

Integrity in public policy

Keys to prevent
corruption

Executive summary

Integrity in public policy

Keys to prevent corruption

Executive summary

Title:
Integrity in public policy: keys to prevent corruption
Executive summary

Legal Deposit: DC2019001640

ISBN: 978-980-422-152-1

Editor: CAF
publicaciones@caf.com

The views expressed in this publication
are the responsibility of the authors
and do not necessarily represent the official position of CAF.

Graphic design: Estudio Bilder / Buenos Aires.

Printed in: Panamericana Formas e Impresos S.A.
acting only as a printer
Bogota, Colombia - October 2019

The digital version of this book
can be found at: scioteca.caf.com

© 2019 Corporación Andina de Fomento
All rights reserved

Executive summary

Corruption has been one of the main concerns of Latin Americans for some time now. Indicators of corruption perception have shown relatively high levels in the region at least since the 1990s, and current data suggests that this has not changed. In recent years, this has become a central issue in the public debate, following numerous cases that affected the political system of several countries.

Governments in the region have launched reforms that are both a cause and a consequence of recent investigations and scandals. Although some countries show more concrete progress than others, the general panorama shows a broad spectrum of initiatives in this regard, ranging from investments to improve institutional capacities and transparency in public service to changes in legal instruments to prosecute and punish corruption.

This report presents an outlook on how this agenda is unfolding in Latin America and highlight the remaining challenges to reduce the incidence of corruption. The objective is to identify the most important lines of action based on previous experiences in the region and elsewhere, and on the evidence collected in this document.

Measuring corruption

Corruption is very difficult to quantify. Since it refers to illegal practices, there are no databases available with complete information. This poses major challenges to anyone who wishes to measure the extent and prevalence of the problem, as well as to anyone who wants to study its causes and consequences.

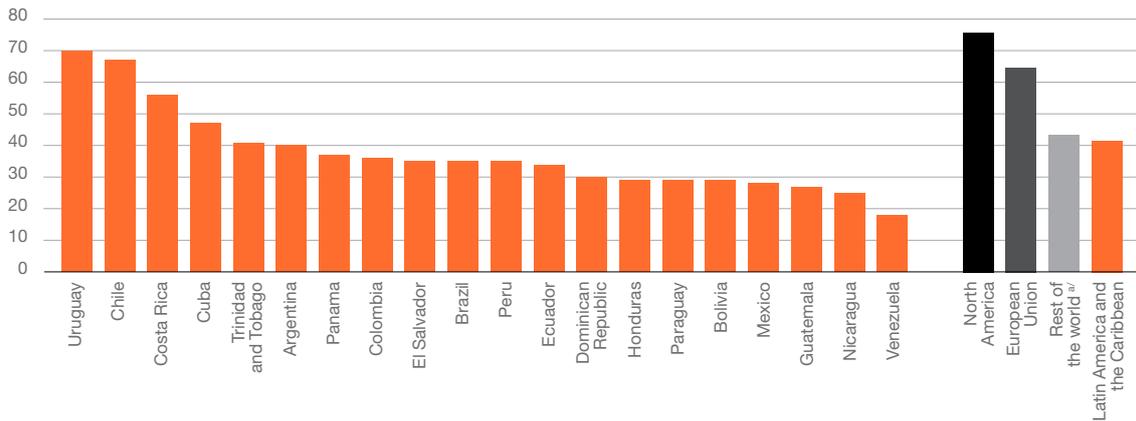
Estimates of corruption levels are usually based on perception and victimization surveys, or on data concerning cases that have been investigated and adjudicated through official proceedings. An alternative approach is to measure the institutional quality to fight and control corruption in a given jurisdiction, for example by constructing indices based on the views of experts and relevant actors.

Indicators published by Transparency International suggest that corruption perceptions in Latin America and the Caribbean are slightly higher than in the rest of the world, and much higher than in more developed regions (Graph 1). Chile, Costa Rica, and Uruguay stand out in the region with values close to those of high-income countries, a pattern that is also apparent in other indicators.¹

1. Unfortunately, due to methodological changes, this index can only be used to make comparisons after 2012, and no significant changes in the region are apparent since then.

Graph 1 Transparency International's Corruption Perceptions Index

Index (higher scores indicate lower perceived corruption)



Note: This graph shows scores for the 2018 Corruption Perceptions Index. The index ranges from 0 to 100, where higher scores indicate lower perceived corruption. Bars on the right show average scores for countries in Latin America and the Caribbean, in North America, in the European Union, and in the rest of the world.

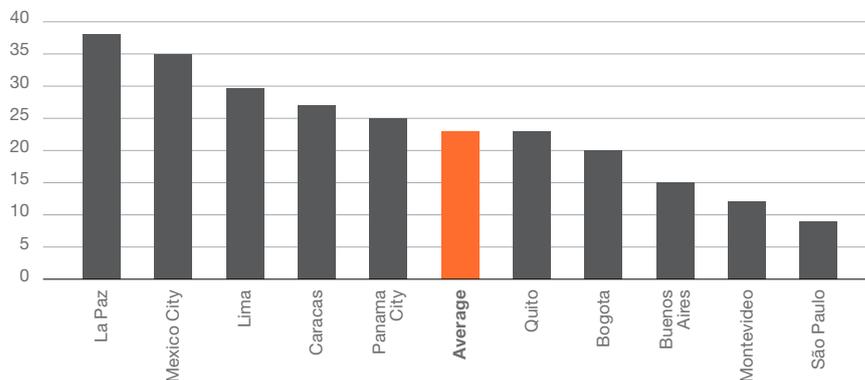
a/ Indicates the world average without considering Latin America and the Caribbean's countries.

Source: Compiled by the authors, based on data from the Corruption Perceptions Index (Transparency International, 2018).

Victimization figures are also relatively high. Results of the 2018 CAF survey show that 23% of respondents were asked for a bribe or an informal payment in order to access a public service or to expedite an administrative procedure over the previous year (Graph 2) (ECAF 2018).

Graph 2 Bribe solicitation in Latin America

Individuals who have been asked for a bribe (%)

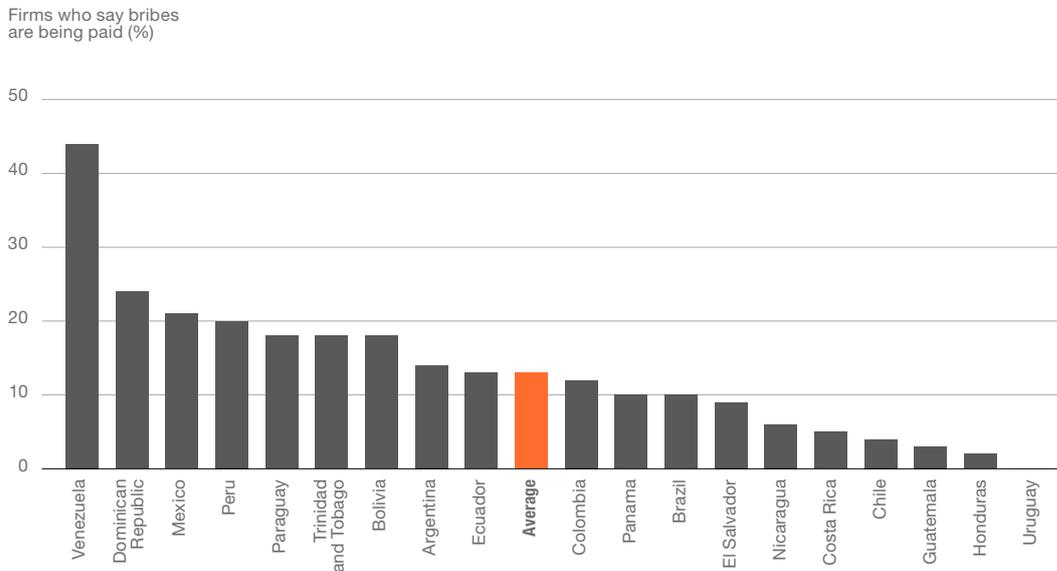


Note: This graph shows the percentage of respondents who reported that at least one public servant had asked them for a bribe over the previous year. A percentage is calculated for each city, and then a simple mean for these cities.

Source: Compiled by the authors, based on data from ECAF 2018 (CAF, 2019).

In the business sector, 13% of the executives and owners of Latin American firms surveyed in the World Bank Enterprise Survey believed that companies like their own paid bribes to secure government contracts (Graph 3) (World Bank, 2019).

Graph 3
Incidence of bribery: perceptions among business executives



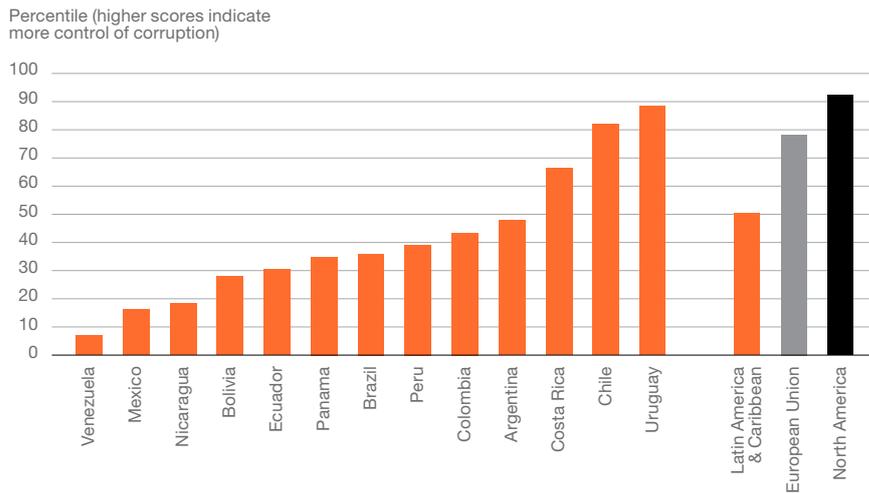
Note: This graph shows the percentage of respondents who say firms like their own pay bribes to secure a government contract. It is calculated as a percentage of all industrial companies who obtained or tried to obtain a government contract over the 12 months prior to the survey. Percentages (unweighted) are reported by country, along with a simple mean for these countries. This is based on the most recent available data for each Latin American country (over the period 2009–2017).

Source: Compiled by the authors, based on data from the Enterprise Surveys Indicators (World Bank 2019).

Furthermore, the World Bank’s Worldwide Governance Indicators—which are based on the analyses and opinions of experts and key actors—point to institutional deficiencies in Latin American countries. Graph 4 presents the control of corruption indicator in the year 2017, showing a significantly worse average performance in Latin America and the Caribbean than in North America and the European Union². However, there is substantial heterogeneity within the region. Countries like Chile, Costa Rica, and Uruguay attain values that are close to those of high-income countries.

2. Throughout this report, statistics for North America include only the United States and Canada, while Mexico is included in Latin America

Graph 4
The World Bank's Control of Corruption Index



Note: This graph shows each country's percentile in the distribution of this index for 2017. A higher percentile shows more control of corruption. Bars on the right show average scores for countries in Latin America and the Caribbean, in North America, and in the European Union.

Source: Compiled by the authors, based on data from the Worldwide Governance Indicators (World Bank, 2018b).

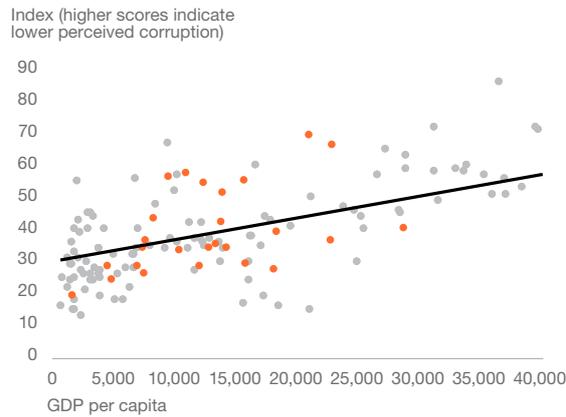
An obstacle on the path to development

An initial approximation to measure the costs of corruption is quantifying the amount of money involved in these transactions. In a recent document, the International Monetary Fund (IMF) calculated that about 1.5 to 2 trillion dollars—approximately 2% of global GDP—are lost in bribes each year (IMF, 2016). Globally, losses in the construction sector are estimated to be between 10 and 30% of total investment, meaning that close to 6 trillion dollars per year could be wasted by 2030 due to corruption and inefficiencies in project management (Matthews, 2016). In the Odebrecht case, the company admitted to having paid 788 million dollars in bribes to politicians and public officials in 12 countries, between 2001 and 2016 (United States Department of Justice, 2016). In Mexico, the National Institute of Statistics and Geography (*Instituto Nacional de Estadística y Geografía* - INEGI, 2018) estimated that close to 370 million dollars are paid in bribes by households in activities linked to administrative procedures, requests for public services, and other interactions with the authorities (this amounts to approximately 115 dollars per affected person). In Ecuador, Brugués, Brugués, and Giambra (2018) calculate that 475 million dollars a year (approximately 0.44% of GDP) are paid in overprices in government contracts largely to the favor of companies with political connections.

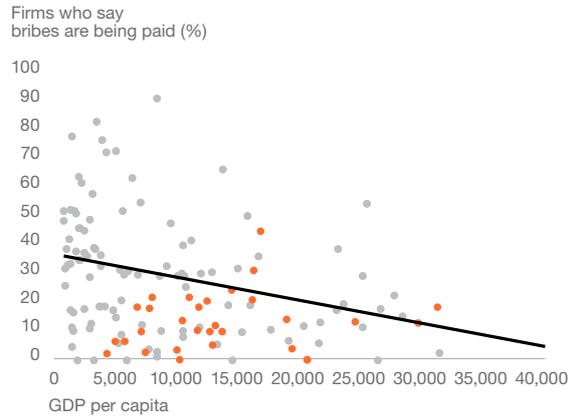
However, the costs of corruption go far beyond the money that changes hands in these operations. Its consequences involve welfare losses and reduced opportunities for development in the affected societies. Consistent with this concern, there is a strong correlation between GDP per capita and various measures of corruption, including Transparency International's Corruption Perceptions Index, the incidence of bribes paid by firms in the Enterprise Surveys Indicators, and the Control of Corruption Index in the Worldwide Governance Indicators (panels A, B and C in Graph 5, respectively).

Graph 5 Relationship between income and corruption

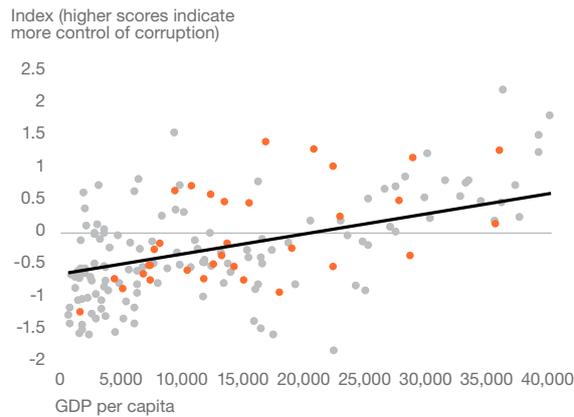
Panel A. Transparency International's Corruption Perceptions Index



Panel B. Perceptions of business executives about incidence of bribery



Panel C. Control of Corruption Index



Note: This graph shows the correlation between different measurements of corruption and GDP per capita (expressed in dollars and adjusted for PPP), for different countries. The following corruption measurements have been used: in panel A, the Corruption Perceptions Index for 2018, which ranges from 0 (higher perception) to 100 (lower perception); in panel B, the percentage of companies who say that bribes are being paid, according to the most recent data for each country (2009–2017) in the Enterprise Surveys Indicators; in panel C, the Control of Corruption Index for 2017, which ranges from -2.5 (less control) to 2.5 (more control). Each dot represents a country (countries in Latin America and the Caribbean are highlighted in orange), while the black line represents the linear regression between the two variables. This analysis is restricted to countries and territories with a GDP per capita (adjusted for PPP) of less than 40,000 dollars.

Source: Compiled by the authors, based on data from the Corruption Perceptions Index (Transparency International, 2018), the Worldwide Development Indicators (World Bank, 2018a), the Worldwide Governance Indicators (World Bank, 2018b), and the Enterprise Surveys Indicators (World Bank, 2019).

Corruption causes welfare losses through several specific channels. First, embezzlement reduces the quantity and quality of public goods and services in areas that include education, healthcare, and infrastructure. This can deepen socioeconomic inequalities, since it disproportionately affects the poor. In extreme cases, access to public services could require illegal payments that are relatively more expensive, or even unaffordable for lower-income households.

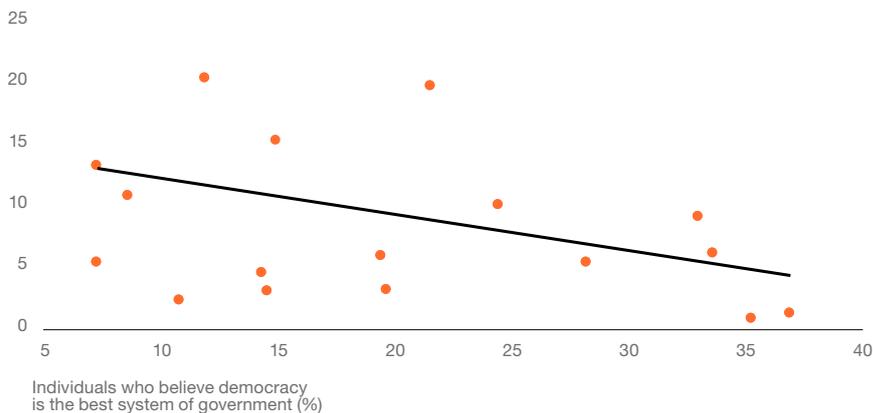
Corruption also lessens productivity and economic growth, by distorting resource allocation both within and between firms. Clientelism and low integrity in business cause aggregate investment to fall, especially in long-term projects. In line with this, when personal connections and influence peddling determine economic and regulatory policies, competition and innovation dwindle, and firms move their resources away from productive tasks and towards activities associated with rent extraction.

Finally, the most potentially damaging consequences of corruption are linked to a loss of confidence in public institutions and in the democratic system itself, which in turn paves the way for political and social instability. Graph 6 shows that, at an aggregate country level, there is a negative relationship between the perception of corruption by citizens and their belief in democracy as the best system of government. At a more disaggregated level, data obtained from the ECAF 2018 show that individuals who perceive more corruption in interactions between citizens and the state also report more distrust of political leaders (Graph 7).

Graph 6

Perception of corruption and confidence in democracy in Latin America

Individuals who believe corruption is the main problem (%)

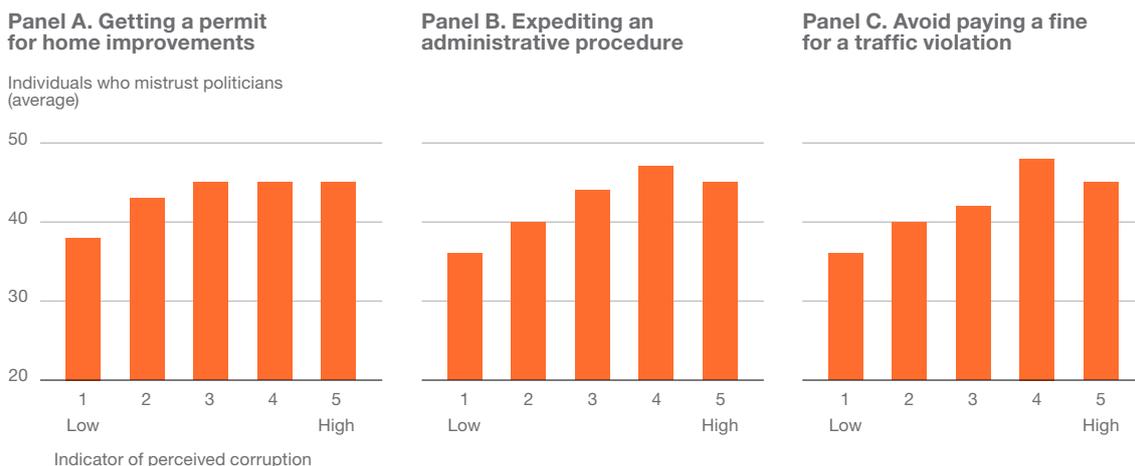


Note: This graph shows the correlation between the percentage of individuals who believe corruption is their country's main problem and the percentage who strongly agree that democracy is the best system of government, for Latin American countries. Each dot represents a country, while the black line represents the linear regression between the two variables.

Source: Compiled by the authors, based on data from Latinobarómetro (Corporación Latinobarómetro, 2017).

Graph 7

Perception of corruption in interactions with the State and distrust of politicians



Note: This graph shows the percentage of individuals who mistrust politicians, based on the level of perceived corruption in various interactions with the State. The level of perceived corruption is measured on a rising scale from 1 to 5, for each of the following interactions: getting a permit for home improvements (panel A), streamlining an administrative procedure (panel B), and avoid paying a fine for a traffic violation (panel C). These figures are a simple mean for the following Latin American cities: Buenos Aires, La Paz, São Paulo, Bogotá, Quito, Mexico City, Panama City, Lima, Caracas, and Montevideo. In this calculation, an individual is taken to mistrust politicians when they say that all or most politicians put their personal interests above citizens' interests.

Source: Compiled by the authors, based on data from ECAF 2018 (CAF, 2019).

Defining corruption

Throughout this document, we speak of integrity in public policy decisions when these are based on the goal of maximizing social welfare. Corruption is the opposite of integrity, since it involves abusing the powers of public office to secure private gains. This does not mean that acts of corruption are committed unilaterally by public officials. Indeed, these acts often involve private individuals and companies.

Finally, an abuse of public office does not always imply breaking a law or a formal rule, so it is important to avoid a narrow and legalistic interpretation of this issue. There are circumstances that bias the policy process in favor of vested interests but are hard to classify or prosecute as crimes. For example, social or family ties with businesspeople may affect the decisions made by public officials without an explicit exchange of favors. More generally, it may be very difficult to produce evidence of influence peddling when there is no illegal transaction of goods or money. Moreover, even when such transactions exist, uncovering them and linking them to decisions made by the relevant public official may be a very complex task.

This does not mean that legal instruments are useless to foster integrity. In fact, reviewing and adjusting legislation so that wrongful conducts are punished in court must be a priority. However, efforts to promote integrity in public policy need complementary measures aimed at aligning the incentives of public officials with the common good. Such measures include increasing political competition and meritocracy in

the recruitment of civil servants, simplifying administrative procedures, strengthening decision-making processes within the state, and improving corporate governance in both state-owned and private firms.

Investing in transparency policies is also essential, as is making the most of the options enabled by technology. Governments who digitize procedures and grant access to information that is relevant to fight corruption enable greater citizen oversight over state actions.³ This helps governments themselves, as well as auditors and prosecutors, to detect embezzlement and other misuses of public resources, and to produce the relevant evidence.

Structure and main messages of this report

Opportunities for corruption are inherent in the organization of modern societies. Society as a whole cannot directly execute the multiple tasks associated with procuring the common good. It therefore assigns those tasks to public officials—both politicians and civil servants—and grants them the privilege of making decisions on behalf of all citizens. The root of the problem is that these officials may have private interests that conflict with the public interest, and society cannot perfectly observe their actions—much less, their intentions.

This combination of factors causes an *agency problem*: a situation where a principal (in this case, citizens) hires an agent (a public official) to carry out a task, but finds it difficult to ensure that the principal acts as desired. There is a latent risk that the responsibilities attached to public service will be used to secure private gains: the risk of corruption. Societies seek to mitigate it through institutional arrangements aimed at solving the agency problem by constraining officials' decision-making within certain parameters.

This report analyzes how the behavior of agents responds to different institutional arrangements, with the intention of suggesting formulas that relieve the tension between collective and private interests and promote integrity in public policy decisions. Of course, there are many institutional arrangements that can affect corruption, and they take varied forms. To guide this discussion, they are grouped into four categories: rules and oversight of public officials; mechanisms for political selection and civil service recruitment; transparency and citizen control; and governance of private interests.

Rules and oversight of public officials

Public officials' privilege of making discretionary decisions is at the root of the risk of corruption. Indeed, more discretion increases the probability of irregularities. This relationship is apparent in many public policy contexts, like distributing resources among government agencies, purchasing products or services, hiring staff, and imparting justice. Two different types of arrangements can be used to counter this: *ex ante* rules to restrict public officials' scope of action (what decisions they may make, and how) and *ex post* oversight to audit these decisions and actions once they have been carried out.

In many contexts, applying decision rules based on protocols and objective criteria minimizes the risk of corruption. For example, in the context of procuring public infrastructure, it is better to use standardized evaluation formulas than to resort to subjective criteria. Reforms to Colombia's royalty distribution system,

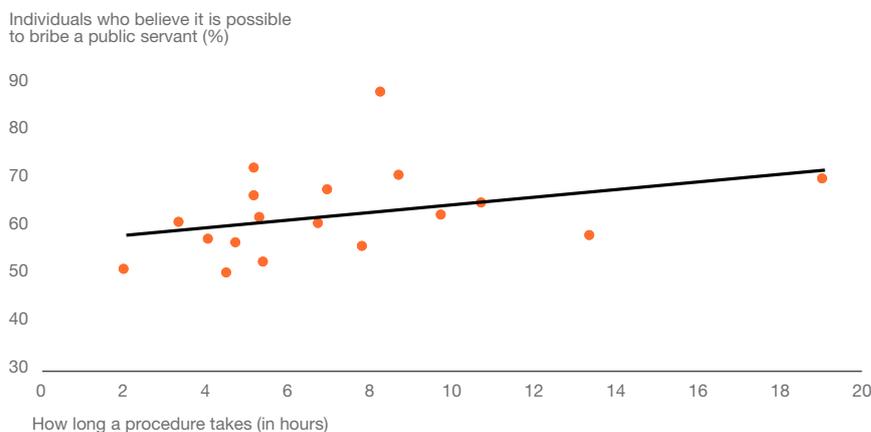
3. Among this information are public procurement and contracts, property and company registers, and disclosures of interests and asset declarations filed by public officials.

that imposed more strict regulations on the use of these funds by municipalities, seems to have diminished the incidence of irregularities in local governments.

Technology also makes it possible to reduce discretion in some contexts. Administrative procedures are one area where this is apparent. Efforts to simplify and digitize these procedures help to reduce the power that officials may hold on power citizens. As shown in Graph 8, individuals are more likely to perceive bribes as useful to secure benefits when procedures are slower. Thus, it is important for Latin American countries to step up their efforts to simplify and digitize administrative procedures.

Graph 8

Time taken to complete an administrative procedure and perceived corruption in Latin America



Note: This graph shows the correlation between the percentage of individuals who believe it is possible to bribe a public servant and the average time required to complete an administrative procedure in different Latin American countries. The indicator of perceived corruption is based on the question: "What are the chances of bribing someone at a ministry here to be able to obtain a contract?" ("¿Qué probabilidades hay aquí de poder sobornar a alguien en un Ministerio para poder conseguir un contrato?"). This considers administrative procedures at a State office over the previous 12 months, along with the indicator of perceived corruption. Each dot represents a country, while the black line represents the linear regression between the two variables.

Source: Compiled by the authors, based on data from Latinobarómetro (Corporación Latinobarómetro, 2017).

However, restricting the autonomy of public officials comes at a cost in terms of agility in public administration. The way public procurement systems work illustrates this point. These systems tend to require more open (i.e., less discretionary) processes as contract size exceeds certain thresholds. However, these rules could have negative consequences if they are not carefully designed. Public officials may find that more demanding procedures are too cumbersome and slow down their actions. Even without corrupt motivations, these officials may deliberately avoid these procedures by adjusting the amounts of money involved in a contract or using exceptional formulas in their procurement and hiring processes. The design of *ex ante* rules that restrict the actions of public officials is useful, but it needs to suit the context to ensure they are not too costly in terms of flexibility without actually achieving more integrity.

A more general conclusion is that restricting the autonomy of public officials must not be seen as an alternative to *ex post* audit systems. Strengthening the institutions tasked with detecting and punishing

irregularities must be a priority, can serve as deterrents. Many organizations, both public and private, have internal audit departments in charge of investigating misconducts, and their importance must be stressed. However, centralized audit agencies also have a major role to play in preventing irregularities. These institutions can only work well if they are credible, independent from political criteria, able to learn and adapt, and if there is a sustained commitment to these principles.

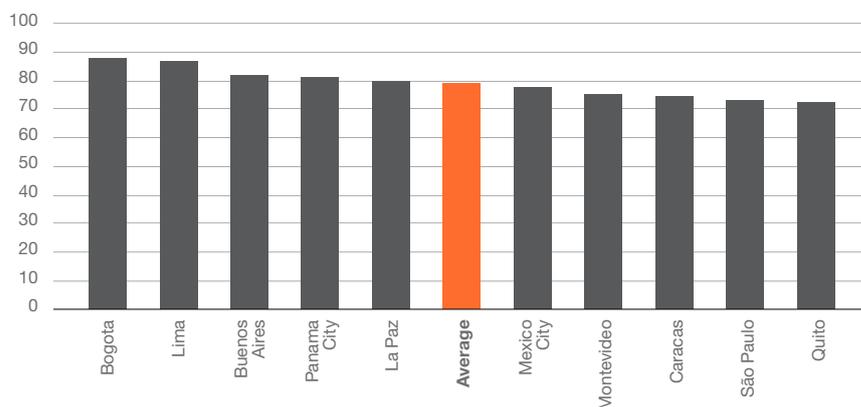
Financial and process oversight of government bodies by Supreme Audit Institutions have proved to be valuable tools for any integrity agenda. For example, some results of the Random Audit Program conducted by Brazil's Federal Comptroller General (*Controladoria Geral da União*, CGU) support this notion. To maximize the effectiveness of these agencies, it is important to be careful with some aspects of the design and implementation of audits. One essential point is that they lose their deterrent effects when they are either predictable or rare. The threat of being subjected to an audit must be constant, whether because audits are frequent or because they are unpredictable. Technology's potential to strengthen and improve efforts to monitor public officials' actions is another issue that needs to be taken into consideration. Digital records of government transactions, combined with data analysis techniques, can guide the actions of those with oversight duties.

It is especially important for audit agencies to have strong links to prosecutors and other agents in position to take administrative and legal actions against wrongdoers. Judicial punishment is crucial to discourage crimes of corruption, so that securing the correct functioning of the judicial system must be another priority in any integrity agenda. As shown in Graph 9, the majority of Latin Americans believe that the courts are not tough enough on corruption. A central goal must be strengthening the capacities of public prosecutors offices and other actors involved in the investigation of cases of corruption. These crimes are complex, so prosecuting them requires specialized technical teams with autonomous powers, and protocols for investigation and for the collection of evidence.

Graph 9

Perception of judicial punishment of corruption

Individuals who think it is punished less than necessary (%)



Note: This graph shows the percentage of respondents who believe that judges punish corruption less than they should. A percentage is calculated for each city, and then a simple mean for these cities.

Source: Compiled by the authors, based on data from ECAF 2018 (CAF, 2019).

As a complement to these investments, some reforms in substantive and procedural law may be helpful. In particular, the use of plea bargain to investigate corruption cases is a promising innovation that has delivered concrete results in recent years. However, this tool does entail some risks, and it is very important to build the institutions necessary to regulate its use. Among other things, it is fundamental to: define the conditions in which such agreements can be reached; carefully design the incentives (usually, sentence reductions) that are to be offered to suspects who cooperate; and specify the role of public prosecutors, judges, and other actors in this process.

Besides discouraging wrongful conduct through disciplinary measures, it is also important to gauge whether integrity can be promoted through compensation schemes and career incentives to public officials. Wages—and the prospects of a raise—are more relevant for civil servants than for politicians, because the former hold their positions for longer periods. Even so, higher salaries can only promote integrity in contexts where audit mechanisms work well and individuals face real risks of dismissal if they engage in irregularities. Compensation does not seem to have a first-order impact on integrity levels; its effect will depend on whether there are disciplinary mechanisms in place. Conversely, salaries are very relevant to attract capable individuals into public service.

Reelection is one career incentive that can indeed have greater impact on politicians' behavior. Some results suggest that the option of seeking reelection integrity, in their effort to remain popular and be able to run for another mandate. Still, entrenchment in power entails risks of its own, and term limits are necessary when the institutional context fails to provide effective checks and balances.

Mechanisms for political selection and civil service recruitment

The mechanisms to recruit public officials, whether elected office or appointed, are key in the fight against corruption. Transparent, meritocratic mechanisms favor the selection of individuals free from clientelistic ties, which makes them crucial to ensure the independence of office holders and an effective system of checks and balances.

Governments must aim to recruit capable individuals with a low tolerance for corruption. Motivating such people to work in the public sector is the first step to achieve that. The role of perceptions and expectations should not be underestimated in this context. Both the incidence and the perception of corruption impact how attractive the public sector is. This is why reforms to boost integrity need to be able to communicate achievements in that effort, in order to improve citizens' beliefs and expectations about the functioning of government.

Once individuals decide to seek a public office, there are recruitment mechanisms in place to determine who gets the positions from the pool of candidates. These mechanisms will differ greatly depending on whether it is an elected office or a civil-service job, and both need to be discussed separately.

Electoral systems are the gateway into elected office, and their goal should be to maximize plurality and competition. Evidence shows that politicians who perform best tend to come out of the elections that are tight and in which candidates' qualities are most clearly visible. Conversely, there is less accountability when a district is evidently dominated by one political group. Thus, competition must be encouraged in districts where it is lacking. Introducing competition within political parties can compensate for a lack of competition among parties, for which primary elections may be useful.

The regulation of political finance, particularly campaign funding, is a priority. Recent scandals have shown that campaign donations are often at the center of favor exchanges between politicians and

businesspeople. Moreover, large private donations may deepen inequalities in political representation and increase the influence of vested interests.

This is an active area of reform in Latin America, at least formally. Countries generally regulate the sources and amounts of political contribution, with approximately half of them banning corporate campaign donations entirely. Also, legislation usually caps spending and provides public funding for campaigns. There is evidence that certain specific campaign finance rules are useful. For example, imposing bans and caps on individual contributions can be effective to reduce the risk of political capture. Additionally, restricting the level of spending allowed in campaigns can encourage electoral competition, especially in contexts where candidates' personal wealth is a major factor for success at the polls.

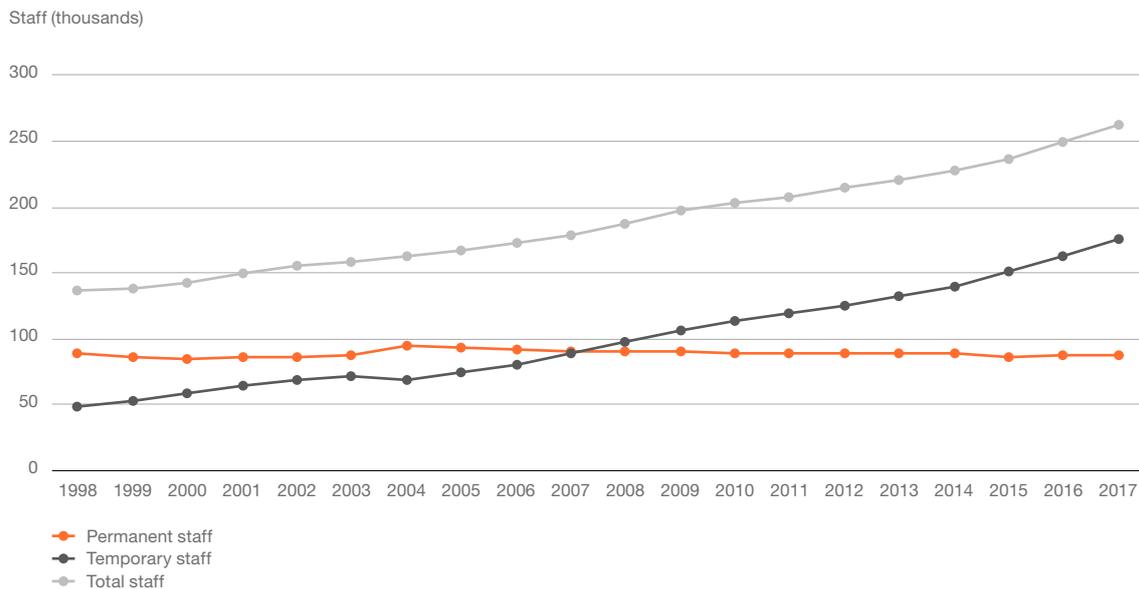
However, improving regulation on this issue requires above all closing the gap between regulatory frameworks and their implementation. It is crucial to strengthen the monitoring capacities of electoral courts and other supervision mechanisms, which tend to be rather weak in Latin America. Increasing the harshness and scope of punishment for campaign finance violations and promoting transparency and citizen oversight are also important. These are necessary steps to reduce irregular political funding, which hides conflicts of interests and seriously hampers accountability.

Mechanisms to access non-elected office in the public administration pose their own challenges. The clientelistic use of public-sector employment (patronage) can undermine efforts to attract and recruit better-quality civil servants, and it contributes to the institutional weakening that allows systemic corruption to thrive. Even though political leaders can enjoy some autonomy in the appointment of staff in some positions of trust within executive teams, this privilege must not extend to the whole civil service. Discretion to appoint and dismiss staff in the public administration often leads to patronage.

Merit must be the decisive factor for entry into the civil service. To ensure it is, impartial recruitment processes are required, with decisions based on candidate suitability and skills. The best way to achieve this involves public service exams, as long as these meet certain conditions. They must guarantee that the available vacancies and the selection procedures are adequately publicized, ensure broad access by potential candidates, and involve an evaluation system based on technical, objective, and transparent criteria.

Almost all Latin American countries hold public exams to fill permanent professional and operational positions in their civil services. However, there are still some challenges in this respect. In particular, the number of hires under conditions of exception and the use of fixed-term contracts, often the most frequent hiring method, must be reduced. Graph 10 shows that even in Chile, which stands out in Latin America for its institutional quality, the proportion of temporary staff has risen significantly over the past two decades. These schemes should be used only in cases where they are justified. One tool to accomplish this is to set limits on the use of fixed-term and exceptional hires, but even more important is to improve the working of regular recruitment channels (making it easier to hire staff through standard procedures), and to increase efficiency in the civil service. Additionally, the use of public exams should be promoted in areas of public-sector employment with less institutionalized recruitment processes: subnational governments, and education and healthcare services are typical cases.

Graph 10
Composition of civil service staff in Chile



Source: Compiled by the authors, based on data from Chilean Finance Ministry's Budget Department (Dirección de Presupuestos del Ministerio de Hacienda de Chile, 2008, 2018).

To implement these recommendations, it is recommended that the civil service regime is managed by an autonomous, technical body with the sufficient resources to perform its duties.

Transparency and citizen control

Intuitively, we tend to think of citizens as the final safeguard against corruption, as they bear the burden of any losses and inefficiencies caused by it. However, in order to exercise their oversight role efficiently, citizens need some inputs: information on the actions of public officials, the ability to recognize acts of corruption and react accordingly, and accessible channels to protest, complain and demand accountability. These requisites are not always met.

The most important ingredient to activate citizen control is information on the actions of the public administration. It is therefore natural to start off from the hypothesis that more transparency should lead to a lower risk of corruption. Calls to divulge information about the actions of the state and individuals officials to the public reflect this rationale. The first generation of these initiatives involved the enactment over the past two decades of freedom of information acts that forced governments to respond to citizens' requests (Figure 1). While Latin American countries have adopted regulations of this kind, there is still significant room for improvement concerning delays in the delivery of information and the level of correspondence between citizens' inquiries and the answers provided by agencies.

Figure 1
Freedom of information laws in Latin America



Note: Countries that are shown in gray are yet to implement freedom of information laws. Bolivia and Venezuela have enacted rules on some aspects in this area, while in Costa Rica this right rests on dispositions held in the country's constitution (Organization of American States 2013).

Source: Compiled by the authors, based on data from the Observatory on Principle 10 in Latin America and the Caribbean of the Economic Commission for Latin America and the Caribbean (ECLAC, 2018).

On the other hand, open government initiatives require that states play a more proactive role and provide information without citizens having to explicitly request it. The opening of data in formats that anyone can access is a central element of these initiatives. It is important to acknowledge that the complexity of the state apparatus, with multiple bodies and agencies that conduct many procedures and transactions, makes it difficult to provide clear, manageable information. This is why standards for the governance, production, interoperability, and communication concerning these data are essential.

The provision of open information by governments pursues multiple goals. The Open Data Charter identifies a few databases that are particularly valuable for accountability. These correspond to many of the issues that are highlighted in this report, including information concerning election campaigns, registers of companies and government contractors, records of public officials and interests, and the results of audits and legal proceedings.

For information to have a positive impact on accountability, it must be credible. Credibility will depend on the institutions who produce this information, but also on the agents who process and communicate it to citizens. NGOs and the media very often play that role and are therefore important. Governments should promote an environment that boosts these agents' credibility. Hence, it is important to protect freedom of the press and to promote high levels of coverage and competition in the media. NGOs should also ensure their funding is highly transparent, to dispel any doubts about conflicts of interests or corporatism in their activities.

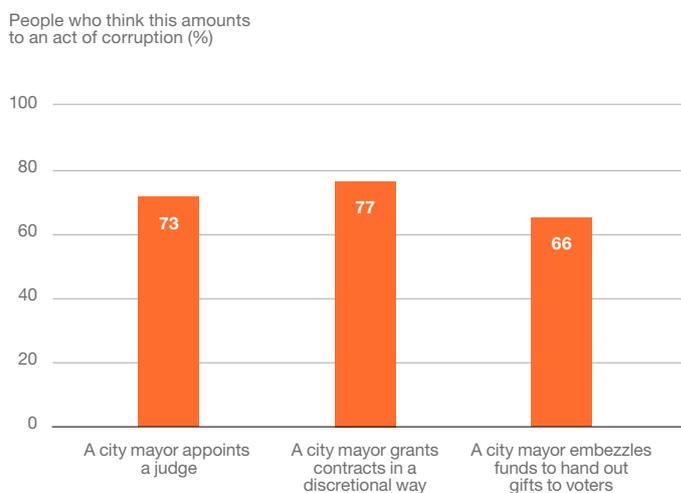
The ability of citizens to understand and use the information they receive is as important as the production and dissemination of such information. To punish acts of corruption, individuals first have to be able to identify them and to keep an intolerant attitude towards them. However, this is not always the case. ECAF 2018 data suggest that approximately one third of all individuals do not recognize situations that describe typical cases of corruption as such (Graph 11). Additionally, some circumstances seem to make people

more lenient on corruption, for example: perceived competence of the public official in question, political or ideological affinity, clientelistic relationships, or the prevalence of social standards that discourage issuing formal complaints.

Greater understanding of the problem and more firm attitudes towards it can only be attained with sustained investments through the formal educational system and other spaces of learning and transmission of values. Mass campaigns to educate citizens and raise awareness about the manifestations and consequences of corruption may be useful. In some contexts, successful behavioral interventions have been implemented using role models to encourage people to make formal reports of malfeasance, countering social norms that foster silence concerning irregularities.

Graph 11

Recognizing typical corruption scenarios



Note: This graph reports the percentage of respondents who think each of these situations involves an act of corruption. It shows a simple mean for the following Latin American cities: Buenos Aires, La Paz, São Paulo, Bogotá, Quito, Mexico City, Panama City, Lima, Caracas, and Montevideo.

Source: Compiled by the authors, based on data from ECAF 2018 (CAF, 2019).

Finally, citizens can only discipline public officials when they have access to adequate channels to do so. Elections play an essential role to aggregate collective preferences, but clientelistic practices reduce their legitimacy as an accountability mechanism. While vote-buying is hard to measure accurately, surveys suggest that it is widespread in Latin America. Combating vote-buying and other clientelistic practices requires addressing both the demand and the supply of these types of transactions. Reducing politicians' discretion in the allocation and provision of social programs and public services must be a priority. Social and economic vulnerability facilitates clientelism, and the provision of public services and benefits should not depend on arbitrary decisions by officials. Complementarily, it is important to increase awareness among voters about the value of independent voting, which can be promoted through informational interventions.

Elections need to be accompanied by other, more direct, mechanisms to channel citizen demands and complaints. However, the high costs associated with making formal reports of malfeasance and a generalized pessimism about their effectiveness lead to low level of active oversight by citizens. Governments should make the most of the opportunities that technology offers in this regard, such as the creation of platforms that allow individuals to report malfeasance and file complaints.

Beyond that, new formulas to involve the communities directly in the design and implementation of public projects and policies are being rehearsed. Community-based programs foster bottom-up monitoring of government actions and thus can improve accountability. They can be very valuable in specific cases, but they should not be seen as a substitute for traditional, top-down monitoring.

The governance of private interests

In many cases, members of the private sector play a very active role in corruption, by inciting an exchange of favors that erodes the integrity of public policies. There is abundant literature showing that company's revenue and stock value increase when they get preferential access to public-policy decision-makers. This means that a comprehensive anti-corruption agenda must include measures to promote integrity in the private sector and in its interactions with the public sector.

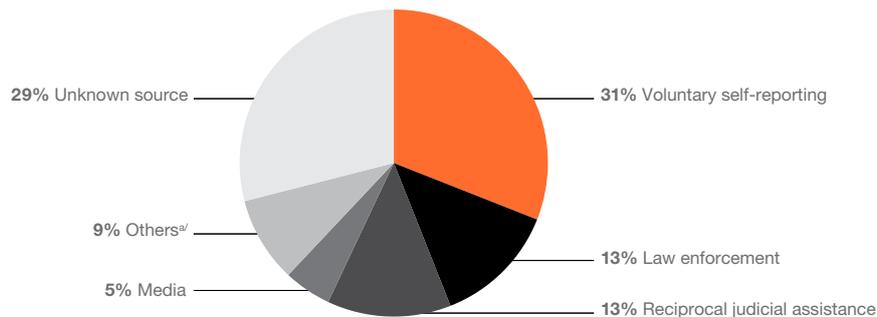
There are many mechanisms that private interests can use to coopt the public decision-making process. Bribery is probably the most obvious. Several international agreements urge states to strengthen their legal structures against bribery. Criminalizing active bribery must come coupled with provisions that make legal persons liable for acts of corruption, including the bribery of foreign public officials. Several Latin American countries have taken steps to adopt legal instruments that get them closer to these standards. However, recent data and scandals suggest that bribery continues to be a pressing issue in the region. This is why it is necessary to supplement legal reform with institutional investment to improve implementation. The starting point needs to involve recognizing that corruption crimes are complex, and that efforts to investigate them are difficult and time-consuming. Investments must focus on strengthening the capacities of investigative institutions, adjusting procedural mechanisms to make the task easier, and creating protocols for cooperation between jurisdictions.

One of the purposes of establishing a corporate criminal liability regime is to create incentives for companies to adopt internal compliance programs. The experience of implementing the United States Foreign Corrupt Practices Act (FCPA) and other regulations against international bribery shows that voluntary self-reporting by firms is one of the most frequent ways in which cases get to be known by the authorities. This is clear from Graph 12, based on data from the OECD Foreign Bribery Report. This further shows the value of the arrangements to detect irregularities within organizations. Compliance programs typically involve setting up internal channels for informants (whistleblowers), among other components. The promotion of whistleblowing is very valuable because an organization's employees are the people most likely to hear about any wrongful practices. However, the evidence shows that incentivizing these actions is difficult: the costs of being an informant are very high and may involve retaliation and even dismissal. Protocols on this matter need to be very carefully designed to prevent false or irrelevant allegations.

Beyond bribery, private interests entail other risks for integrity in public policy. Conflicts of interests emerge when public officials need to make decisions on issues on which they have vested interests that run counter to their public responsibilities. Such conflicts do not constitute acts of corruption in and of themselves, but they are a major risk factor that have to be addressed. The central elements for the governance of conflicts of interests involve banning certain private activities while holding public office, obligations to disclose interests and activities, and the design of mechanisms for resolution of conflicts.

Graph 12

Original source of information concerning cases of foreign bribery



Note: This graph refers to international embezzlement cases closed over the period 02/15/1999–06/01/2014.

a/ This category includes inside informants, international organizations, investigations into different crimes, financial intelligence units, and citizen complaints.

Source: Compiled by the authors, based on OECD (2015).

Regulations for the disclosure of private interests by public officials are crucial. Legislation must not only list items of information that officials have to provide, but also establish clear responsibilities and consequences in cases of non-compliance. Latin American countries have regulations in place on this issue, but several aspects of these instruments could be improved. First, greater emphasis should be put on the disclosure of additional activities and positions held by officials, even if these are not a current source of income. Second, regulations need to ensure more public access to the information that is provided, balancing the demand for transparency with considerations concerning the privacy of public officials.

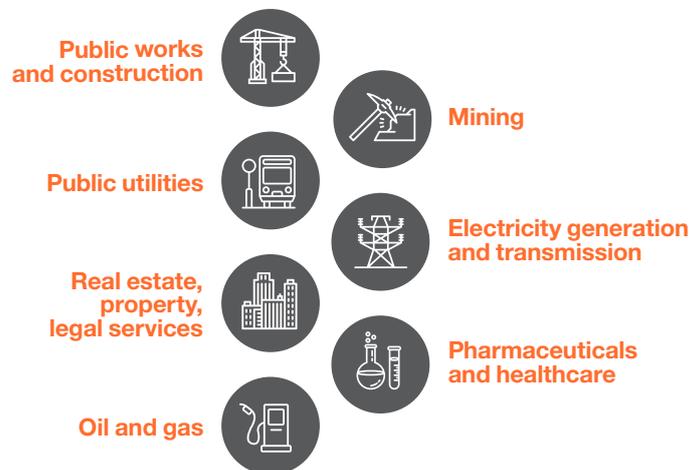
The mechanisms to resolve conflicts may include the possibilities of officials recusing themselves from situations with conflicts and the existence of formal procedures for relevant authorities to separate officials from those situations. However, a sufficiently comprehensive obligation to publicly disclose interests should discourage officials from acting in conflicting circumstances, due to reputational costs. Thus, priority should be given to institutional efforts to improve the declarations of interests and to punish officials who fail to comply with those obligations.

Lobbying is another strategy that the private sector uses to influence public policy. While it is legitimate for individuals and companies to communicate their views and preferences to their political representatives, there is a risk that those instances of interaction are used by well-organized, powerful groups to buy connections that grant them excessive influence over public decision-making processes. The rules on this matter must aim at regulating and fostering transparency in lobbying. Registering lobbyists and their interactions with public officials is fundamental, which should be complemented with the publication of comprehensive information about these officials' decisions and actions in the exercise of their office. At the same time, efforts need to be made to improve access to decision-makers by less powerful, less organized groups. This is a difficult challenge, but addressing it is necessary to ensure a fairer representation within political systems.

Finally, it is important to acknowledge that some of the tasks carried out by the public sector imply allocating significant resources between private firms, and those activities are particularly vulnerable to the risk of capture. This explains why certain forms of malfeasance are more prevalent in specific industries. Figure 2 shows the list of industries with the highest perceived corruption among business executives, according to Transparency International's 2011 Bribe Payers Index (Hardoon and Heinrich, 2011).

Figure 2

Industries most vulnerable to rent-seeking



Note: This illustration shows the seven industries with the worst results in Transparency International's 2011 Bribe Payers Index.

Source: Compiled by the authors, based on Hardoon and Heinrich (2011).

Natural resource management and the provision of infrastructure are two vulnerable tasks of particular relevance in Latin America, so it is crucial to strengthen decision-making processes in these areas. State-owned firms tend to play a major role in performing those tasks, so boosting governance within these organizations is a further priority.

The procurement of public works requires careful design and oversight throughout the whole project cycle. First, it is important for officials or agencies in charge of different tasks (project formulation, adjudication decision, supervision and auditing, contract renegotiations) to be independent from each other. Standardized documents can be useful to prevent processes tailored to favor specific companies. Solid capacities need to be developed in procuring institutions, to prevent inadequate contracts that trigger costly renegotiations. Amendments to contracts are very common in public infrastructure projects, which facilitates corruption. This stage requires particular care, and clear rules should be set to assess amendments and to ensure that clear information on any and all renegotiations is made public in a way that allows to track the entire evolution of a project. This is relevant for projects granted both under traditional public contracting models and as public-private partnerships (PPP).

Regarding natural resource management, the processes for granting licenses to private operators entail similar risks to the procurement of public works. And besides that, a second source of concern is that revenue generated through extractive industries may erode accountability. The Extractive Industries Transparency Initiative (EITI) makes a series of valuable recommendations to improve governance based on transparency about processes and outcomes. The emphasis should be in reporting and publishing any information concerning the flow of resources in these industries: cash inflows and outflows of operators, public-sector agencies, and state-owned firms involved; transfers to special funds and subnational governments, and so on. These efforts to increase transparency should be complemented with very clear rules on the use and final destination of those resources.

Governments must make a special effort to encourage high standards of integrity in state-owned enterprises. The risks of malfeasance in these organizations generally stem from flaws in the governance models they adopt. States should institutionalize the way in which it exercises its property rights, chooses its representatives to serve on corporate boards, and implements oversight protocols. This can be done through a single ownership entity or through a coordinating agency that manages property rights over all companies where the state holds stock. A further priority in this area involves ensuring autonomy in the management of these companies and preventing that political concerns interfere with their operational and commercial interests. Through its representatives on corporate boards, the state must communicate goals and expectations on the performance of firms, without interfering with their daily management.

The political economy of reforms

There is one essential question beyond identifying what reforms need to be implemented to control corruption: How can political and institutional processes that favor an effective implementation of these reforms be launched?

The reform processes needed in a society depend on its starting point in terms of institutional development and the manifestations of corruption that take place in that society. In general, Latin American countries have moderately functional democracies, in which popular demand affects policy, but where coordination problems make it difficult for citizens to achieve organized action and demand structural reforms in terms of integrity.

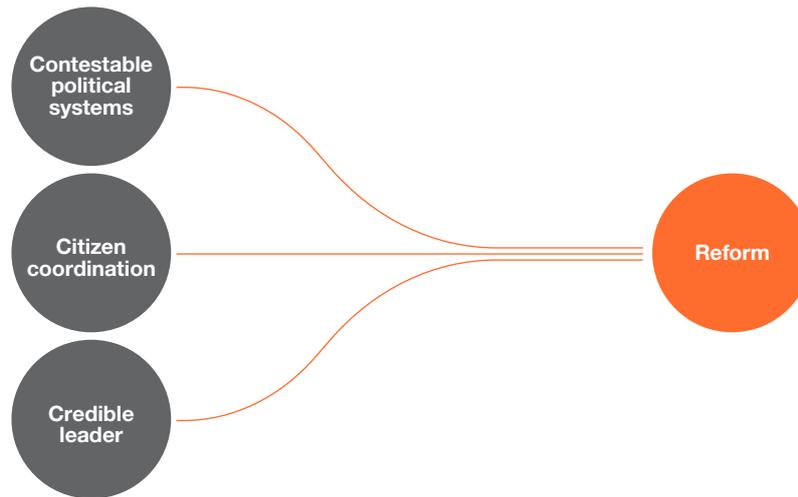
The hurdles to coordination are due to various factors, including lack of information, prioritization of other issues, and high costs of participation and mobilization. Additionally, politicians and citizens often build clientelistic relationships that may be mutually beneficial for those involved, at least in the short term, but which reduce accountability and tend to be self-perpetuating.

The basic elements required for change

While it is difficult to develop a complete theory of reform, we can identify the necessary conditions to implement it: a contestable political system (that is, one where individuals who hold power face a real threat of being replaced), sustained citizen coordination focused on an integrity agenda, and a leader in charge of effecting the reform (Figure 3).

Figure 3

Basic ingredients for reform to promote integrity



Source: Compiled by the authors.

Competitive political systems encourage governments to adopt reforms that promote transparency and integrity for various reasons: gaining popular support, preemptively restricting rivals' actions in case they get to power, or even imposing restrictions on potential competitors that occupy other offices. For example, regional or national governments may introduce changes that restrict the ability of local governments to benefit from clientelistic relationships. This is important, because the level of political contestability can vary significantly among regions and levels of government within a given country. Systems that are highly competitive at the national or state level may coexist with highly coopted political institutions, with little competition and significant clientelism, at the local level.

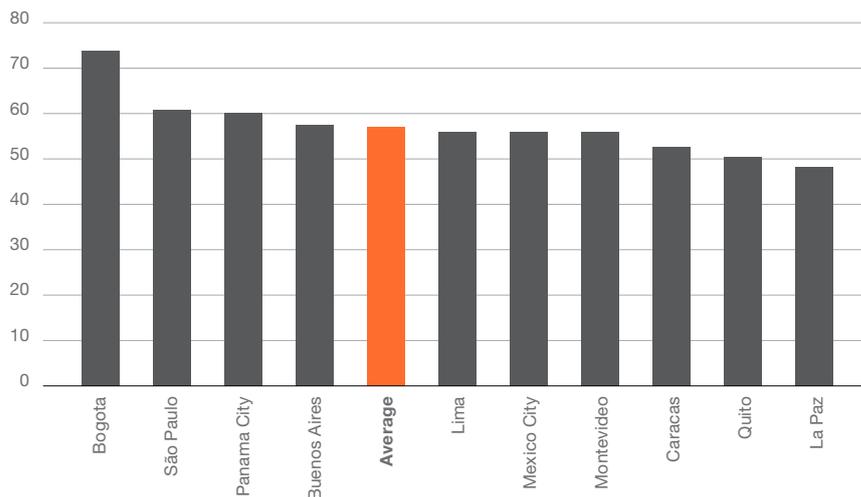
The second ingredient involves citizen coordination. Citizens' demand for integrity faces several obstacles, even at the individual scale. Indeed, many people believe that others don't do much to fight corruption. Data from ECAF 2018 suggest that, in surveyed cities, an average of 57% of respondents believe that their fellow citizens punish corruption less than they should (Graph 13). A central issue is that corruption is not the only aspect people consider when they act politically, and it may not even be the most important issue they consider. This is particularly noticeable when high levels of economic and social vulnerability impose other priorities on the population and facilitate clientelistic mechanisms that reduce accountability.

Collective demand for more integrity can be boosted through a gradual shift in preferences and attitudes. However, exactly what factors may produce such changes remains uncertain. The link between socioeconomic vulnerability and patronage prompts the hypothesis that economic growth and the consolidation of a large middle class will lead citizens to demand more accountability. There is also evidence that the contents of educational curricula have a lasting impact on people's civic values, so educational systems can be an important pathway to change attitudes toward corruption.

Graph 13

Perception of fellow citizens' concern about corruption

Individuals who think other citizens are less concerned than they should be (%)



Note: This graph shows the percentage of respondents who believe that other citizens are less concerned about corruption than they should be. A percentage is calculated for each city, and then a simple mean for these cities.

Source: Compiled by the authors, based on data from ECAF 2018 (CAF, 2019).

Collective demand can also be coordinated in the wake of major scandals that place corruption on a country's public agenda. This is how windows of opportunity for reform emerge, encouraged by popular pressure in reaction to scandals. Of course, these windows of opportunity close as soon as popular discontent subsides, so reform requires quick action. An important challenge involves managing the temporary coordination produced by these cases, so that citizen interest on this issue can last longer. Such episodes have arisen in several Latin American countries throughout the year, and they have been used to effect change with varying degrees of success.

Finally, the role of leaders to implement the reforms is crucial. Legitimacy is the single most important quality for individuals and groups in leadership positions. Their background and formal positions may vary depending on the context. For example, the role can be played by political entrepreneurs who build platforms around policies for integrity; or by outsiders to the political stage: NGOs, experts, and academics may be central, if there is widespread perception of their objectivity and excellence. In any case, political action will always be necessary to pass legislation and regulations. Therefore, if outsiders to the political system lead the effort, they need to build a symbiotic relationship with committed public officials. If the commitment of officeholders is not strong, reforms are most likely to fail. NGOs can also play a valuable role in the effort to monitor and disseminate progress concerning this agenda.

Other catalysts for reform

Some factors that are exogenous to the institutional quality of a country may help to accelerate the process of adopting and implementing reforms. International cooperation stands out among them. Through it, efforts can be coordinated, shared legal and regulatory standards can be agreed upon and implemented, and countries can learn from practices that have been tested elsewhere.

Integration into international markets can also be an important catalyst to promote competition and to push firms to strengthen their corporate governance practices, as they become subject to legislation in multiple countries. This increased institutional strength might also be transmitted along value chains.

Finally, it is important to highlight the disruptive role of technology. Tools to produce, open, and process data provide many opportunities. Technological applications enable improvements in resource management, communication, and intragovernmental monitoring, and they provide new channels to disseminate information both within governments and to citizens. Political entrepreneurs can make the most of this potential to push for an open-government agenda that promotes transparency and participation.

How can this transition be managed?

Sustained efforts are crucial to achieve effective reform. Legal changes take long, institutional capacity-building takes longer, and transforming social norms and expectations is an even slower process. This means that it may take a while for new reforms to lead to more definitive behavioral changes.

When new rules are launched in a context with historically high levels of corruption, there are adjustment costs in the short-term, which manifest in several ways. For example, public opinion may interpret the rise in the number of cases that are detected and punished as an increase in the level of corruption, and sanctions on firms may slow down activity in certain industries. This should not lead to less rigorous efforts to detect and punish malfeasance, since such efforts are needed to build up the credibility to make the new rules deterrent in the longer term. However, these adjustment costs do need to be taken into consideration. During a transition from a situation with loose regulations to one with tighter rules, governments must balance two goals: maximizing the deterrent effect of punishment and minimizing destruction of value in the short term.

In Latin America, one of the concerns that have emerged from investigations in the case known as Operation Car Wash (*Operação Lava Jato*) is that excluding suppliers from the market has brought to a halt ongoing public construction projects and made it more difficult to launch new ones. Although doubts persist about whether this case is evidence of structural institutional change in the region, but it nevertheless exposes a relevant problem: how to deal with the disruptive effects of increased enforcement against corruption.

Paralysis in the construction sector may be exacerbated by the lack of options available for states to react to malfeasance in contracts they have signed. Legal frameworks in the region usually stipulate that an act of corruption immediately triggers the contract to be rendered null and void. This generally entails that the contract between the government and the contractor, and all other contractual relationships derived from that agreement, become invalid, without pre-specified mechanisms to facilitate the continuity of the project, or the participation of actors who were not involved in illicit behavior. Thus, the threat of this happening creates major uncertainty for all actors considering getting involved in these projects, even if they are not directly associated with acts of corruption.

Public-private partnerships are particularly affected by this, because they have complex financial structures, bring together many stakeholders (including shareholders, financiers, construction firms,

operators, insurance companies, and suppliers), and involve long-term investments (typically recouped in 15–20 years) that are backed by income flows produced by the projects themselves after completion (through toll charges, fees, availability payments by the government, and so on).

In this context, the aim of balancing exemplary punishment with the need to preserve the continuity of public works demands the development of legal and administrative instruments that enable institutions to handle corruption cases in more flexible ways, rather than simply declaring them null and void. Some countries, such as Colombia and Peru, have launched initiatives of this kind, through legislative changes that seek to ensure that sanctions are imposed on firms who engage in illegal activities, while at the same time creating channels to enable construction activities to continue under actors who were not involved in wrongdoing.

It is still early to assess the results, but these measures represent concrete attempts to manage some of the short-term effects of enforcing legislation against corruption. In any case, the central question is whether Latin American countries are actually moving toward the adoption of stronger institutions, and this question remains shrouded in uncertainty. The answer will depend on whether countries in the region can sustain the reforms that have been launched and consolidate their implementation over time.

Bibliography

Brugués, F., Brugués, J., and Giambra, S. (2018). *Political connections and misallocation of procurement contracts: Evidence from Ecuador* [CAF – Working Document No 2018/20]. Retrieved from <http://scioteca.caf.com/handle/123456789/1394>

CAF (2019). *ECAF 2018: Percepciones y actitudes de los latinoamericanos ante la corrupción* [Database]. Retrieved from <http://scioteca.caf.com/handle/123456789/1468>

Corporación Latinobarómetro (2017). *Latinobarómetro 2017* [Database]. Retrieved from <http://www.latinobarometro.org/latContents.jsp>

Dirección de Presupuestos del Ministerio de Hacienda de Chile (2008). *Estadísticas de Recursos Humanos del Sector Público 1998–2007* (Informe Estadístico de Recursos Humanos 2008). Retrieved from http://www.dipres.gob.cl/598/articles-41362_doc_pdf.pdf

Dirección de Presupuestos del Ministerio de Hacienda de Chile (2018). *Estadísticas de Recursos Humanos del Sector Público 2008–2017* (Informe Estadístico de Recursos Humanos 2018). Retrieved from http://www.dipres.gob.cl/598/articles-176466_doc_pdf.pdf

Hardoon, D., and Heinrich, F. (2011). *Bribe Payers Index 2011*. Berlin: Transparency International.

IMF (2016). *Corruption: Costs and Mitigating Strategies* (Staff Discussion Note No 16/05). Retrieved from <http://www.imf.org/external/pubs/ft/sdn/2016/sdn1605.pdf>

INEGI (2018). *Resultados de la Encuesta Nacional de Calidad e Impacto Gubernamental 2017* (Comunicado de prensa No 136/18). Retrieved from https://www.inegi.org.mx/contenidos/saladeprensa/boletines/2018/EstSegPub/encig2018_03.pdf

Matthews, P. (2016). *This is why construction is so corrupt*. Retrieved August 22, 2019, from <https://www.weforum.org/agenda/2016/02/why-is-the-construction-industry-so-corrupt-and-what-can-we-do-about-it/>

Observatory on Principle 10 in Latin America and the Caribbean of the of the Economic Commission for Latin America and the Caribbean (ECLAC) (2018). *Latin America and the Caribbean: Countries with freedom of information laws*. Retrieved November 26, 2019, from <https://observatoriop10.cepal.org/en/resources/countries-freedom-infomation-laws-2017-latin-america-and-caribbean>

OECD (2015). *OECD Foreign Bribery Report: An Analysis of the Crime of Bribery of Foreign Public Officials*. Retrieved from https://www.oecd-ilibrary.org/governance/oecd-foreign-bribery-report_9789264226616-en

Transparency International (2018). *Corruption Perceptions Index 2018* [Database]. Retrieved from <https://www.transparency.org/cpi2018>

United States Department of Justice (2016). *Information: United States of America v. Odebrecht S.A.* Retrieved from <https://www.justice.gov/opa/press-release/file/919911/download>

World Bank (2018a). *World Development Indicators* [Database]. Retrieved December 10, 2018, from <https://datacatalog.worldbank.org/dataset/world-development-indicators>

World Bank (2018b). Worldwide Governance Indicators [Database]. Retrieved December 10, 2018, from <https://datacatalog.worldbank.org/dataset/worldwide-governance-indicators>

World Bank (2019). *Enterprise Surveys Indicators* [Database]. Retrieved from <http://www.enterprisesurveys.org/>

Report on Economic Development 2019
Integrity in public policy: Keys to prevent corruption

The Report on Economic Development (RED), CAF's flagship report, is published by the Vice Presidency of Knowledge for Development. Pablo Sanguinetti and Gustavo Fajardo edited the 2019 Report, with Eduardo Engel and Claudio Ferraz as academic advisors.

Chapters and authors of the full report:

Chapter 1 Progress in the integrity agenda - Gustavo Fajardo and Pablo Sanguinetti

Chapter 2 Autonomy without impunity - Juan Vargas

Chapter 3 Choosing the best - Pablo Brassiolo and Ricardo Estrada

Chapter 4 Transparency and citizen control - Lucila Berniell and Dolores de la Mata

Chapter 5 Keeping private interests in check - Gustavo Fajardo

Corruption has been one of the main concerns of Latin Americans for some time now. This is hardly a surprise, considering the significant negative effects that corruption has on development. It affects the productivity and economic growth of countries, it reduces the capacity of the State to provide public goods and services, and it can weaken society's trust in institutions.

Recent scandals have led to a resurgence of the issue, and currently the fight against corruption is a central point of public debate in Latin America.

With this report, CAF contributes to the ongoing reform agenda in order to promote integrity in public policies. The study covers different areas of action, including the functioning of control and oversight instances within the state; the importance of electoral and civil service systems to attract independent and honest public officials; the role of transparency initiatives and citizen control; and the strengthening of institutional and legal frameworks to limit the influence of private interests in public policy decisions.