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Can Private Sector Action Tackle Corruption?

Corruption is an impediment to growth and poverty reduction. As the authors in this issue of *Development Outreach* well document, corruption limits opportunities, creates inefficiencies and forms additional barriers to the smooth delivery of services. Crucially, from the perspective of the World Bank Group, corruption cumulatively undermines progress towards achieving development objectives, not least as its impact is most adversely felt by the world's poor. The World Bank has taken a clear public stance—based on exhaustive research—to seek ways to combat corruption. To this end we do and must work together with other international organizations, governments, civil society groups, and the private sector. As noted by World Bank President Paul Wolfowitz, the private sector worldwide is one of the most important partners in this process and, without the active engagement of business, progress will be limited.1 Business action is already showing the potential for sustainable results in limiting opportunities for corruption, but a core theme of this publication is that such potential is best realized by being integrated with the efforts of other stakeholders in the form of collective action.

Why should business care?

"Corruption not only undermines the ability of governments to function properly, it also stifles the growth of the private sector. We hear it from investors, domestic and foreign, investors who worry that where corruption is rampant, contracts are unenforceable, competition is skewed, and the costs of doing business becomes stifling. When investors see that, they take their money somewhere else." – *Paul Wolfowitz, World Bank President, Jakarta, Indonesia, April 11, 2006*

A lot is at stake for the private sector. It is becoming increasingly obvious that the private sector has a critical role to play, alongside more traditional government and civil society actors, in fighting corruption. But why should business care? Continuing to participate in, or turning a blind eye to, corrupt activities can have significant negative consequences for the private sector in terms of competitiveness, the ease of doing business and the sustainability of development efforts. As Peter Brew notes in his article in this issue on "The Power of Joining Forces," corruption is estimated to add 10 percent or more to the costs of doing business in many parts of the world. Corruption also renders

effective, which in turn produces negative knock-on impact on the business environment.

Corruption affects everyone and exists all over the world—in developed and developing country contexts—and can greatly hinder firm, national and regional-level competitiveness, as well as significantly affect the attractiveness of investment climates. According to Batra, Geeta, Kaufmann and Stone,[2] the level of corruption is identified as a serious constraint to doing business by over 70 percent of firms in South Asia and almost as many in East Asia and in the Middle East and Northern Africa regions. Sixty-four percent of firms in Africa, almost 60 percent of those in Latin America, and about half in the Commonwealth of Independent States (CIS) and Central and Eastern Europe regions report corruption to be a serious impediment to private sector development.

Capacity of government to regulate is key. The private sector is recognizing that it is in its own best interest to fight corruption to foster sustainable and stable business growth. Global business leaders are more publicly supportive of increased regulation to limit corruption and to ensure a level playing field. However, as commonly reiterated by fellow authors in this issue, treaties, conventions and codes are only as effective as their enforcement. Therefore a careful assessment is needed of the capacity of government and international agencies to enforce, or private sector bodies to self-regulate, these agreements, as well as the capacity of the range of companies (in size and ownership structure) to implement procedures to reduce corruption. Multinational businesses typically have the resources to train and monitor internally, but local firms, including down to the level of small and medium enterprises, will often require assistance to develop workable controls.

So, What Is Being Done?

A range of actions are underway. Recent experiences show that effective and consistent private sector efforts can be effective in combating corruption. Actions can be at the level of an individual firm, through the collective action of business associations, and as a result of work across entire industries.

Action by individual firms. The articles by Mohamed Ibrahim of Celtel International and Glenn Ware of Diligence LLC outline what individual firms can and are currently doing to fight and avoid corruption, for example by instituting and enforcing tighter ethical codes combined with training for employees on how to manage typical situations where pressures arise to participate in corruption. However, corruption is hard for one firm to eradicate on its own—and if a firm does attempt to uphold strict standards, it can have all too real negative consequences in terms of lost business. Some large companies may have the resources to absorb this loss or find ingenious, but typically more expensive, ways to supply the promised goods and service, but, for most companies, this is not an option and they subsequently feel trapped into accepting corruption.

Collective action and the role of associations. This suggests the importance of taking anti-corruption initiatives to a more collective action level. This endeavor can be private sector-led, for example by business associations, who can act as cheerleaders for policy reform, develop and provide access to training tools and codes relevant to their members, as well as utilize their clout that comes with representing a broader swathe of business. Leading private sector institutions, such as the International Chamber of Commerce (ICC), have a potentially important role to play in this regard, as do counterpart national chambers of commerce and business associations at the country level. They can provide guidelines for member companies, but also utilize their outreach skills and typically high level access to decision makers to be positive agents for reform, linking with other sectors. There is great value in linking business with government and civil society to find more comprehensive solutions, as Peter Brew points out in his article using the example of the China Business Leaders Forum anti-corruption initiative. Other examples include the Center for International Private Enterprise (CIPE) country-level anti-corruption initiatives, and Transparency International's national integrity pacts, in which companies, together with government and civil society, voluntarily implement anti-bribery agreements that are monitored by an external party.

Industry-wide efforts also hold promise. Effective change must also be pursued at the industry

level and through global governance channels. Industry specific initiatives among businesses and other stakeholders have proven to be an effective method of tackling corruption as they impact local business practices beyond the capacity of any single company. The Extractive Industries Transparency Initiative (EITI) and the Forest Law and Enforcement and Governance (FLEG) initiative are just two examples of recent ground-breaking initiatives, both supported by the World Bank and International Finance Corporation, that have brought multiple stakeholders together to collectively address corruption within a particular industry sector. In further signs of this trend, we have also seen significant business and NGO investment in ensuring good practice in specific industry segments, such as the Kimberley Process for diamond production and the code now under development for gold mining.

Global standards can be effective at producing peer pressure to reform. In terms of fostering global governance, efforts to bring together government, business and civil society in dialogue around anti-corruption initiatives have proliferated, not least through efforts to identify appropriate global standards. The OECD Convention on Combating Bribery of Foreign Public Officials continues to gain traction and has been supplemented by the UN Convention Against Corruption Treaty. As Georg Kell discusses in this issue, in 2004, the UN Global Compact added a tenth principle to its list of principles stating that "Businesses should work against all forms of corruption, including extortion and bribery."[3] Signatories commit to mainstream these principles into business activities worldwide.

The World Bank's Contribution

Leadership in international efforts to combat corruption. To help foster both industry and global initiatives to combat corruption, the World Bank Group works closely with international anti-corruption organizations and networks, including the Partnership for Transparency Fund, Financial Action Task Force, the Public Expenditure and Financial Accountability program, and OECD-Development Assistance Committee Network on Good Governance and Capacity Development. Active participation in such international efforts illustrates how the Bank has progressed rapidly from taking an ad hoc, low-visibility approach towards instances of fraud and corruption in member countries, Bank-financed projects, and among staff, to assuming a clear leadership role among multilateral institutions in all three areas.

Increased attention to its own loan portfolio. The growing attention the Bank pays to anti-corruption work, and, more broadly, to public sector governance and institutional reform, is reflected by changes in its loan portfolio. In the 1995 fiscal year, only 0.6 percent of Bank lending went to support public expenditure, fiscal management, and procurement reforms. As of the end of June, 2005, it had climbed to 4.6 percent. In the 2005 fiscal year, almost half of the new Bank projects had at least one component addressing governance, public sector or rule of law issues. The proportion of new projects with accountability/anti-corruption components jumped from 0.4 percent in the 1995-96 fiscal years to an average of five percent in the 2004-05 fiscal years. Within its overall loan portfolio and operations, the Bank recognizes that it has no magic immunity to corruption. Therefore anti-corruption initiatives related to its own lending portfolio are very effectively spearheaded by the Bank's Department of Institutional Integrity with the strong backing of senior management.

The power of data and benchmarking. The International Finance Corporation plays a proactive and innovative role in partnership with its private sector clients in improving effective long term corporate governance through mechanisms such as the Equator Principles and through development and application of measurement tools such as the *Doing Business* indicators. Many countries and businesses worldwide have found the data encapsulated in the *Doing Business* surveys to be critical in benchmarking their performance, not least on good governance.

Embedding governance and anti-corruption at the heart of country strategy. Increased Bank financing for good governance components contributes to the core objective of supporting anti-corruption efforts at the country level. To help meet this goal, the Bank now requires that all Country Assistance Strategies (CAS) address governance issues. In some of the higher risk countries, governance and anti-corruption have become central planks of the

In support, the World Bank Institute (WBI), with the benefit of fifty years of experience in capacity development, facilitates action-oriented and participatory programs to promote good governance and limit corruption at the country level. Deliveries, in collaboration with World Bank Operations and often in partnership with international organizations, are targeted to around thirty countries—principally in Sub-Saharan Africa, Latin America, Eastern and Central Europe, and more recently, Asia.

Powerful diagnosis and analytical tools help guide actions at the country level. These efforts are supported by rigorous empirical diagnostics and analysis. WBI publishes data and analyses assessing many dimensions of governance for 209 countries and territories which are used extensively to raise awareness nationally and globally and to help inform policy reform. These indicators, which are constructed on the basis of hundreds of variables, measure voice and accountability, political stability and absence of major violence and terror, government effectiveness, regulatory quality, rule of law, and control of corruption.

Affecting both the demand and supply side of good governance. WBI utilizes such data and analysis to build momentum for change. The complexity and pervasive nature of the corruption problem pushes a capacity development approach that moves beyond conventional training to knowledge dissemination, policy advice based on the latest research and operational findings, and participatory and consensus-building activities. It is not enough to look at the symptoms of corruption. Instead we must look for new tools that will help tackle supply and demand. Individual efforts, although necessary, are not sufficient, and the fight against corruption needs to be taken to the next level.[4] As highlighted throughout this publication, the challenge is to work with the range of stakeholders in society, not least the private sector, and to maintain an open approach that strengthens individual stakeholder actions, but also recognizes the potential value of collective action through bottom-up coalitions for reform.

The Challenge of Forging Effective Collective Action

"…fighting corruption requires a long-term strategy that systematically and progressively attacks the problem, and that is why any strategy for solving the problem requires the commitment and participation of governments, private citizens, and private businesses alike." —*Paul Wolfowitz, World Bank President, Jakarta, Indonesia, April 11, 2006*

Collective action is potentially an integral part of the solution, but is not a panacea. As outlined above, the Bank, along with other development actors, is reviewing approaches to combat corruption to improve efficacy. However, scaleable impact will also require engagement from government and civil society. So, are collective multi-stakeholder approaches the most viable? On paper the logic is clear —corrupt activities, and the corrupting influences that generate them, permeate all sectors of society, often rendering unilateral solutions to fighting and reducing corruption inappropriate or ineffective in the long-term. Yet, there is still a need for caution. The range of projects reviewed in this issue suggests there are emerging best practices and lessons to be learned, but there is not yet a systematic operationalization of concrete multi-stakeholder governance and anti-corruption strategies.

Multi-stakeholder partnerships are a complex and nuanced undertaking. To date, existing documentation of collective action and multi-stakeholder partnership anti-corruption initiatives is largely anecdotal. As Roderick Hills points out in his article, the void created by a lack of empirical research makes such initiatives difficult to replicate, scale-up, monitor and evaluate over time. Furthermore, factors such as the level of political engagement and the transparency of the business environment, as well as the capacity of individual stakeholders to engage in partnerships, can all impact any initiative's effectiveness and long-term sustainability. Understanding business environment indicators, as Michael Klein points out based on the findings of the World Bank Doing Business surveys, are indicative of specific economic and social outcomes, among them levels of productivity, informality, and corruption in a particular country.[5] It is important to study these factors and to carefully build capacity locally and across stakeholders before considering and engaging in collective action initiatives. WBI is committed to doing exactly this through its learning programs that support the

efforts of the private sector and other stakeholders, individually- and in partnership, to fight corruption and render development efforts more effective.

In This Issue

This issue of *Development Outreach* specifically considers the role that the private sector can play in the fight against corruption. Georg Kell stresses the importance of the individual responsibility of the private sector through the expansion and deepening of corporate citizenship and corporate governance on a global scale. In order to affect this principles-based organizational change across organizations, institutions and supply chains, Kell argues, all actors in society must be involved in promoting organizational change, providing necessary tools and training, and supporting action campaigns against corruption. Following on this message, Peter Brew argues the case for collective business action in fighting corruption, examining the pros and cons of business-led versus multi-stakeholder initiatives and providing a concise list of the elements necessary for effective collective business action. William Laufer, however, cautions against the immediate inclination to jump on the collective action bandwagon, stressing the necessity of assessing the situation thoroughly before adopting a multi-stakeholder partnership solution.

The overall success of reducing corruption depends on two forces working in parallel: government's own efforts and the response of the private sector. Roderick Hills continues with a call for business–led collective action among academia, government and the private sector to effectively identify corrupting influences and to deal with corruption. To this end, Glenn Ware points out that, while governments take steps to strengthen their own anti-corruption requirements, the private sector is a critical stakeholder throughout this process as it decides if and how to respond to increasing mandatory and voluntary regulatory pressure.

Implementation of anti-corruption measures is possible even in difficult environments. The next two articles concentrate on anti-corruption experiences at the implementation level. Mohamed Ibrahim of Celtel International outlines in detail how an African company has dealt with corruption, while operating in often corrupt and corrupting environments. Kebour Ghenna provides a civil society perspective from Ethiopia, focusing on private-private corruption. Ghenna argues that, to be truly effective, ethics must play an integral part in organizational culture, which requires the mobilization and strengthening of the civil society sector to undertake regular monitoring, enhance public awareness and encourage widespread private sector commitment and support. The article by Dani Kaufmann, Aart Kraay and Massimo Mastruzzi focuses on specific myths and realities related to the measure-ment of corruption and helps set the context for assessing the private sector's role in corruption, as well as its impact in fighting it, rendering the private sector more of an "investment climate maker" than an "investment climate taker." Kaufmann et.al. emphasize the value of empirical research in problem diagnosis and the monitoring of results. However, as the article points out, there is still much debate on how best to go about these activities.

Dialogue can be a powerful tool for change. The department Voices from the Field features two conference summaries: "Research on Corruption and Its Control," by Moana M. Erickson, and "Seeking Clarity in A World of Murky Transactions." The latter covers a global high-level e-discussion, "Towards a More Systematic Fight against Corruption: The Role of the Private Sector," organized jointly by WBI, the UN Global Compact and Zicklin Center for Business Ethics Research at the Wharton School of Business from June 26 to July 7, 2006. The impressive level of participation in the e-discussion, as well as the depth and breadth of the discussion itself, reinforces the importance of information sharing. Of equal importance is remaining open to new and innovative ideas on how to combat corruption, while maintaining a level of flexibility knowing that corrupt actors will also adapt to new anti-corruption strategies. Corruption is a multi-headed beast that will not be slain easily.

Frannie Léautier is Vice President of the World Bank Institute.
Djordjija Petkoski is Head of the Business, Competitiveness and Development Team, World Bank Institute.
Michael Jarvis is Consultant, Finance and Private Sector, World Bank Institute.

Endnotes

1 Wolfowitz, Paul, World Bank President, Jakarta, Indonesia, April 11, 2006

2 Batra, Geeta, Daniel Kaufmann and Andrew H. W. Stone, "The Firms Speak: What the World Business Environment Survey Tells Us about Constraints on the Private Sector Development," in *Voices of the Firm 2000: Investment Climate and Governance Findings of the World Business Environment Survey*, World Bank Group, 2002.

3 http://www.unglobalcompact.org/AboutTheGC TheTen Principles/index.html

4 Kaufmann, Daniel, "Myths and Realities of Governance and Corruption" in Schwab, Klaus and Michael Porter, *The Global Competitiveness Report 2005-2006*, World Economic Forum, 2006. According to Daniel Kaufmann, Director of Global Programs at the World Bank Institute, the way forward is not "fighting corruption by fighting corruption" (i.e. launching another anti-corruption initiative, introducing more anti-corruption commissions or implementing new codes of conducts).

5 Klein, Michael, *Doing Business in 2005: Removing Obstacles to Growth*, World Bank, 2005. The Bank is a leader in the development and application of governance diagnosis, from the *Doing Business* report to *Investment Climate Assessments* to indicators that assess six dimensions of governance in more than 200 countries. These indicators are used extensively to raise awareness nationally and globally and help to support policy reform.

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