is a problem. When control of corruption is weak, corrupt politicians have incentives to increase capital expenditures to produce big projects that will demand higher capital budgets and probably will not generate positive results in terms of growth. (Tanzi and Davoodi, 1997)

More recently, it was reaffirmed that corruption emerges as a distortion of the public expenses structure. Indeed, corruption was observed as public expenditures on fuel and energy, culture and public services increased. All of the aforementioned are spending that guarantees more discretion and therefore, more opportunities for corruption. Distortions in public spending function at the expense of social spending like education, health, and social protection, which usually involve more standardization and restrictions. (Delavallade, 2006)

## Judicial Independence: A Precondition for Control of Corruption?

Judicial independence is considered a key element of national institutional systems to prevent abuses of power. Despite finding its origins in the British courts, the establishment of judicial independence, as we know it today, has been linked to the institutional consolidation of the US. According to Kaufman (1980), American colonists tried to avoid the courts´ subjugation to the British Crown and Parliament by creating an institution independent from the government, which could solve disputes impartially. In parallel to the creation of a fundamental law, the founding fathers also created a federal judiciary to prevent law violations through abuses of power by the government or Congress.

Courts and judges are still considered by some scholars the base of the social contract and democratic governments, as well as the last hope to preserve the Republic from the dark side of human nature. (Carrington, 1998) Essentially, the impossibility of politicians to block judges´ investigations because of judicial independence is still considered a key factor of the Italian “Clean Hands” process. (Maor, 2004)

However, judicial independence is a complex concept. For instance, Fiss (1993) underlines three main perspectives to analyse it. He states that judges should be independent not only from the parties of the litigation but also from hierarchical relations within the judiciary, as well as political institutions and the public in general. Conversely, Rose-Ackerman (2007) highlights that judicial independence does not necessarily guarantee judicial transparency. Judges can be independent and corrupt at the same time, since independence can enable them to follow their own interests and benefit from those who make payoffs.

Nevertheless, the specialized literature tends to agree on common characteristics that define the independence of a judiciary. Some of the most prevalent include: high remunerations; merit-based selection processes; long-terms appointments (Cordis, 2009); invulnerability to bribery or intimidations (Carrington, 1998), and judicial integrity and predictability. (Buscaglia, 2003)

Beyond its definition, opinions regarding the relationship between judicial independence and political corruption tend to be unanimous: with higher judicial independence, political corruption decreases. Rose-Ackerman (2007) observes that judicial independence has a positive relationship with less corruption and more political freedom. Della Porta et. al. (2003) state that judicial independence is important for political and economic freedom. Cordis (2009) concludes that judicial independence, as well as constitutional rigidity, is a significant predictor of political corruption. This means that countries where judges have a high level of independence, government officials tend to be less corruptible.

This is confirmed by an evidence-based study run by Buscaglia (2003), who concludes that judicial independence and fairness are the most important causes of low and high level corruption in the public sector. Moreover, he underlines the relevance of independent judges to prosecute organized crime, even where politics have been captured by it.

Finally, Mungiu-Pippidi (2015) confirms the existence of a strong correlation between control of corruption and judicial autonomy, highlighting that this variable is a highly significant and robust factor of control of corruption. Furthermore, she considers judicial independence a key constraint for corruption.

# 3. Methodology

In this thesis, our aim is to study the relation between control of corruption (the dependent variable) and political finance regulation (the independent variable). Following a multivariate model and based on the equilibrium model by Mungiu-Pippidi (2015) we seek to analyse other independent variables, public investment and judicial independence, considered an opportunity and a constraint of control of corruption. Figure I shows a graphical representation of this model.

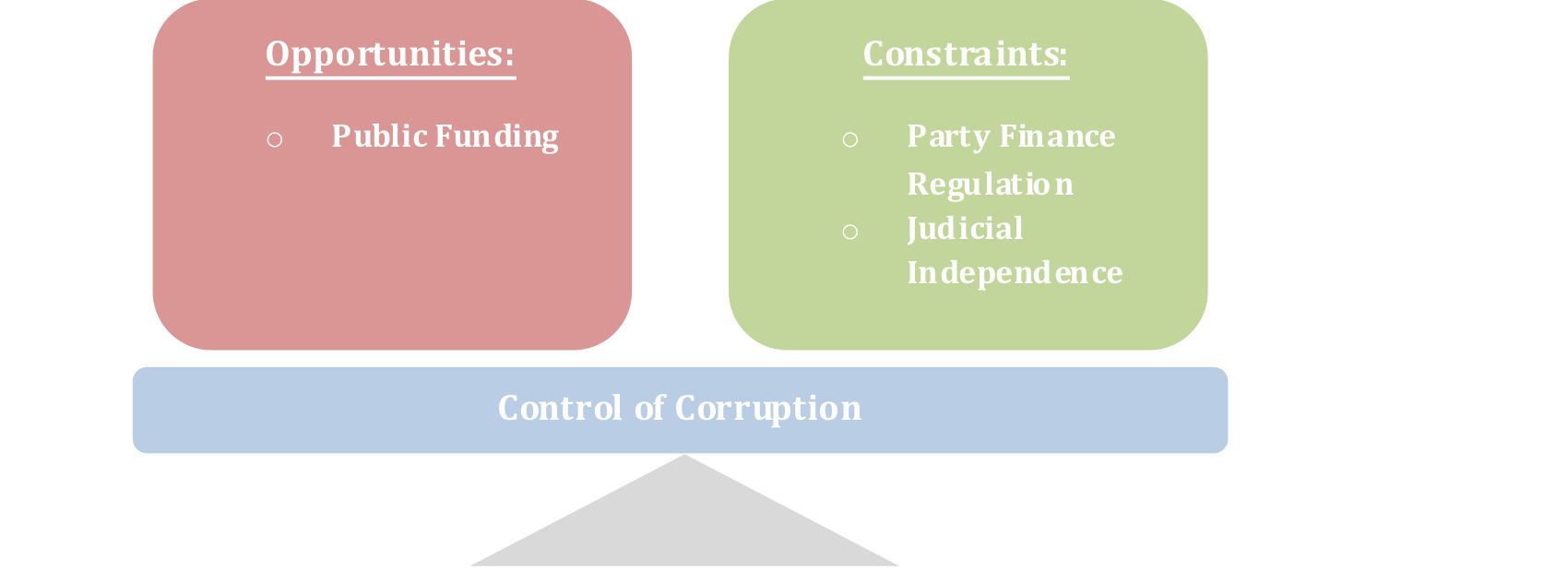


Figure I. Equilibrium Model (based on Mungiu-Pippidi's (2015))

To measure the variations of the dependent variable control of corruption between countries and across time, we decided to use the index developed by the World Bank for their World Governance Indicators (WGI). The Control of Corruption (CoC) Indicator of the WGI measures “the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as capture of the state by elites and private interests. (Kaufmann et al., 2006, p. 4). The original indicator has a scale of -2.5-2.5 but it was rescaled to 0-10 to avoid negative numbers. With the new scale, 0 is a country with no control of corruption and 10 is a country with the highest score. The WGI has information about more than 200 countries and goes as far back as 1996.

In the same sense, there was a need for reliable data to analyse one of the independent variables: political finance regulation. We used the IDEA Political Finance Database to develop a Political Finance Regulation (PFR) Index. IDEA includes more than 180 countries and excludes cases where no elections have been held in the previous 30 years, as well as where political parties are not allowed to exist or register candidates.

IDEA’s Political Finance dataset is comprised of 43 questions, which reflect each country's legislation in the matter. The database has a high response rate, with around 7000 answers from more than 1000 sources. In addition, the dataset provides the exact source and year when the law was enacted on its appendix.

The responses of the IDEA questionnaire are useful to build a cross-sectional index, but the supplementary information of the legal sources and documents provides an opportunity to trace changes in the legislation through the years. With both sources of information, we built a panel dataset that spans from 1996 to 2015.

Specifically, every YES response in the IDEA questionnaire was coded with a 1 and every NO with a value of 0. Additionally, a value of 0 was coded for every previous year of the date that the law in the matter was enacted, and a value of 1 since that year onwards.

To build the PFR Index, we considered only YES-NO questions. Because of this, only 31 questions of the questionnaire where taken into account. In the case of categorical questions (with different options for a YES response), the detail of the response was ignored and only filled with a YES. Qualitative questions in the survey were not taken into account. Moreover, the answers were divided in the four categories of the database:

* *Bans and limits on private income (BLPI)*, questions 1 to 18.
* *Public funding (PF)*, questions 19 to 28.
* *Regulation of spending (RS)*, questions 29 to 34.
* *Reporting oversight and sanctions (OS)*, questions 35 to 43.

Following IDEA’s criteria, the few cases with sources of judicial decisions were also taken into account. Additionally, if a question had legislative sources from different years, the oldest date is considered as the year the law was enacted. This has the objective of avoiding favouring specific legislation and to provide methodological simplicity. In this respect, our indicator was more sensible to older legislation in questions with multiple sources. Moreover, in questions with only one source that was updated on a subsequent year, the index takes into account only the most recent update. Methodologically, this seeks to provide certainty about the moment when the requirements of that particular question count as an affirmative answer. This makes the questions with updated sources more sensible to the most recent regulation.

The PFR Index is useful for a descriptive analysis of the world’s legislative efforts of party finance. Also, it provides panel data to do an inferential statistical analysis of our region of interest, Latin America, with a model that includes other relevant variables like life expectancy or percentage of rural population.

For our other independent variable and based on the equilibrium model, we used data from capital expenditures of Latin American countries available from the Economic Commission for Latin America and the Caribbean (ECLAC), a United Nations regional commission to encourage economic cooperation. This information is provided as a percentage of GDP of the 20 countries of Latin America. The information as a percentage does not capture the increase in real terms of these kinds of expenditures, given the economic growth of the region during this time. Taking this into account, we multiplied it with information about GDP in US dollars provided by the World Bank. The ECLAC provides information on capital expenditure as far back as 2003. Nevertheless, we only used data from 2006 to 2015 given the limitation on another relevant variable for our model, judicial independence.

In this study, we also work with a variable developed by the World Economic Forum (WEF), which measures the independence of the judiciary from influences of the government, individuals, or companies. (WEF, 2016) This indicator has a scale of 0 to 7, with countries with lower scores having less judicial independence than countries with higher scores. This data extends between 2006 and 2015, so a panel data analysis including this variable would only account for ten yearly observations for each country. It is worth mentioning that the WEF Judicial Independence Index excludes Cuba and includes only five years of observations for Haiti, so our analysis for Latin America excludes both countries and only takes into account the remaining members of the ECLAC. Including all of these variables results in an analysis of 18 countries across ten years, or in other words, 180 observations.

The gathered information allows performing a panel data analysis, taking into account differences between countries as well as changes over time. We chose to study Latin America because most of its countries have enacted political finance regulation in the recent years but are still fighting to increase its levels of control of corruption. Also, all of the countries in the region are constitutional democracies and have a common colonial past. Furthermore, after our statistical analysis we will go into deeper analysis with three cases: Argentina, Chile and Mexico. Chile is regarded as one of the main achievers of the region, while Argentina and Mexico struggle to increase their control of corruption. It is also worth mentioning that the three countries have different contexts and are three of the most influential countries in the region regarding their economy, population and size.

# 4. Results

This section includes the results of a descriptive and inferential statistical analysis of the variables previously mentioned. All of the figures are based on our calculations and using the aforementioned databases. The section is divided as follows:

1. A worldwide analysis of the Political Finance Regulation through the Index created for this study. This section includes most the countries in the IDEA Political Finance Database.
2. A regional analysis of the Political Finance Regulation focused on Latin America.
3. Results of the panel data regression analysis with a specific focus on Latin America.

## A) The state of Political Finance Regulation in the world

The results show an overall incidence of Political Finance Regulation in most of the countries in the world and a growing trend of efforts in the matter over the last 20 years. Figure II shows the levels of the PFR Index in 2015. Countries in lighter shades of yellow have lower levels of regulation; inversely, countries in darker red shades have higher ones. In the map one can see clearly the high levels of regulation in Latin America, low levels in Africa and a mixed scenario in Europe and Asia, considering that there is no data in countries like China and Saudi Arabia.

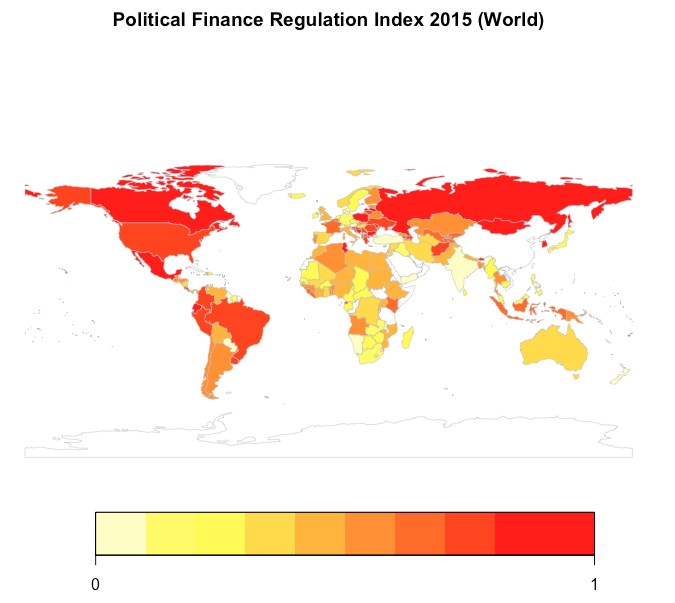


Figure II. Worldwide levels of PFR 2015

The yearly increase of regulation is evident in Figure III, which shows the changes over time of the PFR Index. This figure displays an increasing trend in the regulation effort in all regions. The slope remains positive for the period 1996-2005, increasing its steepness after 2006. Europe is the region that increased its party finance regulation the most, implementing 55% of regulations, with notable growth after 2010. The Americas and Asia occupy the second and third places respectively in terms of adoption of regulations.

Figure III. PFR Index times series by regions, 1996-2015: America, Europa, Africa, Oceania, and Asia

The increase of Party Finance Regulation has not been reflected in control of corruption. Figure IV displays the increasing trend of the PFR Index but also shows that the average of the CoC Indicator has stagnated and even displays a slight downward trajectory. The evolution of both suggests that the political finance regulation efforts made by different countries are not associated with an overall improvement in the control of corruption.

Figure IV. PFR and WB Control of Corruption Index time series, 1996-2015

The overall increase in the PFR Index is reflected in all of the categories of the database, although there are some small differences to note. Figure V shows that the regulation area that has increased the most in relative terms in all regions is *oversight and sanctions*, while the *public funding* has been the least regulated issue. Nonetheless, the figure displays that all the sub-indexes have increased systematically since 1996. This reflects a widespread trend around the world to increase Party Finance Regulation in a comprehensive manner, including regulations across the whole spectrum.

Figure V. PFR Sub-Index level in 1996 and 2015 by region. BLPI: Bans and limits on private income, PF: Public funding, RS: Regulation on spending, OS: Oversight and sanctions

## B) Political Finance Regulation and Control of Corruption in Latin America

The worldwide increase in the PFR Index is also reflected in the Latin American region. Figure VI shows that most countries have a medium or a high degree of PFR. However, there are exceptions like Bolivia, Venezuela and Paraguay, which show low levels in the PFR Index. Of our countries of interest, Mexico has a high level of regulation, while Argentina and Chile have medium levels. The following sections include different figures with different time periods, either 1996 to 2015 or 2006 to 2015. This is aimed to maximize the clarity of the changes of the different variables over time.

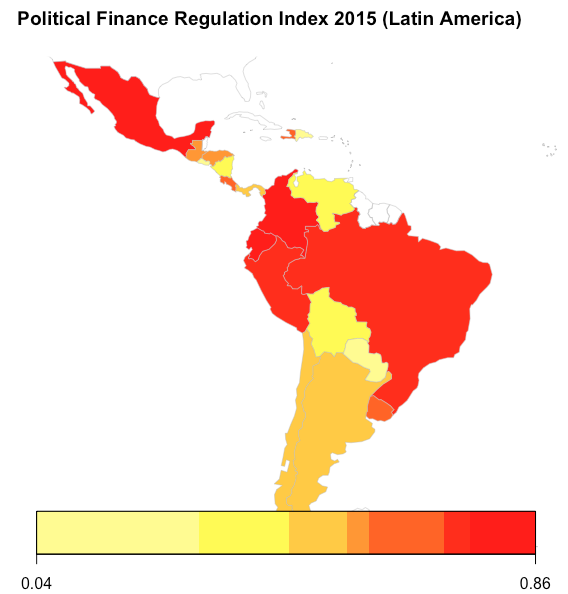


Figure VI. PFR Index in Latin America 2015

Following the worldwide trend, Figure VII shows the evolution for the PFR Index and its subcomponents for Latin America. The regulation category that increased the most is *oversight and sanctions*. In second place appears *regulation on spending*, followed by *bans and limits on private income* and *public funding*.

Figure VII. PFR Sub-index time series in 1996 and 2015 for Latin America. BLPI: Bans and limits on private income, PF: Public funding, RS: Regulation on spending, OS: Oversight and sanctions

Moreover, Figure VIII shows the levels of the PFR Index in 2006 and 2015 for Latin American countries. Results indicate that Ecuador is the country with the biggest increase in party finance regulation, followed by Mexico and Colombia. Contrarily, Paraguay and Dominican Republic show no change.

Figure VIII. PFR Index level in 2006 and 2015, Latin America

As with the rest of the world, in Latin America an increase in the PFR Index is not reflected on the CoC Indicator. Figure IX shows the average change in the level of political finance regulation for the region and the average change of the CoC Indicator from 1996 to 2015. The Figure also shows that while the CoC Indicator slightly improves for the period 1996-2010 in Latin America, this is reversed after year 2011 with a strong deterioration of the levels of corruption.

Figure IX. Mean PFR Index and World Bank Control of Corruption time series in 2006-2015, Latin America

The data shows that countries that increased their regulation the most between 2006 and 2015 are Ecuador, Mexico and Colombia, which is represented in Figure X. This suggests that increases in legislation are not always correlated with a reduction in the control of corruption. Ecuador seems to be the exception by showing an improvement in its control of corruption. In addition, Guatemala, Honduras and Uruguay have also shown improvements in the last decade.

Figure X. PFR Index and World Bank Control of Corruption change in 2006-2015, Latin America

The WEF Judicial Independence Indicator, as illustrated in Figure X, complements the relation between control of corruption and political finance regulation. Among all Latin American countries, there are three achievers in terms of control of corruption: Chile, Uruguay and Costa Rica. As seen in Figure XI, these countries also have the highest score of judicial independence. Within this group, Uruguay and Costa Rica made a significant amount of efforts regarding political finance regulation from 2006 to 2015, while Chile’s Index did not rise at their pace. Also, Uruguay and Costa Rica improved their CoC Indicator, while Chile´s worsened. This suggests that in countries with high levels of judicial independence, higher political finance regulation leads to an increase of control of corruption.

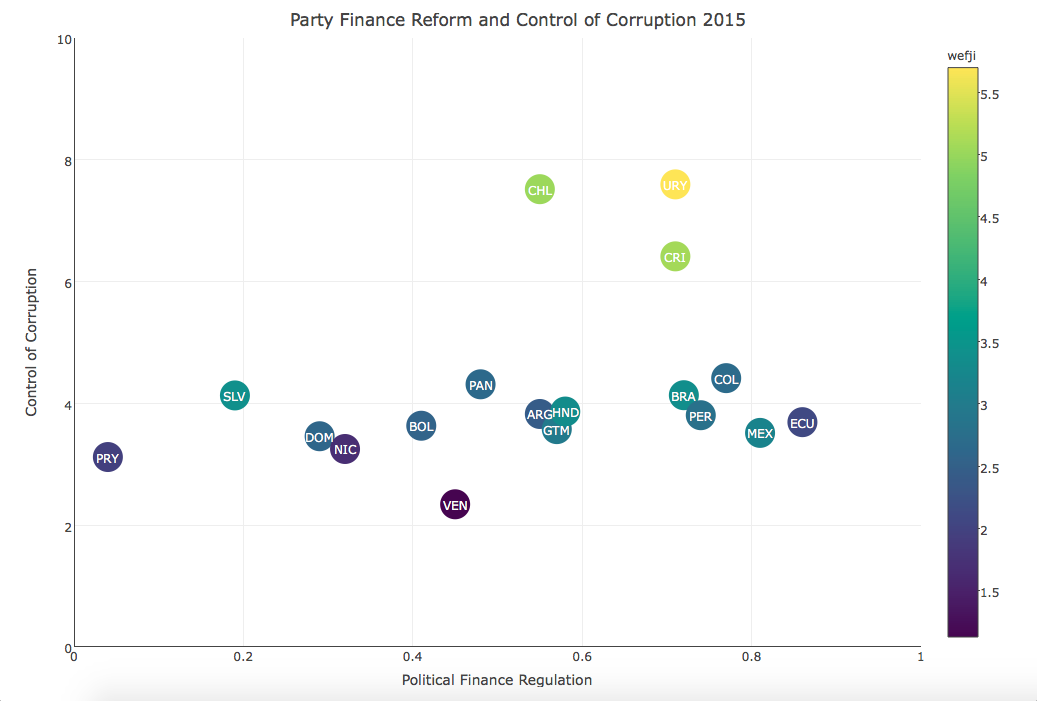
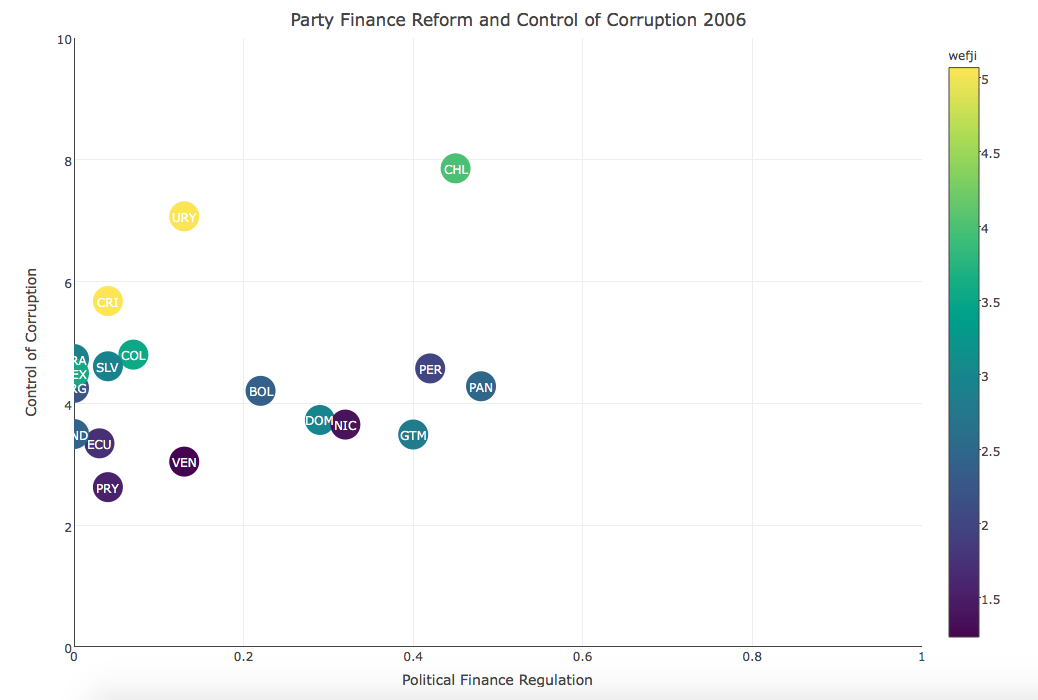


Figure XI. CoC, PFR and WEF Judicial Independence 2006 and 2015

## Panel regression model of Latin America

To further explore the relationship between control of corruption, political finance regulation and judicial independence, inferential statistics are necessary, allowing to further include other variables like public investment, as well as control for level of development. This model includes 18 countries of Latin America from 2006 to 2015.

### Variable description

As explained in the methodology chapter, the dependent variable is control of corruption, while the independent variables are political finance regulation, public investment and judicial independence, using the previously mentioned indicators. The regression model will intentionally resemble the equilibrium model described in the theoretical section of this study. In addition, life expectancy and the percentage of rural population and are included as control variables for level of development.

### Simple regression model

Table I shows the simple regression model, where results 1 to 9 are estimated using pooled OLS, fixed effects (FE) and random effects (RE). The first of the following equations represents 1 to 3, the second 4 to 6 and the third 7 to 9:

With respect to the results, party finance regulation has a significant positive effect on control of corruption in a pooled OLS model. This result is reversed when accounting for idiosyncratic characteristics of each country in panel estimations. Public investment and judicial independence have the expected signs, negative and positive, respectively. Thus, an increase in public investment is associated with deterioration in control of corruption. Inversely, increases in judicial independence are correlated with improvements in the dependent variable. Both regressors are statistically significant at usual levels of confidence.

|  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  | OLS | FE | RE | OLS | FE | RE | OLS | FE | RE |
|  | (1) | (2) | (3) | (4) | (5) | (6) | (7) | (8) | (9) |
|  |  |  |  |  |  |  |  |  |  |
| PFR | 0.750\*\*\* | -0.0649 | -0.0601 |  |  |  |  |  |  |
|  | (0.205) | (0.0491) | (0.0494) |  |  |  |  |  |  |
| PI |  |  |  | -0.265 | -0.496\*\* | -0.49\*\* |  |  |  |
|  |  |  |  | (0.503) | (0.230) | (0.228) |  |  |  |
| JI |  |  |  |  |  |  | 0.546\*\*\* | 0.0608\*\* | 0.151\*\*\* |
|  |  |  |  |  |  |  | (0.0229) | (0.0300) | (0.0310) |
| Cons. | -0.63\*\*\* | -0.27\*\*\* | -0.277\* | -0.27\*\*\* | -0.25\*\*\* | -0.264 | -1.96\*\*\* | -0.48\*\*\* | -0.76\*\*\* |
|  | (0.103) | (0.0232) | (0.158) | (0.0637) | (0.0190) | (0.171) | (0.0741) | (0.0918) | (0.124) |
|  |  |  |  |  |  |  |  |  |  |
| Obs. | 180 | 180 | 180 | 178 | 178 | 178 | 179 | 179 | 179 |
| R-sq. | 0.070 | 0.011 |  | 0.002 | 0.028 |  | 0.763 | 0.025 |  |
| N |  | 18 | 18 |  | 18 | 18 |  | 18 | 18 |

Table I. Simple Regression Model. Standard errors in parentheses, \*\*\* p<0.01, \*\* p<0.05, \* p<0.1

### Multivariate regression model

To better reflect the equilibrium model, a multivariate regression is needed. The multivariate regression model is estimated in equations 1 to 9. Results for pooled OLS, fixed effects (FE) and random effects (RE) are presented. Several results are offered to assess the robustness of the analysis. The equations for the models are the following.

The equation for 1 to 3 is:

The equation for 4 to 6 is:

The equation for 7 to 9 is:

The results are reflected Table II. Number 10 shows a fixed effects model of the last equation with robust standard errors to correct for heteroscedasticity and serial correlation, which were found after running regression diagnostics. The results of these tests can be found in the appendix. The estimated coefficients maintain their sign and statistical significance, as well as presenting similar magnitude.

Table II shows that increases in political finance regulation are related with a deterioration of control of corruption in Latin America. This relationship is statistically significant in the panel estimations. Inversely, the negative relationship between regulation and control of corruption becomes positive in countries with high levels of judicial independence. Furthermore, for countries with high levels of judicial independence, an increase in political finance regulation has a positive effect on control of corruption.

|  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  | OLS | FE | RE | OLS | FE | RE | OLS | **FE** | RE |
|  | (1) | (2) | (3) | (4) | (5) | (6) | (7) | **(8)** | (9) |
| **PFR** | -0.0601 | -0.0131 | -0.0078 | -0.81\*\*\* | -0.353\*\* | -0.380\*\* | -0.302 | **-0.309\*\*** | -0.320\* |
|  | (0.121) | (0.0567) | (0.0625) | (0.306) | (0.150) | (0.164) | (0.241) | **(0.140)** | (0.170) |
| **PI** | -0.287 | -0.551\*\* | -0.635\*\* | -0.879 | -3.53\*\*\* | -3.31\*\*\* | -8.00\*\*\* | **-2.37\*\*** | -3.41\*\*\* |
|  | (0.268) | (0.271) | (0.287) | (1.208) | (0.984) | (1.057) | (1.105) | **(0.936)** | (1.100) |
| **JI** | 0.551\*\*\* | 0.0691\*\* | 0.147\*\*\* | 0.419\*\*\* | -0.0299 | 0.0365 | 0.258\*\*\* | **0.0309** | 0.0971\*\* |
|  | (0.0253) | (0.0300) | (0.0309) | (0.0545) | (0.0345) | (0.0366) | (0.0424) | **(0.0385)** | (0.0394) |
| **JI×PI** |  |  |  | 0.189 | 0.902\*\*\* | 0.819\*\*\* | 1.914\*\*\* | **0.673\*\*** | 0.844\*\*\* |
|  |  |  |  | (0.353) | (0.279) | (0.301) | (0.304) | **(0.262)** | (0.310) |
| **JI×PFR** |  |  |  | 0.258\*\*\* | 0.110\*\*\* | 0.119\*\*\* | 0.108 | **0.108\*\*\*** | 0.0969\*\* |
|  |  |  |  | (0.0946) | (0.0413) | (0.0455) | (0.0729) | **(0.0393)** | (0.0471) |
| **LE** |  |  |  |  |  |  | 0.031\*\*\* | **-0.073\*\*** | -0.031\* |
|  |  |  |  |  |  |  | (0.00810) | **(0.0239)** | (0.0178) |
| **RP** |  |  |  |  |  |  | -0.02\*\*\* | **-0.011** | -0.02\*\*\* |
|  |  |  |  |  |  |  | (0.00218) | **(0.0106)** | (0.00519) |
| **Cons** | -1.93\*\*\* | -0.45\*\*\* | -0.69\*\*\* | -1.56\*\*\* | -0.146 | -0.354\*\* | -2.66\*\*\* | **5.378\*\*\*** | 2.351\* |
|  | (0.0797) | (0.0911) | (0.125) | (0.156) | (0.106) | (0.141) | (0.613) | **(1.937)** | (1.349) |
| **Obs** | 177 | 177 | 177 | 177 | 177 | 177 | 160 | **160** | 160 |
| **R2** | 0.760 | 0.060 |  | 0.770 | 0.189 |  | 0.880 | **0.264** |  |
| **(n, T)** |  | (18, 10) | (18, 10) |  | (18, 10) | (18, 10) |  | **(18, 10)** | (18, 10) |

Table II. Multivariate regression model. Standard errors in parentheses. \*\*\* p<0.01, \*\* p<0.05, \* p<0.1

The marginal effects plot in Figure XII illustrates this relationship, showing how different levels of the PFR Index and judicial independence interact with control of corruption, and it uses the following equation:

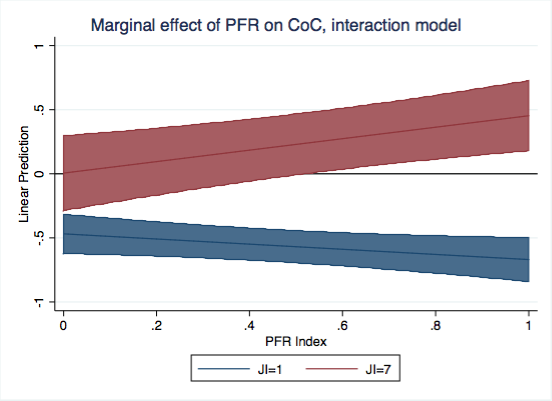


Figure XII. Marginal Effects of PFR on CoC for different levels of judicial independence

In a similar way, increases in opportunities to corrupt, represented by levels of public investment, have a significant and negative effect in control of corruption. This relationship is also reversed for countries with high levels of judicial independence. Figure XIII illustrates this with the following equation:

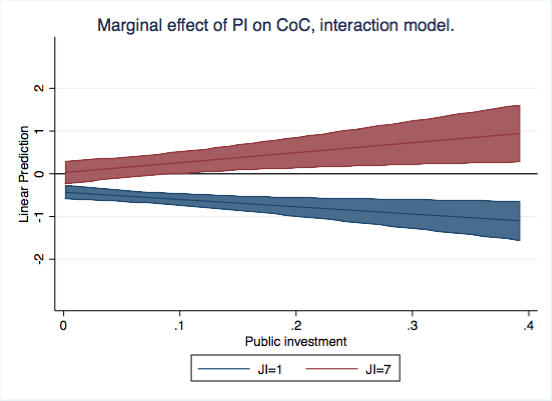


Figure XIII. Marginal Effects of PI on CoC for different levels of judicial independence

Furthermore, Figure XIV clarifies the relationship between predicted and actual values of control of corruption for Latin America. According to the equilibrium model, control of corruption values for Chile are significantly above predictions, while in Argentina and Mexico they are below the expected values, considering the levels of all the other variables.

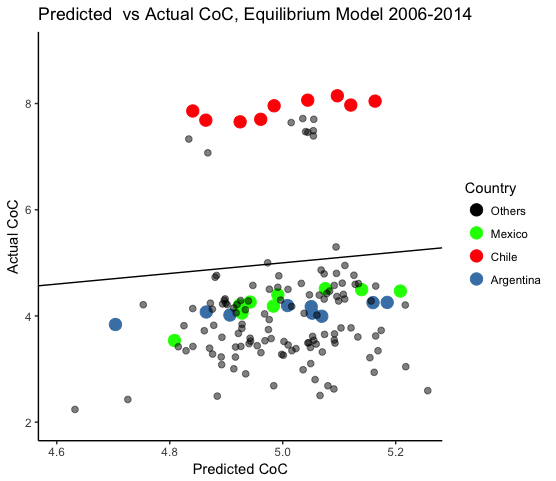
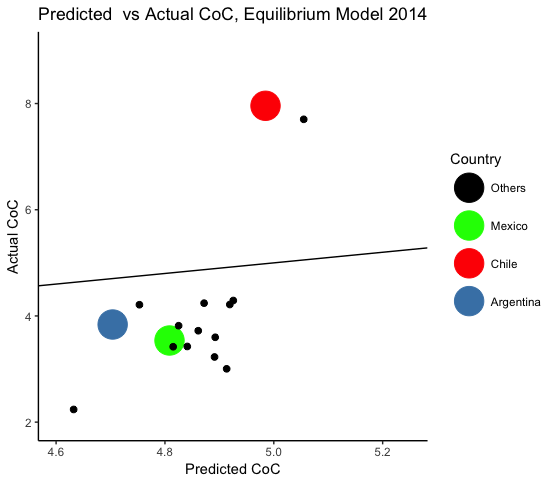


Figure XIV. Predicted vs. Actual CoC. Equilibrium Models 2014 & 2006-2014

In brief, efforts in terms of political finance regulation are effective only in countries with high judicial independence. As Figure XII shows, the marginal effect of passing new political finance legislation is significant when both judicial independence and the PFR Index are high. Conversely, in countries with low levels of judicial independence, adding rules to the realm of political finance is self-defeating, since control of corruption keeps deteriorating.

On the other hand, Figure XIII illustrates a very similar dynamic between control of corruption, judicial independence and public investment. In countries with weak judicial independence, increasing public investment impacts control of corruption negatively. Conversely, when judicial independence is high, increasing public investment does not necessarily extent opportunities to corrupt.

## How to improve control of corruption in Latin America?

Conclusively, the main results of the previous analysis confirm that in Latin America, judicial independence is a key variable to control of corruption. Table II highlights the negative correlation between the PFR Index and the CoC Indicator, as well as between public investment and the CoC Indicator. This means that, within our sample of countries and according to the data, an increase of the PFR Index and/or public investment is significantly correlated to worse performance in control of corruption. However, when both variables are separately interrelated with judicial independence, the correlation with control of corruption turns positive. This means that judicial independence is central for political finance regulation and public investment. Even more considering that judicial independence shows no significant correlation with control of corruption by itself.

According to the theoretical framework, societal control of corruption is the result of the interaction between opportunities and resources to corrupt and different kinds of institutional and social constraints. This equilibrium model theory suggests that improvements in control of corruption “can occur only gradually and through a succession of radical actions and disequilibria until a new equilibrium is achieved with a superior control of corruption” (Mungiu-Pippidi, 2015, p. 211) Therefore, domestic agency tends to be more effective than external governance strategies, and the particular context of a country is highly important to draft interventions in order to improve control of corruption. (Mungiu-Pippidi, 2015)

Besides this, the few countries that developed successful strategies to fight corruption applied their own models of state building, but they also followed others’ fruitful models when required. (Mungiu-Pippidi, 2015) With this in mind, we will focus on how to improve control of corruption in Argentina, Chile and Mexico. Considering the governance contexts of these nations, we will analyse how each country has been performing in control of corruption in relation with the rest of Latin America. The analysis will follow the explanatory variables set in this part.

# 5. Studies of Argentina, Chile and Mexico

The following section is comprised of analyses on changes in control of corruption, political finance regulation, judicial independence and public investment in Argentina, Chile and Mexico. Based on the results and on the best performers of the region, we present some guidelines to improve control of corruption in the three countries.

## Argentina

Argentina is a constitutional democracy organized as a federation of 24 political sub-unities: 23 provinces and the Autonomous City of Buenos Aires. It has a presidential system, which has been uninterrupted since 1983, when it was implemented following the end of a military dictatorship. In 2015, the country registered a population of 43.4 million of people and a GDP of 583 billion USD. Its life expectancy is over 76 years old and it has a GNI of 12.5 thousand USD. Within Latin America, Argentina is the third biggest economy and the fourth most populated territory. (World Bank, 2017)

### The Corruption Context

Corruption has been one of the main concerns of Argentina for the last decade. Even with an on-going economic crisis, people considered corruption one of the most relevant problems of the country in 2016. (Latinobarómetro, 2017) Similarly, a local survey from 2013 showed that 86% of Argentineans qualified corruption among the society as high (56%) or medium (30%) and only 13% considered it low. Furthermore, corruption was believed endemic and widespread in all public areas, affecting the political sphere in particular. (Universidad de Belgrano, 2013)

Global perception indicators are aligned with these results. The Corruption Perceptions Index (CPI) of Transparency International ranks Argentina 95out of 176 countries with a score of 36 out of 100. It also states that in 2016 Argentina improved 3 points compared to 2015, but only 1 point since 2012. (Transparency International, 2016)

Furthermore, the International Country Risk Guide from the PRS Group highlighted corruption as one of the most critical factors of the country’s political risk in January of 2015. (The PRS Group, 2015) Finally, the WGI ranks Argentina in 68 out of 208 countries, with the lowest scores being the most corrupt. (Kaufmann et. al., 2010)

While corruption has been relevant for a longer period of time, it was only in the last five years that it became one of the most prominent issues of concern in the country. The reason was the emergence of renowned cases of corruption, which involved the highest levels of the public and private sectors. Current examples include the local justice investigation of President Macri and his father for serious accusations related to the Panama Papers scandal (La Nación, 2017).

Also, the former President and Vice President are being prosecuted for embezzlement. Similarly, the former Minister of Public Infrastructure and Federal Investment was charged in 2016 with the crime of misappropriation of federal resources and one of his closest assistants, the former Secretary of Public Infrastructure was arrested in June 2016 while he was trying to hide 9 million USD in a monastery. (La Nación, 2016)

All things considered, we can observe that Argentina presents many characteristics of competitive particularism governance regimes as defined by Mungiu-Pippidi (2015). For instance, power is stratified but disputed competitively; the State’s autonomy tends to be captured by those who win the elections; public allocation of resources is particular and mainly dependent on the governing party; the separation between public and private sectors is weak and sometimes inexistent, and government accountability tends to be possible only when there is a change in ruling parties.

### Argentina’s performance within Latin America

Following, we present an analysis about how Argentina has been performing in terms on the main variables of this study with respect to Latin America. Table III provides a first glance of the country´s performance from 2006 to 2015 in absolute and relative terms.

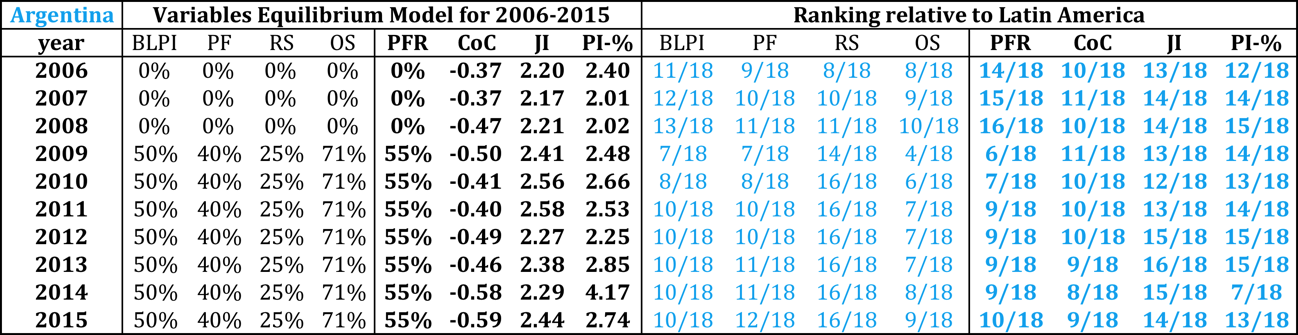


Table III. Argentina's variable change 1996-2015

Control of corruption in Argentina deteriorated by almost 60% between 2006 and 2015, when it reached its worst score from the last ten years. Despite some improvements between 2010 and 2013, as Table III shows, Argentina could not reverse the CoC Indicator’s downward trend for more than two successive years. These absolute numbers are important, because in 2015 Argentina ranked better than in 2006 compared to the rest of Latin America. However, this only means that other Latin-American countries have been performing worse than Argentina.

Figure XV. Argentina CoC, 2006-2015 (Source: own calculations)

Regarding political finance regulation, Argentina data shows significant efforts in 2009, which led the country to rise from the last positions in Latin America to the 6th place in the ranking.

Figure XVI. Argentina PFR Index, 2006-2015 (Source: own calculations)

Going into detail, Figure XVII shows that the category *oversights bodies and sanctions* was the most regulated (71%) in relative terms, followed by *bans and limits on private income* (50%) and *public funding* (40%), while *regulation on spending* remained the weakest category (25%). Beyond the particularities of this regulation, it is interesting to remark that one year after a legal reform in political finance passed in 2009, control of corruption improved. Nevertheless, afterwards it did not stop decreasing and in 2015, Argentina ranked 10 out of 18 countries in terms of political finance regulation. After 2009, the country passed no other regulation in the matter, while other Latin American countries did.

Figure XVII. Argentina PFR Subcategories (Source: own calculations)

In terms of judicial independence, the other constraint of corruption analysed, data shows a more negative scenario. From 2006 to 2015, Argentina was not able to join the best performing Latin American countries. Despite improving in absolute terms, the country moved back from the 13th position in 2006 to the 14th in 2015, becoming one of the worst performers.

Figure XVIII. Argentina Judicial Independence, 2006-2015

Finally, public investment in Argentina has been relatively low in terms of percentage of the GDP. As shown in Table III, it increased less than 0.3% from 2006 to 2015. While it had a visible rise in 2014, it fell back to its normal range the next year. It is important to note that elections were held in 2015, which following our previous analysis and described theories, could indicate a misuse of public capital expenses in 2014 to finance the electoral campaign. Moreover, the country is part of the first quartile of countries with the highest public capital expenses in absolute terms.

Figure XIX. Argentina Public Investment, 2006-2015

### The strategy to improve control of corruption in Argentina

Based on these results, Figure XX shows an analysis of the specific balance of the equilibrium model in Argentina compared with the Latin American average and the best performers of the region: Chile, Costa Rica and Uruguay. The goal is to identify the strengths and weaknesses of the Argentinean case, in order to build a control of corruption strategy, based on the best performers’ experiences and taking into account the local context.



Figure XX. Equilibrium Model for Argentina and Achievers

In the first place, Figure XX elucidates that Argentina is performing even below the Latin American average regarding its control of corruption and the reason is undisputable. While the three main achievers managed to develop high levels of judicial independence, Argentinean performance is one of the worst in the region, even below the average.

The rest of the picture shows that Uruguay and Costa Rica have high scores in the PFR Index, while Chile is at the same level than Argentina and in line with the Latin American average. This, as well as the results presented in the first part of this thesis, shows that increasing political finance regulation can have positive effects over control of corruption, but only if the judiciary is really independent.

Concerning public investment, two out of the three achievers assign a lower percentage of funds to public investments than Argentina. However, Chilean capital expenditures exceed Argentina’s, being at the same level than the Latin American average. This scenario is in line with the observation that, as long as a country has high judicial independence, public investment as a percentage of the GDP does not affect control of corruption negatively.

Overall, Argentina needs to enhance judicial independence to improve its control of corruption. Since these changes take time, the country also needs to improve public investment procedures to discourage corruption. Finally, the country should adopt better policies in the matter of political finance regulation.

### Judicial Independence

The topic of judicial independence has been debated in Argentina since the end of the dictatorship and the return of democracy in 1983. However, it gained significant relevance in the last years due to a combination of political decisions of the former and current governments and the rise of serious problems such as corruption. (Poder Ciudadano, 2016)

The lack of judicial independence in Argentina is said to be rooted in the early constitutional decision made by the Latin American founding fathers, aimed at creating an institutional system of *checks and balances* combined with a strong presidentialism*,* capable of guaranteeing the unity of the three powers. However, from that moment on, this decision enabled governments to rule over judiciaries and parliaments in most of the region. Hence, to improve judicial independence, it is considered necessary to balance the influence of the three powers, together with new mechanisms to enhance real participation of citizens in judicial processes. For example, Costa Rican and Colombian *tutelas* are considered successful tools to improve access to justice and judicial independence. (Gargarella, 2016)

Scholars highlight two problems that seriously affect judicial independence in Argentina. First, the paralysis of the Argentinean Judicial Council *(Consejo de la Magistratura)* created in 1994 to appoint national judges and reduce undue influences of governments over the judiciary. It is worth noting that in 2006 the ruling party managed to increase the government’s power within this body, which almost froze the processes to appoint judges and disciplinary. The second problem is directly linked to the first as it derives from the instalment of substitute judges, which in accordance to the law are appointed through a specific process that gives higher discretionary powers to the government and exposes temporary judges *(jueces subrogantes)* to stronger external influences. By 2015, almost 20% of the national judges were temporary and 75% of them had no fixed term. (Herrero & Leonardi 2016; ACIJ 2016)

Additionally, specialists also focus on the process to appoint justices from the Federal Supreme Court. The Argentinean Constitution states that the President shall appoint them with the consent of two-thirds of the present members of the Senate. In 2003, the ruling President signed an executive decree that significantly increased transparency in the designation of Supreme Court´s justices by establishing public audiences to debate their profiles. However, in 2016 President Macri appointed two new supreme justices by decree without following the existing process. This was considered a step back in terms of independence of the highest judicial authority in the country. (Saba 2016; ACIJ 2016)

Finally, the lack of transparency and accountability of the judiciary are other obstacles that undermine Argentina’s judicial independence. For instance, the Criminal Code prohibits the publicity of all legal cases, including those related to corruption. Moreover, the Supreme Court decided that the regulation that forces all public servants to disclose their personal patrimony, did not apply to the judiciary. (ACIJ 2016)

The obstacles to judicial independence in Argentina might explain the difference in performance regarding control of corruption in comparison with Latin American achievers. The specialized literature states that after the recovery of democracy in the last 30 years, most Latin American countries promoted reform processes of their judiciaries with different results. (Skaar 2003; Inclán & Inclán 2005; Sousa 2007)

Together with Chile and Costa Rica, Argentina’s reform is considered “far-reaching”CITA, since it covered an important number of issues. However, while in Costa Rica population’s trust in the judiciary is high, in Argentina it is one of the worst in Latin America. When it comes to the obstacles for judicial independence, in Argentina the problem seems to be the strong influence of the executive, while in Chile and Costa Rica, this is not an issue. In these countries, the dependence is mainly hierarchical, meaning that governments or parliaments do not influence the Judiciary but, within its structure, judges are subject to their superiors. (Popkin 2004; Sousa 2007)

Moreover, unlike Argentina, the Costa Rican executive and legislative powers have no influence over Judicial Council members´ designation. Furthermore, while comparing judicial reforms in Latin America, certain matters like quality, education, responsibility and transparency of the judiciary appear to be topics in which Chile and/or Costa Rica are performing better than Argentina. (Sousa 2007) For instance, the creation of a Judicial Academy, which plays a key role in training future judges, had very positive results in Chile. (Popkin 2004)

Finally, scholars conclude that success and profit from judicial reforms in Latin America have been related to transparent and participatory reforms, adjusted to social, economic and political local contexts. For example, the Committee of Ethic for the Judiciary created by the Chilean Supreme Court and the use of Internet to guarantee public access to most of the judicial information adopted by the Supreme Court from Costa Rica, are highlighted as two positive measures to increase transparency and accountability and to reduce corruption within the judiciary. (Popkin 2004; Sousa 2007)

Another difference regarding successful reforms of the judiciary is the gap between formal and real judicial independence. Argentina performs worse than Chile and Costa Rica in both areas, and bellow Uruguay in real judicial independence. (Sousa 2007) Even though scholars observe that Uruguay’s judicial reform was more superficial than the Argentinean and Chilean ones, mainly because it had no economical, historical or social incentives to drive the reform (Skaar 2003), the Uruguayan judiciary has been considered one of the most independent in Latin America. Practitioners remark the merit-based professional career within the judiciary as the key pillar of the system, which allows judges to make decisions against ruling politicians. (Miguel Loinaz 2015)

Another key issue that differentiates Chile from Argentina is the political parties´ commitment to assure real judicial independence. In Chile, the two biggest political parties agreed on providing independence to the Supreme Court and this led to positive results. During Argentina’s reform, this did not happen. (Skaar 2003)

In short, to improve judicial independence Argentina must take the following measures: 1) Reduce the influence of the governments over the Judicial Council; 2) Shorten the time taken by the Judicial Council to appoint new judges; 3) Recover the practice of public audiences for Supreme Court justices appointment and make them less discretionary; 4) Enable more civil society participation in judicial processes; 5) Improve the autonomy of the different stages of the judiciary from the government and the Parliament; 6) Develop a stronger merit-based structure within the judiciary; 7) Require permanent training and education to judicial servants.

Concerning the current balance of power and the contextual stakeholders map, it is important to mention that Argentina presents a window of opportunity to foster judicial independence. In the early 2000s, the civil society built up the movement called *“A Supreme Court for Democracy”* to protest a Supreme Court completely dependent of the government.Its role was key for the renewal of many justices and the adoption of transparency rules. Today, a new coalition of Civil Society Organizations called *“Coalition for the Judicial Independence”* has been founded, with the main goal of fostering reforms to enhance judicial transparency, impartiality and independence. (La Nación 2015)

### Public Investment Control

Judicial independence reforms are not simple and extend over long periods of time. Therefore, following our quantitative analysis results, Argentina could and should reduce corruption opportunities concerning public investment in the meantime to balance the control of corruption.

Unlike almost all Latin American countries, Argentina has no public procurement law. Public purchases are ruled by a presidential decree from 2001. Even worse, this regime does not include public infrastructure contracts, which are still ruled by a law from 1947. In the region, only Chile and Mexico have the same regulatory framework. Moreover, the Argentinean norm authorizes direct contracting in unjustified situations, an exception that is practiced abusively. Moreover, conflict of interest is poorly regulated too; former public officials, civil servants, their relatives, close friends and private societies are not disabled to contract with the state. Finally, the organ created to rule the public procurement system is not independent and has no control or punishment competences. (Volosin 2016)

The information related to public procurement tenders is also very limited. The official website of the Argentinean Infrastructure Ministry only publishes the call for applications and the only option to identify the winning companies is following the daily Official Gazette. Moreover, the public data made available by the National Office of Public Purchases dates only from 2006 to 2012, and the public procurement tenders are not registered.[[1]](#footnote-1)

The clearest example of the shortcomings of the discretion ruling public procurement happened in 2015, when the Minister of Public Infrastructure decided to publish the list of the top 40 private service providers of the state. It was a unilateral decision considered a response to a corruption accusation but because the methodology behind the list was never revealed, the outcome was seriously criticised by specialists. (Bidegaray 2015)

Looking at good practices among Latin American achievers, the adoption of technology by the Chilean government in the 1990s to make pharmaceutical purchasing more transparent, is considered a powerful success case for it improved savings and the access of poor people to essential medicines. The salient element was the implementation of an electronic bidding system that opened drug prices information, reducing the risk of collusion among suppliers. (Cohen & Montoya 2001)

The trend was intensified in 2003 with the launch of *ChileCompra,* a new system identified as the leading regional example of public purchasing modernisation aimed at enhancing transparency, preventing corruption and guaranteeing public accountability. The program included the creation of an agency that centralizes all public purchases, a website to facilitate the interaction between the State and its private suppliers and a register of public suppliers to gather information and to reduce paperwork in bidding processes. (Capello & García Oro 2015)

The use of websites by the public administration to increase transparency and public accountability has also been applauded in Uruguay. The improvement of the role of the National Internal Audit Office was also underlined. In addition, the Law of Access to Public Information adopted in 2008 and its mandatory trainings for public servants were received positively. Finally, popular perception about how much the fight against corruption had improved increased from 22% in 2004 to almost 60% in 2009, when regulations like a Public Procurement Code and a Public Procurement Disclosure Obligation were adopted. (Martínez Matute 2013)

Based on the aforementioned analysis, the country should: 1) Adopt a modern and comprehensive legal framework which regulates public procurement and public investments in general; 2) Enhance the legal framework which regulates conflict of interest to prevent collusion from former public officials, their relatives and other potential parties; 3) Make private property disclosure rules broader and stricter; 4) Assign independence, control and sanction attributions to the entity in charge of monitoring public procurements; 5) Increase the use of Information and Communication Technology (ICT) to augment transparency and accountability of public procurements and public investments; 6) Apply ICT to promote more competition among private suppliers; 6) Provide regular trainings for public servants.

### Political Finance Regulation

In 2009 Argentina had parliamentary elections and the governing party lost power. It was then that the government succeeded in passing Law 26,571, which modified the ruling political finance legal framework. This law was presented as a step forward in terms of electoral equity and party finance transparency but a deeper analysis shows the shortcomings regarding that assumption.

According to specialists, instead of improving transparency and equity, the law creates negative incentives that increase the corruption of the political finance system. For instance, it establishes a low limit for private donations, which leads to illegal methods of funding. Moreover, the law unified parties´ ordinary and electoral campaigns bank accounts, increasing the complexity to track money.

Also, the parties’ own advertising spaces were prohibited, limiting their access only to advertising spaces provided by the State. Furthermore, State advertising is unregulated, which, on the one hand, gives the government the opportunity to use advertising spaces with electoral goals, while on the other, it opened a broad margin of governmental discretion to influence the media through the assignment or cancellation of official advertising funds.

In addition, the sanctions’ system concerning transparency and accountability violations is weak and does not affect candidates. Finally, the judiciary has not complied with legal deadlines to sanction parties. (Ferreira Rubio 2012; Secchi 2015)

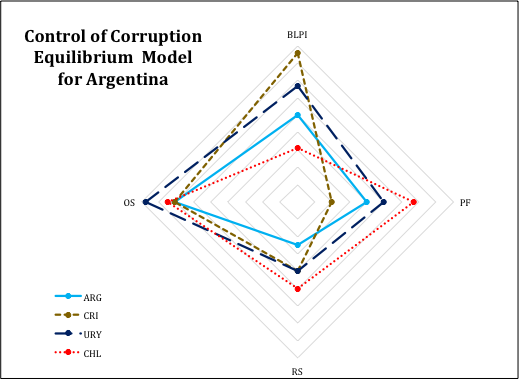


Figure XXI. Argentina PFR sub-indexes and Achievers

Beyond the main weaknesses of the Argentinean political finance system, there is a general agreement that, like in the rest of Latin America, the underlying problem is not the lack of regulation but the inability to enforce legal frameworks. (International IDEA 2014) Nevertheless, as shown in Figure XX, Latin American achievers regulate their political finance systems differently than Argentina, so identifying their patterns of regulation could be helpful to confirm the measures to adopt.

Chile, for example, made all the electoral funding and expenses information public (Poblete 2015) and in 2015, Law 20,860 assigned constitutional autonomy to the Electoral Service, the institution that manages and controlles the elections.

Costa Rica, for its part, eliminated limits to private contributions but kept the obligation of revealing donations’ origin and amount. This decision linked to a higher and robust control by the electoral body, increased transparency. The punishment regime is also positively valued in this country. (Brenes Villalobos 2015)

Finally, the establishment in Uruguay of a subsidy for parties´ permanent activities instead of electoral campaigns, together with the obligation to disclose all the movements of campaigns and parties functioning funds, are considered two pros of the new legal framework. (Olascoaga 2015)

Today, in Argentina, the government is promoting a reform of the electoral system The adoption of a unique ballot, the simplification of the electoral calendar and the creation of an autonomous body in charge of monitoring the elections, are the key topics under debate. (Müller 2016)

Conclusively, to improve political finance regulation, Argentina must: 1) Consolidate the autonomy of the National Electoral Office, which today depends of the Executive Branch; 2) Increase transparency and accountability of electoral campaigns’ donations and parties’ functioning funds; 3) Simplify the party finance system to enable money tracking by citizens and control bodies; 4) Reduce the government´s power to influence media and manipulate official advertising; 5) Promote effective punishment for parties, benefactors and specially candidates, in case of non-compliance.

## Chile

Chile is a Latin American country occupying a long, narrow strip of land between the Andes to the east and the Pacific Ocean to the west. Chile has been one of Latin America’s fastest-growing economies in recent decades, enabling the country to significantly reduce poverty. (World Bank, 2017) It has a population of 17.8 million and a GDP per capita of 23 046 USD. (OECD, 2017) Chile is a founding member of the United Nations, the Union of South American Nations (UNASUR) and the Community of Latin American and Caribbean States (CELAC).

### From colonialism to dictatorship

According to Silva (2016), high levels of public probity in Chile originated in the colonial period. The resource curse was prevented by factors like the absence of gold, Chile’s remote geographical location, earthquakes and the permanent state of war with the indigenous people. Inversely, richer Latin American colonies such as Mexico or Peru had lower levels of probity in public administration. The author emphasizes the quality of colonial governors in Chile as a key relevant factor because they promoted and maintained a “culture of public probity”, honesty and efficiency.

Silva states that this context of good governance highly influenced the local Creole: “Following independence, Chile possessed a local administrative elite who had assimilated the good practices of the late colonial administrations, thereby providing a relative degree of continuity in the running of everyday state affairs.” (Silva 2016, p. 180) The transition led to an early consolidation of the Chilean state, which fostered the establishment of strong institutions that “guaranteed the rule of law, economic progress and political stability.” (Silva 2016, p.181)

Similarly, Mungiu-Pipidi (2015) emphasized the role of the development of a centralized unitary state in the early independence in establishing a stable bureaucracy with an important degree of independence from the executive power. This process leads to the autonomy of the state from private interests, an important step in the control of corruption.

The parliamentary democracy period (1891-1925) is characterized by a strong expansion of state agencies and an increase in the number of public servants. This also led to an expanded bureaucratization of the state, which raised concerns as a possible source for corrupt practices. Even though high levels of public probity remained, political parties used bribery to gain votes, mainly in parliamentary elections. (Silva, 2016) Until the recent introduction of probity reforms, political finance affairs were related to most of the corruption scandals in Chilean history.

In the aftermath of the First World War, Chile adopted important institutional reforms to achieve high levels of probity within the state. According to Mungiu-Pipidi (2015) the main reform in this period was the creation of the National Comptroller Agency (Contraloría General de la República, CGR) in 1927, a “superior oversight body of the State Administration, contemplated in the Political Constitution, which enjoys autonomy vis-à-vis the Executive Branch and other public bodies. It is essentially an entity that controls the legality of acts of the State Administration and safeguards the correct use of public funds, independently of the Executive Branch and the National Congress[[2]](#footnote-2)”

This agency simultaneously fulfils the role of an “accounts court, auditor, supreme judicial reviewer of all government bills, and ombudsman” (Mungiu-Pipidi 2015, p. 134) fully independent from the executive and legislative branches. The author also states the important role of long-term tenures for the Ombudspersons at CGR, as well as the lifetime appointments of judges at higher courts, as relevant factors to achieve institutional independence in Chile’s early democratic stage.

During the governments of Frei (1964-1970) and Allende (1970-1973), Chile initiates a social process and economic reform, in which the national comptroller’s autonomy was not weakened and fully played its oversight role, with no deterioration in public probity. Similarly, Silva (2016) highlights the supervisory role played by the right wing opposition and mass media in maintaining public probity during this period.

During the Pinochet dictatorship (1973-1990) “many of the check and balance mechanisms to supervise the performance of the government were abruptly eliminated or neutralized”. Consequently, the judicial power, and with it the national comptroller, were no longer able to maintain their autonomy. In this context, “some of the neoliberal reforms applied by the military government also facilitated the realization of illicit transactions” (Silva 2016, p.186). Examples of these situations arose in the privatization process of state owned companiesthrough secret arm deals run by the military and in the payment of increased wages to public managers appointed by the military. In addition, corruption cases involving the personal enrichment of Pinochet himself and his clan occurred during this period (Silva 2016, p. 186).

On a complementary note, important economic achievements are regarded as consequence of the structural market reforms promoted during the military dictatorship. As such, Schmidt-Hebbel highlights the structural and macroeconomic reforms achieved during this period, which were further deepened and continued during the subsequent democratic governments. These reforms are regarded as one of the key drivers of the accelerated economic growth path that Chile lived in the next two decades after the 1980s. These figures reached average rates of GDP growth of 7.6%, and 5.9% in per capita terms (Schmidt-Hebbel 2006, p. 7).

Similarly, Mungiu-Pipidi highlights important structural market reforms made during Pinochet’s dictatorship, which counterbalanced incentives for rent seeking and promoted growth and competitiveness in the overall economy. Particularly, these reforms promoted market competition, privatization and decentralization. Significant reforms included “property rights security, a subsidiary role of the state, freedom of choice, elimination of price controls and trade quotas, fiscal consolidation and orthodox management of monetary and fiscal policy” (Mungiu-Pipidi, 2015, p.137).

### Transition to democracy

The restoration of democracy in 1990 under the government of Patricio Aylwin (1990-1994) “brought back the full reactivation of the oversight institutions of the government's performance, such as the Contraloría General, the judicial power, the parliament, the political parties, the mass media, private research institutes, and vibrant nongovernmental organization (NGO) communities” (Silva 2016, p.188).

Analysing the transition to democracy during the Frei government (1994-2000), Silva highlights that corruption scandals involving the state owned copper company CODELCO revived debates on public probity. The Frei government managed to establish several policy measures to tackle the issue, establishing a “high-level national commission on public probity (*Comisión Nacional de Etica Pública*)[…] which placed the corruption issue as being a national affair concerning everyone” (Silva 2016, p.190).

One of the noteworthy laws adopted in the framework of this commission establishes the principles of probity and transparency on which state agencies “are obliged to inform the community about the procedures which led to a formal decision, as well as to publish the documents related to that decision. Citizens also obtained the right to demand access to particular documentation and information from the public administration, which have to provide within a short period of time” (Silva 2016, p.190). As a result of this initiative, Civil Society Organizations, the press and political parties were able to play an important oversight role. In addition, other kinds of public probity offences such as the traffic of influence or misuse of public information were enforced.

Even though important progress was made during the Frei administration, corruption affairs directly linked to the funding of politics emerged during the next two centre-left governments. During the Lagos administration (2000-2006), corruption scandals arose from the Ministry of Public Infrastructure and Transport. Firstly, the “*Caso Coimas*” on which bribes were paid by contractors to get the right to operate vehicles inspection companies. The prosecution of this case led to a bigger corruption scandal that involved the whole ministry, when it was revealed that fraudulent contracts with fake companies were made to pay for bonuses to the ministry's staff in what was known as the “MOP-gate” scandal. As a policy response to this case, an improved system, the High Public Management System (*Consejo de Alta Dirección Pública*) was launched to contract public servants on a competitive and transparent manner through established rules and clear procedures for recruiting top officials at the state agencies.

During Lagos’ term, a new mechanism to improve public probity was established. Law 19,884 “On transparency, Limits and Control of Electoral Expenditures” of 2003 establishes limits on private donations for political parties as well as a blind mechanism that safeguards the anonymity of the donor, in order to avoid the risk of policy capture by interest groups in politics. Donations are paid through the Chilean electoral service, *Servicio Electoral de Chile* (*SERVEL*), which later distributes the resources to the beneficiaries. As explored below, flaws in this regulation are areas of possible policy capture by interests groups. Some of these pitfalls would be improved in recent reforms promoted by the Bachelet administration.

The first Bachelet government (2006-2010) started with several cases of corruption. The National Comptroller prosecuted the national agency of sports, Chiledeportes, for divesting public funds to fund political campaigns. On the other hand, in what was known as the “Publicam” case, a socialist congressman close to the government was prosecuted for the use of illegal funding mechanisms for his electoral campaign.

In response, the Bachelet administration promoted a comprehensive probity agenda to finance democracy and avoid conflict of interests. Unfortunately, there was insufficient political support in the parliament from both the government and elected officials. The core proposals of this failed agenda are the same as the probity agenda promoted 10 years later by Bachelet’s second administration. Moreover, the second probity agenda would surface in the aftermath of several corruption scandals in the context of illegal party finance and conflict of interests, where interest groups financed congressmen of different parties.

The agenda focused on improving the control and oversight of electoral spending, banning individuals who are found guilty of bribery and corruption from running for public positions or office, prohibiting legal entities as an income source to politics and requiring exclusive dedication to parliamentary functions[[3]](#footnote-3). None of these policies managed to get enacted, leading to more corruption scandals related to party finance.

Given the poor performance of the centre-left coalition in probity and transparency matters, the Piñera presidential campaign put a strong emphasis on the issue, promising a “new way of governing” (Silva 2016, p. 195). However, once elected, conflicts of interest from recently appointed public officials, pushed the topic of public probity back into the agenda. According to Silva, “at the end of the Piñera administration, the interrelationship between business and politics became profoundly condemned by the Chilean electorate, despite the excellent economic performance achieved by his government” (p. 197).

During the second Bachelet administration (2014-2018), new corruption scandals on illegal funding of electoral campaigns emerged in the context of tax evasion. (Bonnefoy 2015, The Economist 2014) In October of 2014 the *PENTA case* occupied the spotlight after an investigation conducted by the National Tax System revealed that PENTA, an important financial conglomerate in the fields of banking, healthcare and real estate, worth more than 30 billion USD in assets, financed campaigns of congressmen from the right wing party *Union Demócrata Independiente* (UDI) by means of illicit procedures. Politicians provided fake invoices to PENTA, which were assigned as expenses to illegally deduct taxes. Since several politicians also related to Bachelet’s coalition were involved in the case, both opposition and government had a “formal and legalistic” approach to these cases, trying to reduce them as “mere illegal activity of certain party members, and not as an expression of a generalized problem” (Silva 2016, p.198) that affects the whole political system.

This investigation led to prosecutions on tax fraud against the mining company SOQUIMICH, the largest lithium producer in the world, with 9.2 billion USD in assets (Casas-Zamora 2016), related to illegal funding of political campaigns of congressmen from different parties, as well as the Bachelet and Piñera campaigns. In the aftermath of these cases, Bachelet’s son was involved in a case of influence peddling.

After several months of strong press pressure in the spotlight, the Bachelet administration established the commission on “Probity, transparency and Traffic of Influence”. The commission, led by the Chilean economist Eduardo Engel, proposed a set of recommendations to regulate party finance affairs (Casas-Zamora 2016).

### Party finance and corruption

According to Silva, the historical process described above has consolidated the ability of the Chilean state to “maintain the rule of law and political stability” (Silva 2016, p.200). This played an important role to protect the country from the “emergence of widespread corruption” (Silva 2016, p.200), when compared with other countries in the region. The author emphasizes the strong legalistic culture in the country, the strong independence of its judicial power and the homogeneity of the population and united elites, in addition to a popular tradition for the respect of rules. This would lay the foundation for state oversight agencies, especially the National Comptroller Agency, to properly control the performance of the public use of resources.

This resonates with the analysis of Mungiu-Pipidi (2015) that throughout Chilean history, a gradual building of the control of corruption was achieved through each period of democratization, in addition to the market-oriented reforms from the 1980-90s. Moreover, she highlights these accomplishments as remarkable given the natural resources based economy of the country, which provides important opportunities for corruption and rent seeking. In this context, most of the corruption scandals in the spotlight were linked to the field of the finance of political parties, their activities and especially elections campaigns, and not related to the personal enrichment of the politicians involved.

### Party finance regulation and the improvement of the control of corruption in Chile

Table IV shows the overall trajectory of the main variables included in the quantitative analysis for Chile. In this set of indicators, the country has remained one of the top achievers in the region with respect to control of corruption and judicial independence. In terms of political finance regulation, Chile has not been able to keep the pace in modernizing its regulatory framework when compared to other Latin American countries in the last decade.

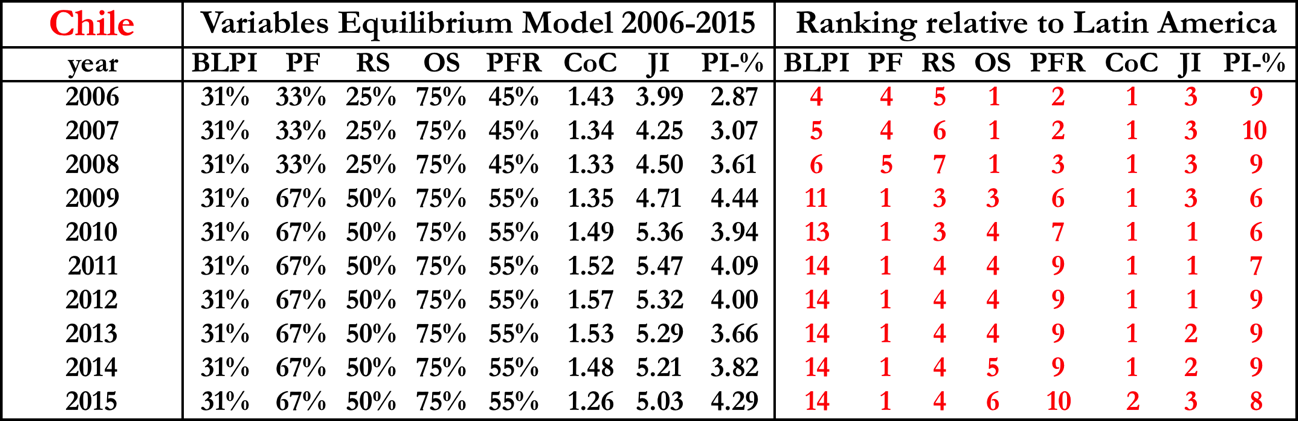


Table IV. Chile’s Variable Change 1996-2015

Chile’s PFR Index has remained above the Latin American average for the analysed timespan. In 2006, it was among the countries with highest amount of regulation in political finance in the region. In the subsequent years its PFR Index converged to the Latin American average, ranking 10 among 18 countries by 2015. Further increases in this Index are expected for 2016 due to the comprehensive agenda promoted by Bachelet’s administration.

Figure XXII. Chile CoC Indicator, 2006-2015

When quantifying progress on different areas of the PFR Index, important patterns are reflected that are addressed in the 2016 reforms. Firstly, important improvement opportunities will be achieved in the area of *bans and limits on private income*, the least regulated area in relative terms when compared to the Latin American mean, and in the bottom part of the ranking when compared in regional terms. Even though *public funding* regulation is advanced in comparison to other countries in the region, important improvement opportunities will be addressed, especially in expanding funds beyond the campaigning period. *Regulation on spending* currenlty aligned with Latin American average, will impose substantive additional regulatory restrictions on campaign spending. Finally, in *oversight and sanctions*, a constitutional reform to provide full autonomy to the electoral agency is at the core of the 2016? reforms.

Figure XXIII. Chile PFR Sub-indexes and Latin American Mean

Chile has remained as the top achiever in the region regarding the CoC Indicator, with a slight decrease of 4% between 2006 and 2015. It was only surpassed as top achiever by Uruguay in 2015.

Figure XXIV. Chile CoC Indicator, 2006-2015

Regarding judicial independence, Chile’s score is among the top performers as well. Between 2010 and 2013 the country was the top achiever in the region, falling two positions to occupy third place in 2015.

Figure XXV. Chile Judicial Independence, 2006-2015

Even though Chilean public investment is above the Latin American average when compared in USD billions, as a share of its GDP it remains moderate, slightly above 4%. Thus, opportunities to corrupt remain constrained in relative terms.

Figure XXVI. Chile Public Investment, 2006-2015

Chile’s equilibrium model analysis in this context seems straightforward. Figure XXVI, shows the four dimensions that balance the model. Being among Latin America's top achievers in control of corruption and judicial independence, as well as having limited opportunities to corrupt given its levels of public investment, the gap that balances the equation for Chile is its political finance regulation level. Figure XXVI shows that when compared with the Latin America mean, Chile performs slightly better, but laggs behind on its regulatory framework when compared with regional top achievers.

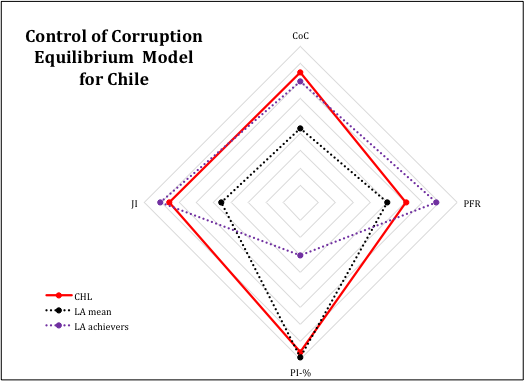


Figure XXVII. Chile Equilibrium Model

Based on this analysis, the probity agenda promoted in 2016 by Bachelet’s administration seems a correct policy response given the current Chilean context, characterized by high levels of judicial independence and above average levels of political finance regulation. As concluded in the quantitative section, the analysis shows that countries with high levels of judicial independence and high levels of party finance regulation, could achieve important improvements in their control of corruption, by increasing their PFR Index even further.

Weaknesses of the party finance regulation and required regulations

The former analysis of Chile’s current situation requires a more detailed revision of the weaknesses of the current party finance legislation in the country, and the improvements that are required to avoid future corruption scandals and policy capture risks by powerful interests’ groups, such as in the CAVAL, SQM and PENTA affairs.

### The probity agenda promoted by Bachelet’s administration

In the context of this analysis, Bachelet’s probity agenda seems like a correct policy response. The political finance regulation issues are being addressed as part of a reform that also encompasses the fields of probity, transparency and influence peddling in a comprehensive manner. This agenda was promoted in May of 2016 and includes 14 executive policies and 16 that should be voted in by Congress to strengthen democracy and safeguard the relationship between business and politics.

### Public funding contributions to political parties

According to the OECD (2016), public funding directed towards political parties is a strong mechanism for balancing the playing field in the process of democratic competition. Private contributions to politics are necessary and have a fundamental role in the democratic process. However, when parties’ income sources are highly dependent on big donors they become vulnerable to the risk of policy capture by powerful special interests.

Additionally, the specific mechanisms chosen to allocate public funds have important consequences on democratic competition and equity among parties. For example, the OECD (2016) states that public funding allocated based on previous electoral performances “may result in an uneven playing field for challengers and smaller parties” (p. 41). It is also recommended that public funds should be extended beyond campaigning periods, and finance the whole political cycle of parties. “To be effective, a comprehensive regulation of political finance should focus on the whole cycle including the pre-campaign phase, the campaigning period itself, and the period once the elected official takes office” (p.28)

The pre-2016 Chilean electoral system achieves the first equity criteria, since it allocates funds on the performance of current election, with a formula based on the amount of votes each candidate gets. However, public funding is only allocated for campaigning, excluding the broad political cycle. The new legislation allocates public funds to political parties for their daily activities, conditional on transparency and civil society involvement activities. Thus, in this new setting, campaigning funds would represent 50% of public funds disbursement towards parties. The other 50% would be allocated based on Congress representation and conditional on civil society involvement activities. In order to foster small donations and civil society involvement, a matching fund system is proposed, for which the state will provide additional funds to parties based on small donations received by citizens, which reduces the risk of policy capture by big donors. (Engel 2015, p. 72)

Another improvement is centred on mechanisms to promote gender equality through public funding. According to the OECD, political finance for female candidates “remains one of the greatest areas to their entry into politics” (p. 43). The new electoral law made improvements using a quota policy of 40/60, which meant no gender could have less than 40% representation of overall candidacy in every electoral district. In addition, at least 10% of public funding provided to political parties will be directed towards activities that promote the participation of women in politics (Figueroa, 2016, p. 127)

### Bans and limits on private income and limits on spending

The OECD deems private funding to politics an important channel for the political expression of citizens. However, when it is not regulated in a proper manner, it can turn into a main source of policy capture (p. 46). Here, there are some imbalances in the Chilean party finance landscape regulation. First, there is strong participation of private income in political parties’ budget, reaching more than 80% of the overall budget, compared to the OECD average of around 20%[[4]](#footnote-4) (IDEA 2014). Second, natural citizens as well as private companies are allowed to contribute to party finance to safeguard the anonymity of their identity. Third, there is no ceiling on private income donations to political parties.

The Engel commission (Engel 2015) produced recommendations on the matter aligned with OECD’s best practices, which were later enacted by law in the 2016 agenda. Important increases in public funding as well as more stringent limits on private donations were promoted to better balance both income sources in party budget. Overall spending limits were reduced by 50%, and limits were set in every electoral district. Important reductions on individual contributions were made, aiming to reduce the risk of policy capture and possible pressure from donors to candidates upon election.

Moreover, contributions from legal entities to political parties are prohibited. According to Figueroa (2016), the rationale is that they represent interests rather than preferences, since their relationship with politics is based on maximizing their profits rather than an advocacy on a political position. In addition, anonymous donations were also banned, according to best practices.

### Oversight and sanctions

In the Latin American landscape, it is widely recognized that there exists an important implementation gap between regulation in political finance and the current levels of weak its enforcement (Casas-Zamora, 2016, p. 13). Flaws in the oversight institutions encompass characteristics such as the lack of required independence and the legal authority or resources to properly enforce the legislation. (OECD, 2016)

In Chile, it is recognized that the supervisory body on the matter, SERVEL, has several areas of improvement. Currently, this institution lacks the legal faculties to implement an oversight role without faculties to levy sanctions, with its main purpose being to supervise administrative procedures. In addition, it does not have the required personnel to properly supervise political finance issues. From its permanent workforce, only 29% are professionals in charge of supervising on a permanent basis. The remaining personnel is in charge of operational tasks. In addition, temporary operatives increase only for the election period (Figueroa 2016)

However, the new legislation reforms include proposals to expand the institutional capacities of SERVEL. They will grant it full autonomy from the executive and the required faculties to properly oversee and levy sanctions when parties’ don’t comply with funding regulation. Budget increases and the required staff will also be provided.

### Integral ecosystem of reforms

The probity agenda addresses the main weaknesses in political finance legislation, but its scope goes beyond the relationship between money and politics, understanding it as part of a much “broader integrity-enhancing ecosystem […] In the absence of such a system, political finance rules are of limited value to protect the integrity of political institutions, no matter how strict they might be on paper (International IDEA et al 2015). “ (Casas-Zamora 2016, p.8)

Thus, “the reform package included changes to rules on lobbying and conflicts of interest, norms governing declarations of assets by public officials, corporate governance, and the creation of systems to monitor transparency and integrity levels in the public and private sector (Consejo Asesor Presidencial, 2015).

## Mexico

Mexico is a federal republic of 32 federal entities located at the north of Latin America. It has an estimated population of over 120 million, which makes it the eleventh most populous country and the most populous Spanish-speaking country in the world, as well as the second most populous country in Latin America, behind Brazil. Mexico is a member of the United Nations, the World Trade Organization, the G20, the Pacific Alliance and a founding member of the Open Government Partnership. Mexico joined the OECD in 1994, and was later followed by Chile, the only other Latin American country in the Organization.

The center-left Institutional Revolutionary Party (PRI) ruled the country from its foundation in 1929 to 2000, when it was defeated by the center-right National Action Party in 2000. The PRI returned to power in 2012 with the election of President Enrique Peña Nieto, whose single six-year term ends in 2018.

Mexico is the second biggest economy in Latin America and is classified as an upper-middle income country by the World Bank. It has the fifteenth largest nominal GDP and the eleventh largest by purchasing power parity in the world. (World Bank Group, 2017) Mexico could become the world's seventh largest economy in 2050 (Pwc, 2013), but it is decelerating with an annual GDP growth of 2.3% in 2016, down from 2.6% in 2015. This is due to a global environment of modest growth and stagnant trade. A further economic slowdown is expected from a slowdown of investment derived from the uncertainty of a potential renegotiation of the North American Free Trade Agreement (NAFTA). (World Bank Group, 2017) However, there is another aspect that obstructs the full economic potential of Mexico. The think thank Mexican Institute for Competitiveness (IMCO) estimates that corruption is costing Mexico from 2 to 9% of potential GDP growth.

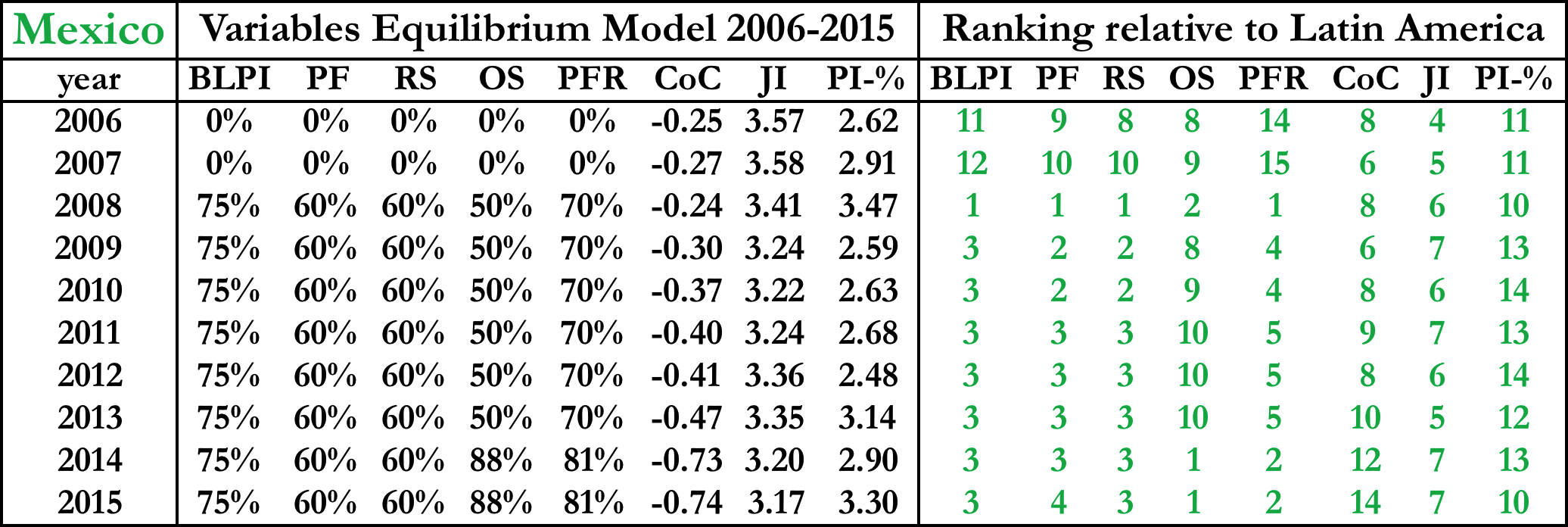


Table V. Mexico Variable Change, 1996-2015

### Corruption in Mexico

As shown in Table V, Mexico suffered the worst decrease in the region regarding the CoC Indicator from 2006 to 2015. Other evaluations from international organizations go in the same direction. According to the Heritage Foundation, widespread corruption has increased public dissatisfaction. (Heritage Foundation, 2017) Mexico ranks 123 of 176 in 2016’s Corruption Perceptions Index of Transparency International with a score of 30, a decrease of 5 points and 28 places compared to 2015. (Transparency International, 2016) In its Integrity Review of Mexico, the OECD warned that if corruption is not tackled effectively, it will be impossible to effectively address many of the other dire challenges facing the country: slumping productivity and competitiveness, stubborn inequality and serious regional security issues. (OECD, 2017)

Figure XXVII shows the fall of Mexico’s CoC Indicator from 2006 to 2015. The country decreased from 4.49 in 2006 in the recoded version of the index to 3.51 in 2015, almost a complete point decrease (half a point with the World Bank’s original coding). It also illustrates that this decline is higher than the one observed in the average of Latin America.

Figure XXVIII. Mexico CoC, 2006-2015

In the same sense, public perception about corruption reflects a negative trend. On the National Survey of Quality and Governmental Impact (ENCIG) from Mexico’s National Institute of Statistics and Geography (INEGI) of 2015, corruption is cited as the second most important problem with 51% of Mexicans considering it a main burden for the country, just behind insecurity and crime. In the survey from 2013, 49% reported that they believed corruption was a major issue in their state. (INEGI, 2015) Similarly, in the 2015 Latinobarometro survey, only 3.9% of Mexican respondents declared having high confidence in government, 17.1% some confidence, while 35.2 and 42.4% declared having low and no confidence respectively. (Latinobarometro, 2017)

The drop in rankings and confidence is related to recent high-profile corruption scandals that have dominated news cycles. In November of 2014, journalist Carmen Aristegui published a report exposing how a company with multiple infrastructure government contracts owned the mansion described by the First Lady as the “real family home” in a society magazine. (Tuckman, 2017) In August of 2015, Comptroller Virgilio Andrade, a presidential appointee, cleared the President of any wrongdoing. (Alper, 2015)

Two years later, during the signing of the General Law of the National Anticorruption System (NACS) in 2016, the President acknowledged that the scandal had hit his government's credibility, but claimed that his family had done nothing illegal. (Partlow, 2016) The biggest drop seen in Figure XXVII is recorded in 2014, the year of the corruption allegations against President Peña Nieto.

Two of the other most well known cases of corruption are also from members of President Peña Nieto’s PRI, although it is worth mentioning that corruption is not limited to that party and there have been corruption scandals involving politicians from the most popular parties as well. The former governor of the Tamaulipas state, Tomás Yarrington, was indicted by a jury in the United States on charges of drug smuggling, bank fraud, racketeering, money laundering and taking millions of dollars in bribes from the Gulf Cartel and other traffickers since 1998, when he was the mayor of Matamoros. After almost five years on the run, Yarrington was arrested in Italy on April of 2017. (Elefteriou-Smith, 2017)

After an investigative report on the website Animal Politico, Javier Duarte, the former governor of the Veracruz state, fled the country at the end of his term in 2016 amongst allegations of corruption, involvement in organized crime and embezzling millions of dollars. Further fueling citizen’s anger, the new governor Miguel Angel Yunes accused Duarte’s government of giving sugar-water instead of chemotherapy to children with cancer. A few days later after Yarrington’s arrest, Duarte was apprehended in Guatemala. (Al Jazeera, 2017)

The common theme of these cases is that the investigations did not come from the Mexican political system, neither from oversight authorities nor opposition parties, but from other sources, in two cases from the media and in another from judicial authorities from the US.

Aimed at restoring the credibility of the Mexican political system, the aforementioned NACS is just the latest of reforms that aims to fight corruption in the country. According to the OECD, the eight laws that create the System aim to overcome “key shortcomings of the past” by addressing fragmentation in policies, avoiding implementation gaps, improving co-ordination between levels of government, strengthening enforcement mechanisms and reinforcing oversight through greater transparency, expanded auditing powers and involvement of civil society. (OECD, 2017)

Specifically, the laws include a governance structure comprised of a NACS Co-ordination Committee, a Citizen Participation Committee and ethics committees in ministries. They also involve a revamping of codes of conduct for public officials, as well as the federal manual for internal control and risk management standards. Also, they include the development of an online platform comprised of key databases of sanctions and procurements, to support better detection and oversight. (OECD, 2017)

Furthermore, the law requires that states develop their Local Anti-corruption Systems (LACS) and respective committees. It will oblige more rigorous asset and interest declarations of all officials, and both government employees and firms involved in public sector activities will be subject to a new disciplinary regime for integrity violations. Finally, it demands the enlisting of Specialized Anti-corruption Prosecutors to prosecute acts of corruption. (OECD, 2017)

Nonetheless, it appears that NACS got off on the wrong foot. In April of 2017, the president of the Citizen Participation Committee Jaqueline Peschard denounced that the System was instated without the Specialized Anticorruption Prosecutor and the regional authorities in charge of imposing sanctions to public servants that commit serious offenses. Mexico’s main parties apparently could not agree on a Prosecutor, which shows the lack of political will to implement the NACS. (Castañeda, 2017)

### Political Finance

Political finance reform was an integral part of the transition of Mexico to a multi-party system. The formulation of some form of public funding for political parties started in the 1960s, but broad political reform was accelerated in the 1990s, during a crisis of credibility of the PRI and the incorporation of the country to the NAFTA. The reforms prohibited public entities from contributing to political parties and banned contributions by businesses, churches, individuals who live or work outside of Mexico and foreign entities. Moreover, the reforms mandated reports from parties to electoral authorities detailing private contributions and all expenditures. (Maldonado et al., 2004)

In efforts to further amend the political finance system, comprehensive reforms were passed after 2005, which is reflected in Figure XX. This displays the sensibility of the PFR Index to the most recent amendments of existing laws. The figure also shows that Mexico has a higher level of regulation than the average of the whole region, an inverse relationship than the one observed regarding the CoC Indicator.

Figure XXIX. Mexico PFR Index, 1996-2015

The reform of 2007, implemented after the contentious 2006 presidential election in which Felipe Calderon became president, altered the financing of political campaigns. It changed the formula for the allocation of public funds to political parties and increased the importance of winning seats, by linking electoral victories to future funding. It also limited private contributions to 10% of the total money that was spent in the previous presidential campaign. (O’Neil, 2013)

In a similar way, the most recent political reform of 2014 introduced a new national electoral body to organize elections all over the country and the reelection for Senators and Deputies for up to 12 years. Also, it amplified regulation by increasing the grounds for annulment of election, specifically by exceeding the permitted funding, as well as by expanding the definitions under which a public servant might break electoral rules. Furthermore, it increased the voting choices for Mexicans voting abroad, gender parity rules and increased the threshold of votes for a party to maintain registry and public funding. It introduced the figure of coalition governments and, in response to a push by civil society, independent candidates, who can now participate in elections and receive public and private funds. (Woodrow Wilson Center, 2015)

However, political finance reform has been ineffective to counter corruption due to a failure of enforcing the rules and there are no signs that the latest efforts will be any different. Electoral authorities lack the necessary tools to truly monitor the campaign financing process, which could be constituted by illegal campaign contributions at more than four times the legal amounts. (O’Neil, 2013) Also, they fail to address two of the worst problems for democracy in Mexico, vote buying and the infiltration of drug money in campaigns. According to the findings on this study, political finance will only be effective if there are steps taken with regards to the independence of the judiciary.

### Judicial Independence

Parallel to the CoC Indicator, there is a downward tendency on the WEF Judicial Independence Indicator from 2006 to 2015. This tendency is reflected in Figure XXIX and might be related to the controversy that has surrounded the three nominations that President Peña Nieto’s made to the Supreme Court. The figure also shows that Mexico is almost in the same level as the region average.

Figure XXX. Mexico Judicial Independence, 2006-2015

However, the downward trend starts before Peña Nieto’s rise to power. This might have to do with the beginning of former President Felipe Calderon’s ‘drug war’ . The inability of the judiciary and the police to assume responsibility over security was one of the reasons Calderon decided to introduce the Army to fight against drug cartels in the country. Calderon often bypassed national courts and extradited drug traffickers to the United States almost immediately after being captured. (Insight Crime, 2011) It is worth mentioning that the security situation did not improve with President Peña Nieto.

Aware of the judiciary’s operative problem, Mexican authorities pushed for the most significant change to the system, a 2008 amendment requiring that all state and federal judicial systems transition from a written-based inquisitorial system to an oral-based accusatorial. States that have complied with the reform say that it has helped them to better allocate of criminal justice resources. However, the reform has been criticized because it does not go far enough in punishing corrupt judges. (Corcoran, 2012)

### Public Investment

The indicator of public investment, which is based on data of capital expenditures by the ECLAC, shows an overall increase of spending in absolute terms since 2006, as shown on Figure XX. Compared with the rest of Latin America, public investment as a percentage of GDP is below the mean, which would be explained by the sheer size of the Mexican economy. In absolute terms, there was a decrease in spending following the 2008 international financial crisis, but it did not fall below 2.48% of the GDP. After this bump, public investment further increased when President Peña Nieto took power.

Figure XXXI. Mexico Public Investment, 2006-2015

An example of this kind of investment under President Peña Nieto is the new airport in Mexico City, which will cost arpund 9.4 billion USD and is expected to open in 2020. (Luhnow, 2014) To maintain a growing public investment in a context of low income from oil exports, the government has increased the national debt. In March of 2017, the debt stood at 9.68 trillion MXN (522 billion USD). (Rodríguez, 2017)

As specified above, public investment acts as an opportunity of corruption if the procurement process allows corrupt public officials to favor specific companies in which they have a stake. In this context, it is important to highlight that the scandals involving President Peña Nieto are related to this type of corruption.

### Improving control of corruption

As in the case of Argentina, judicial independence seems to be the key variable for controlling corruption. The previous analysis show that despite enacting reforms and increasing its PFR Index, the CoC Indicator has decreased, further hit by the increase of public investment in real terms. It also shows that the level of judicial independence is above the average of the region. Nevertheless, this indicator needs to increase to the levels of the high achievers of the region to have an effect on the other variables of the model.

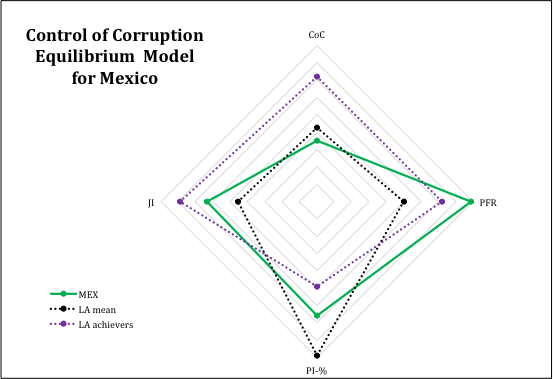


Figure XXXII. Mexico Equilibrium Model

While Figure XXXI shows that Mexico is above the high achievers in terms of party finance regulation, this does not translate to lower levels of corruption. It also displays that Mexico is below the region mean in public investment as percentage of the GDP but above the high achievers, which is consistent with the findings that this kind of investment is an opportunity for corruption, specifically with lower levels of judicial independence. In this respect, Mexico is above the region’s average but below the high achievers. With this in mind, actions should be aimed at strengthening judicial independence and the rule of law.

The most important changes concerning judicial independence in Mexico can be traced to the 1990s. Foreseeing that his party was going to become the opposition for the first time in its existence, former President Ernesto Zedillo pushed for a reform in 1994 aimed at the independence of the Supreme Court. Aspects of that reform were to remove the direct designation of judges by the presidency and an institutional design to ensure its permanence and stability. With the PRI back in power, President Peña Nieto has been able to nominate three spots to the eleven-judge body. However, all of these nominations have been criticized by civil society organizations for responding to partisan quotas and the lack of transparency of the confirmation process in the Senate. (Cárdenas, 2015)

President Peña Nieto’s nomination of former Attorney General Eduardo Medina Mora was the most criticized of all three. This was due to Medina Mora’s previous role as Mexico’s top prosecutor, as well as his work as head of the defunct Secretariat of Public Safety and the organized crime division of the Office of the Attorney General. Civil society organizations denounced that Medina Mora had exercised discretionary power in these agencies and used them for his political aims. (Cárdenas, 2015)

Furthermore, judicial independence in Mexico is limited by the way the judicial branch receives its funds. The executive and legislative branches control the judiciary’s budget, so each year the judiciary has to bargain for it. Distinct from other countries, the Mexican Constitution does not specify a percentage of GDP for the judiciary. (Pozas Loyo & Ríos Figueroa, 2006) This makes the judiciary dependent of the political system despite all written rules to make it autonomous.

Another challenge for Mexico’s control of corruption is related to the judiciary’s capabilities to resist organized crime. Mexico's judicial system is also highly susceptible to corruption because of what the CFR has called “autocratic judges and lack of transparency”. (Lee, 2015) There is also a lack of confidence in the justice sector, so crimes are underreported, which creates widespread impunity. (Shirk, 2011)

A case that illustrates the weakness of the Mexican judiciary and its vulnerability in resisting private interests is the case of Judge Anuar González. The judge from the Veracruz state ordered the release of a young man from a rich and powerful family accused of sexually assaulting a schoolgirl, on the grounds that the perpetrator did not enjoy it. After the outrage over the decision reached international media and led to mass local protests, the Council of the Federal Judiciary suspended González and informed that it would review all of his decisions to look for any ‘irregularities’. (Erickson, 2017)

The recent reform to the judicial sector is considered a way to strengthen the branch but recent information about its implementation paints a bleak picture. Citing a study about the impact of the reform on the state of Morelos, Jose Pardinas, director of IMCO, it failed to address the problems during the prosecution stages prior to the case being presented before a judge. It criticized the lack of investments in training the personnel in charge of procurement, which is often overworked and underpaid. (Milenio TV, 2017)

To overcome the implementation gap of the judicial system, the IMCO recommends improving the operating conditions of the prosecuting system. Specifically, it proposes to increase the number of public defendants and experts, as well as distributing them based on criminal incidence, while guaranteeing conditions of autonomy. It also advocated to increase the number of prosecuting agents and to create an Audit and Monitoring Unit to monitor the quality and delivery of justice. (Instituto Mexicano para la Competitividad, 2017)

This shows that despite reform efforts, Mexico still has a long way to go in terms of ensuring the independence of its judiciary and the functioning of its judicial branch. Among the options that the government should follow are: a) ensure the transparency of the nomination process of all judges, b) guarantee the participation of civil society in this process and follow their recommendations, c) evaluate the funding process of the judiciary branch and consider locking a budget based on a percentage of the GDP or the revenue of the government to ensure its financial independence, d) improve the funding for the prosecuting part of the judicial system, so that judges can work with more efficient information e) reduce capital expenditures, public funding for political parties and invest part of the savings in the judicial branch.

Fundamental for all of these changes is the involvement of civil society. Civil society organizations have been participating increasingly in the transformations of the judicial branch, either by participating in the public debate about nominations to the Supreme Court or by assessing the success of the judicial reform.

The government should also look at the success of the high achievers in the region in terms of control of corruption and judicial independence, which are Chile, Costa Rica and Uruguay, to work towards the professionalization of the judiciary and towards a merit based system. Most importantly, the government should divest resources from capital expenditures, which are much higher than those of the high achievers in the region, towards the professionalization and increase of salaries of prosecuting and judiciary personnel, as well as in the creation of effective oversight entities to strengthen enforcement of regulations and reduce the likelihood of corruption. In the same sense, it should consider decreasing the amounts of funding for parties, since these resources are used as opportunities to corrupt and not to increase the voice of citizens on the democratic process. However, any cut to the parties’ resources could be met with resistance.

The last political reform in Mexico led to the election of Pedro Kumamoto, an independent representative on Jalisco’s State Congress, who won his seat in 2015 when he was 25 years old. In consonance to citizens’ demands, Kumamoto has been leading a campaign to decrease funding of political parties and increase electoral participation. The proposal, which has been backed by civil society and business organizations would calculate the funding for each party depending on turnout and not on the registered voters. Voting for the proposal has been delayed to the end of April and will be a test to see if political parties are willing to reduce their resources in favor of citizens’ demands. (Yo Ciudadano, 2017)

## 6. Conclusion

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