NOTE V. THE ROLE OF THE FUND IN GOVERNANCE AND CORRUPTION: VIEWS OF COUNTRY AUTHORITIES[1]

1. **Country authorities were invited to share their views regarding the Fund's anti-corruption efforts since the adoption of the 1997 Guidance Note (Guidance Note)**, including the overall appropriateness of the Fund's corruption efforts, the links between corruption and macroeconomic impact, the relative engagement under surveillance and programs, the treatment in the context of technical assistance, the evenhandedness of Fund engagement, and collaboration with other institutions in this area. Only about 20 percent (38 out of 189) of the membership provided substantive responses.[2] While the group is not representative of the Fund membership as a whole,[3] a number of interesting and valuable perspectives can be derived from their responses. Therefore, this note provides an overview of those perspectives without treating them as reflecting a cross-section of the membership.

Overall Approach of the Fund on Corruption

2. **In general, country authorities recognize and value the Fund's engagement on corruption issues.** While most respondents were favorably impressed with how the Fund had been addressing corruption and agreed that the Fund's global vantage point provides it with unique perspectives on how corruption impacts macroeconomic outcomes, a significant group felt that the Fund's efforts had been insufficient in one way or another. No respondent called for a retrenchment of Fund efforts in this area and several specifically welcomed the reinvigorated focus manifested by the current work program.

3. **Respondents who were generally satisfied with the Fund's work on corruption emphasized the Fund's comparative advantages.** They noted that the Fund has a broad membership that allows for a cross-country perspective and is uniquely positioned to evaluate how corruption impacts sustainable growth, poverty, and income inequality levels, issues that affect macroeconomic stability. They also emphasized that the Fund's work on corruption is supported by its more broader work in promoting good governance and felt that these issues are fully integrated into Fund mainstream activities—through surveillance, UFR, and capacity development (e.g., fiscal

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[2] The respondents were Albania, Belarus, Belgium, Burkina Faso, Canada, Chile, Congo, Czech Republic, Dominican Republic, Ecuador, Estonia, France, Germany, Hungary, Italy, Japan, Kosovo, Lebanon, Libya, Madagascar, Malta, Mauritania, Netherlands, Norway, Panama, Peru, Philippines, Poland, Portugal, Russia, San Marino, Saudi Arabia, Senegal, Singapore, Switzerland, United Arab Emirates, United Kingdom and United States.

[3] Specifically, 32 percent of respondents were from advanced economies and 51 percent were from the EUR region.

transparency evaluations, AML/CFT, enhancing independence of institutions, statistics and transparency, single treasury accounts, and subsidy reforms)**.**

4. **Respondents who felt that the Fund's efforts on corruption were insufficient noted a tendency for the coverage to be infrequent, indirect, broad, brief, passive or marginal to reports, particularly in surveillance**. Some found that the coverage was sometimes rather general or indirect, even in countries where corruption is recognized to be widespread. A few considered that the Fund's focus on preventive aspects has become less prominent and consistent after the global financial crisis due to reprioritization of the Fund's attention and resources. Others felt that the discussions tended to proceed without relying on analytics on the source of corruption or being forthcoming about policies that could reduce it.

5. **A number of respondents also commented on the scope of the Fund's engagement.** They underlined the importance of limiting Fund engagement to the economic aspects of governance and corruption and that the Fund's judgment should not be influenced by the nature of the political regime. Others emphasized that the Fund should not interfere in the politics of members.

Macroeconomic Impact

6. **Respondents considered that the macroeconomic impact test is not always clearly applied and is difficult to measure in the short and medium term.** There was general recognition that the test is not easy to apply, and many felt that clearer operational guidance for staff was warranted. Given these uncertainties, less than half of countries believed that the standard has been appropriately applied. This group generally considered that macroeconomic performance was not properly defined in the 1997 Guidance Note and that proper tools to measure it have not been developed.

7. **As examples of appropriate engagement based on macro-economic impact, respondents cited:** Ukraine's energy sector, Cyprus' bankruptcy regulation and non-performing loans, Malawi's "cashgate" episode, Afghanistan's Kabul Bank fraud, and the suspension of the Democratic Republic of the Congo's (DRC) ECF arrangement in 2012 over opacity of contracts in the mining sector and of Mozambique's SCF arrangement over the misreporting of government guaranteed debt

8. **Other respondents cited examples where corruption was either not addressed despite its macroeconomic consequences or was raised without attention to macroeconomic analysis**. Some argued that corruption was only discussed when there was a major change in political leadership, or only in cases of grand corruption related to public officials, without being consistent in lower profile cases. Among the examples cited were: the lack of transparent statistics in Greece; public sector wages and ghost workers in Ghana; disappearance of large amounts of petroleum revenues accruing to the national oil company in Angola.

Time Horizon

9. Country authorities were asked whether they felt the current short- to medium-term (generally up to 5 year) time horizon was adequate to assess the macro-economic impact of corruption or the effectiveness of anti-corruption measures.

10. A little over half of those responding to this question generally agreed with the current timeframe. The short- to medium-term time frame was seen as helping to focus attention on areas of corruption where the impact was most imminent. It was also viewed as appropriately aligned with the time horizon of Fund-supported programs.

11. A slightly smaller group saw scope for extending the analytical time frame, at least in some circumstances. They argued that such period does not take into consideration the length of the legislative process for the introduction of anti-corruption measures and the duration of the subsequent implementation phase that require building proper institutions and governance mechanisms, transformation of existing behavior and values, and achieving concrete results and outcomes (e.g., convictions, asset recovery). Some considered that the time horizon should take into account the specific needs and level of income of the country (e.g., fragile states or low income countries might require more time to build capacity).

Programs and Surveillance

12. While acknowledging that there is room for improvement, most respondents were generally supportive of how the Fund has addressed corruption issues in the program context. Several respondents referred positively to situations where the Fund suspended program disbursements because of corruption concerns. Financial assistance has been delayed or suspended in several programs because of corruption and poor governance (e.g., Ukraine, Malawi, DRC, Mozambique), or because of the safeguards assessment exercise on central banks. A number noted that corruption tends to receive more attention in program countries than in surveillance and believed this to be warranted. Moreover, they viewed program conditionality as providing more leverage for Fund involvement. However, a few wondered whether the need to convey confidence in a program could sometimes lead to understatement on corruption and other governance problems.

13. Regarding surveillance, most respondents saw scope for more robust engagement. They considered that there is modest coverage of corruption issues under surveillance compared to programs. Some indicated that there is hardly any discussion of corruption under Article IV consultations in advanced economies even where corruption was known to exist. Accordingly, they felt that more attention is required in surveillance, including with greater follow-up on recommendations and advice. Some underscored how the Article IV consultation provides a unique platform for engagement that should be more effectively mobilized to address corruption and governance issues. A few saw the possibility of augmenting Article IV consultations with other tools (including diagnostic) that could address longer-term, structural corruption issues. However, a few saw no major differences between surveillance and programs, and others actually found that questions of macroeconomic implications were sometimes covered better in surveillance.

Capacity Development (CD)

14. Country authorities were divided on the value of the Fund's CD work for addressing corruption.

15. About half of country respondents cited Fund CD work as playing a very helpful role in addressing corruption-related issues. Many respondents noted the positive impact that CD products and deliverables (e.g., in the areas of tax administration, social security, fiscal transparency, ROSCs, AML/CFT, improving the independence of central banks, ministry of finance, and sovereign wealth funds) can have on reducing the scope for corruption, notably by helping to frame policy advice and conditionality on issues of Fund expertise. Some argued that CD work is a good way to identify structural issues before pressing ahead with required policy measures.

16. The other half seemed to place more emphasis on the limitations of the impact of Fund CD on corruption directly. The limitations cited include the voluntary nature of the CD relationship and the perceived attendant limited traction of CD recommendations, the lack of Fund expertise and skills on corruption issues, and the lack of Board access to CD reports. A few suggested that the Fund should consider developing a methodology for assessing the anti-corruption frameworks of its members as a possible CD product.

Perception of Evenhandedness

17. Countries saw scope to improving evenhandedness although many emphasized that evenhandedness does not mean equal treatment. Accordingly, it was important to avoid a one-size-fits all approach or an inflexible trigger for engagement. This could be achieved by taking into account individual country circumstances, political and economic contexts, and the differing capacities of members.

18. Two-thirds of those responding on this topic saw shortcomings in the evenhandedness of the Fund's engagement on corruption. Some saw the Fund focusing mostly on grand corruption scandals rather than routine corruption; highly visible or egregious instances of corruption tended to receive more Fund attention. Others saw the Fund as failing to engage sufficiently forcefully in countries where corruption was a major concern, or to adequately address cross-border corruption issues, or corruption issues typical to emerging market and advanced economies, such as regulatory capture. Several countries noted that perceived lack of evenhandedness could adversely affect the Fund's traction on corruption issues. Some raised the question of whether over-reliance on perception-based indices (which can be driven by media reports, rather than actual events) could account for lapses of evenhandedness and whether "idiosyncratic factors (such mission team leaders and mission team composition)" could account for perceived uneven treatment.

19. Authorities cited several specific situations which they felt indicted a lack of evenhandedness, including the following: (i) lack of discussion of corruption in advanced economies, under surveillance and FSAPs. For instance, regulatory capture in some advanced economies was not discussed; (ii) CIS countries, especially Central Asian countries were treated more harshly compared to other members; (iii) Angola, where corruption was only mentioned in the context of AML/CFT, de-risking and business climate—not with regard to broader, more pervasive government corruption; (iv) Laos, where despite a high-level corruption case in 2015, staff did not directly mention corruption in the 2016 Article IV staff report. It was noted that, even though government corruption looms large in Laos, staff have not mentioned the issue in the past five Article IV staff reports; (v) Ghana, where the Fund has recently seemed unwilling to properly engage on corruption, though there are major issues involving, for example, reform of the public-sector wage bill and ghost workers that would be suited to Fund engagement; and (vi) Kenya, where staff make no mention of corruption in recent program documents or included in program conditionality.

Use of Third-Party Indicators

20. Country authorities noted the challenges of using third-party indicators. In this regard, some respondents emphasized the need for caution in regard to subjective measures of corruption perceptions and the need for robustness checks, given changes in methodologies for some indicators. Notwithstanding these challenges, some countries saw the existing use of third-party indicators as broadly appropriate, while a somewhat larger group of countries favored expanded use, informed by more regular staff discussions with the World Bank and other sources (such as Transparency International). Only a few country respondents appeared to support the Fund developing its own corruption indicators.

Collaboration with Other Institutions

21. Country authorities emphasized the importance of collaboration with external counterparts. Respondents were divided on how well they felt that this collaboration had functioned in the past, but there was a broad consensus in favor of it being strengthened in the future. While about half of respondents considered that existing collaboration with other organizations is adequate, a significant group saw scope for strengthened collaboration. The latter saw scope for using external expertise (for example, on the nature of corruption and its political context), while maintaining the Fund's focus on the macroeconomic aspects of corruption. A few cited specific examples (Ukraine, Malawi, Madagascar) where they thought such collaboration had taken place in an effective manner. Some explicitly motivated their support for further collaboration by suggesting that Fund staff lacked expertise on corruption issues.

Other Issues

22. Some respondents provided useful views on the impediments to a fruitful discussion related to corruption, and on how to make Fund engagement more effective in the future.

These included the following views and recommendations:

- The Fund's discussions of corruption and setting of anti-corruption reform objectives should take place within a rigorous understanding of the political context of the country, how political power is exercised and how corruption fits in to the political settlement of the country. The Fund is a hugely important external actor, and can have significant influence over the investment climate in a country and the government's willingness to drive reforms, particularly where Fund lending is involved. However, government ownership, and genuine internalization, of reforms will always remain critical to the likelihood of implementation, so the Fund needs to find ways of determining whether governments and agencies are committed to reform, and if not, how best to influence their thinking. The Fund should seek to work with those within country authorities who have the willingness, the mandate and the political cover to drive reforms, and reforms should be designed in such a way as to incentivize and strengthen such reformers.

- Since the 2007 Global Financial Crisis, the Fund has enhanced its surveillance mandate to financial issues (G20 mandatory FSAPs, macro-financial works). The Fund engagement on financial stability and integrity issue should be maintained and enhanced. In this regard, it is key to provide adequate attention and resources on governance and corruption practices in the financial industry.

- It is not clear why the Fund seems to single out corruption and overlook a broad range of other governance issues. For example, institutional shortcomings in many advanced economies and the inappropriately powerful role of financial institutions and their lobbying activities led to the dangerous weakening of regulation and supervision and had profound damaging effect on many economies. New policies should be advocated to close these gaps.

- In relation to LICs, the Fund should continue engaging on PFM, support national audit offices, develop ex-ante fiscal horizon testing, increase FTEs, discuss macro risks of off budget expenditures and liabilities under Article IV, have more long-term resident experts, and develop further analytical work on the cost of corruption and impact on growth.

- The Fund should discuss the effects of informal economies, illicit trade, and the role of financial institutions in relation to AML/CFT.