

**CORRUPTION  
IN POLAND:**

**REVIEW OF PRIORITY AREAS  
AND  
PROPOSALS FOR ACTION**

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## ACRONYMS

APA	Agricultural Property Agency
ARMA	Agency for Restructuring and Modernization of Agriculture
ARR	Agriculture Marketing Agency
CBOS	Center for Public Opinion Research
CEFTA	Central European Free Trade Association
EFTA	European Free Trade Association
EU	European Union
GDP	Gross Domestic Product
ID	Identification
IMF	International Monetary Fund
IT	Information Technology
KRUS	Farmers' Social Security Fund
NFOS	Environment Protection Fund
NGO	Non Government Organization
NIK	Supreme Audit Chamber
OECD	Organization for Economic Cooperation and Development
PFRON	Fund for the Rehabilitation of the Disabled
PLN	Polish New Złoty
PPO	Public Procurement Office
SOEs	State-owned enterprises
WDR	World Development Report
ZUS	Social Insurance Organization

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## **METHODOLOGY**

Corruption is a difficult area in which to gain reliable information: police statistics are likely to show only the tip of the iceberg, given that corruption differs from most offences in that neither party to a corrupt transaction normally has an incentive to reveal it. Surveys of the population are useful in that they can reveal detailed and systematic evidence of experience and perceptions of corruption, as well as amounts, frequency and “reliability” of bribes (they are, however, somewhat less likely to yield robust results in areas where the public does not have direct information). This report builds on surveys of corruption in Poland that have been carried out by reliable survey houses over a number of years, the Ministry of Interior report on corruption in April 1999 to the Parliamentary Internal Affairs Committee, reports of the Supreme Chamber of Audit, published books and articles, newspaper reports, and individual focused interviews with Parliamentarians, government officials, people in the judiciary and business sector, academics and NGOs. We were struck by the high degree of corroboration among those interviewed on both the type and gravity of corruption problems. However, we have not had the opportunity to discuss the report with all of the organizations referred to, and some of our findings are highly sensitive and could be challenged by those who feel criticized or implicitly accused. It should therefore be understood that this initial scan of corruption rests on the material listed above and on the view of informed observers. Comparisons of the regulatory environment and corruption between Poland and other countries in Annex 3 are based on the multinational surveys of the private sector carried out in preparation for the 1997 World Development Report on the Changing Role of the State. We hope the report and proposal for action will provide a starting point for deeper analysis and discussion and for a broad-based and widely supported program to reduce corruption in Poland.

## **ACKNOWLEDGEMENTS**

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# **CORRUPTION IN POLAND: REVIEW OF PRIORITY AREAS AND PROPOSALS FOR ACTION**

## **I INTRODUCTION**

1. This report was prepared by the World Bank (Warsaw Office) in response to a request from the Government of Poland to help identify the areas in which the most serious corruption problems are found and those in which measures to reduce corruption are likely to be most productive. The report aims to provide a scan of areas susceptible to corruption and an initial identification of priorities that will assist Poland in moving towards an effective anti-corruption strategy and program. The final chapter outlines proposals for next steps.

### **Definition**

2. For operational purposes, the World Bank defines corruption **as the abuse of public office for private gain**. While this definition does not include wholly private sector corruption, it does include the interface between private and public sectors without which much private sector corruption could not occur. Some examples:

#### *Bribery*

- Purchasing government contracts, benefits, licenses, and judicial decisions
- Evading customs duties, taxes and other regulations

#### *Theft*

- Misappropriating budgetary funds and public assets

#### *Patronage*

- Nepotism, cronyism

#### *Influence peddling*

- Election or party financing in exchange for influence.

### **World Bank approach**

3. Corruption is not likely ever to be fully eliminated, but the objective is to minimize it, so that it becomes an exception and not the rule, by turning it from a low risk and high return activity into a high risk and low return activity. The Bank's approach therefore focuses on an economic analysis of the conditions conducive to corruption based on rents, discretion and accountability. Corruption is a function of all three. Corruption has the potential to flourish where rents<sup>1</sup> are high, discretion extensive, and reporting and monitoring are poor.

4. In combating corruption, it is useful to focus on minimizing the extent to which these factors can influence behavior, rather than relying solely on prosecution of corrupt individuals. Prosecuting the guilty is important but can do little to reduce the

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<sup>1</sup> In this context, rents means the cash or other benefits to be gained by exploiting a position of control in the allocation of resources, licenses, jobs, or other advantages.

opportunities and incentives for corruption “upstream”. To do this, it will be necessary to focus on rents, discretion and the efficiency of monitoring and accountability mechanisms in the political, administrative and other structures of the state. At the same time, it is important to ask why there have not been more successful prosecutions of corruption in Poland. This highlights the importance of including judicial, prosecutorial and police bodies among the State organizations to be scrutinized. The analysis based on high potential rents, extensive discretion, and low transparency is also relevant to them.

### **Costs of corruption**

5. Corruption undercuts the macroeconomic, efficiency, equity and institutional functions of government. It is helpful to distinguish these four types of costs imposed by corruption:

- Macro-fiscal: lost revenues (from tax, customs duty and privatization) and excessively high expenditure (e.g. through corruption loadings on state contracts);
- Reduction in productive investment and growth e.g. through abuse of regulatory powers, misprocurements and other costs imposed by corruption. International evidence indicates that countries with a higher incidence of corruption systematically have lower investment and growth rates, and that public safety can be compromised by unsafe infrastructure;
- Costs to the public and to the poor in particular: via higher taxes than necessary, bribe-extraction in delivery of services, and poor quality of and access to services. Bribes are frequently a higher proportion of the income of the poor even though they do not pay the highest bribes;
- Loss of confidence in public institutions: corruption can undermine the rule of law, tax compliance, respect for contracts, civil order and safety, and ultimately the legitimacy of the state itself.

### **Formulating a strategy and action program**

6. Analysis of corruption according to the size and type of cost involved can help shape priorities for action, as will the costs and feasibility of appropriate solutions. In all but trivial cases, the efficiency and budget costs of corruption are so great that the benefit/cost ratio of reducing it is positive. But cost factors are unlikely to be the only consideration. In creating a strategy, the availability of committed leaders, the ability to demonstrate results, and involvement of the public will also be important. These themes are further discussed in the final chapter.

## **II THE POLISH CONTEXT**

7. Corruption is a general phenomenon – it can be found in most places at most times. Yet its features are also specific to the time and place. According to cross-national research, corruption in the transition economies including the former Soviet Union is worse than in any other region of the world; corruption in Central and Eastern Europe is

among the worst<sup>2</sup>. The nature of the corruption suffered by transition economies, and the difficulty of finding robust solutions, are closely linked to their history and to specific institutional features of the transition.

### **Features of the transition to a market economy**

8. Poland, like other transition countries, is emerging from a system in which legislative, executive, judicial and enforcement power was centralized, and was also combined with control of the economy. Corruption was rife and transparency low, and negative attitudes to the state were widespread. Vulnerability to corruption is particularly great in the transition period, because the former coercive power of the state has been relaxed, and the formal and informal institutions that controlled and organized corruption in the past are in decline or have been eliminated. Meanwhile new institutions to underpin the new democratic politics, the market economy and the rule of law have not yet been created or are in their infancy. This institutional hiatus creates abundant opportunities for corruption. Part of the transformation required is constitutional and legal, and has to do with the effective separation of powers and the creation of a new transparent governance framework to define and control the exercise of these powers. It must be complemented by a transformation of the organizations of the state: the judiciary, prosecutorial and enforcement services, the regulatory bodies, and the public administration. The probity of these structures – and the extent to which corruption can be minimized - is closely related to the efficiency, transparency, and accountability arrangements of these organizations.

9. A successful transition also requires a human transformation. It is therefore worth taking a brief historical look at the attitudes and experience of the great majority of people in Poland. Under the German occupation and then under the Communist regime, a majority of citizens regarded the state as alien and therefore fair game, while a substantial participating minority saw the state as “theirs” and thus something they were entitled to exploit. For those on the “outside”, loyalty was owed to family, church and informal networks: little or no moral disapproval attached to individuals who cheated or stole from the State or from their places of work, given the perception that the State had stolen their country, a far larger crime. For those on the “inside”, communist ideology, party hegemony and the institutional organization of the state all provided both opportunity and justification of the abuse of public office and trust.

10. Hostility to, and the exploitation of public office by, the officials of an alien State goes back far further than the last 50 years, however. Over many centuries, Poland endured a history of partition and occupation by foreign powers, sometimes brutally coercive. This experience has left a legacy of perceptions of the state as belonging to others, of the state as predator. It has fostered resistance to, and distrust of, the State among the population. And this history has offered few - if any - models for a trustworthy and competent state. In the light of this history, it is perhaps understandable that there were some instances, especially early in the transition, of support for an extreme libertarian view that the State should be minimized and that any behavior that was not

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<sup>2</sup> Brunetti, Kisunko and Weder, cited in the World Development Report: The State in a Changing World, chapter 1, p35, published for the World Bank by Oxford University Press, 1997.

explicitly forbidden was permissible. Such attitudes have made it all the harder to recognize the importance of creating a strong and credible state and to develop a climate of civic responsibility and ethics.

11. It is correspondingly problematic to establish a new state in which the population can reasonably have confidence. But it is worth noting that the inter-war state has the reputation of having been more competent and transparent than the post-Communist state, and that standards of ethical behavior within Parliament and the administration were reportedly better at the beginning of the 1990s than they are now<sup>3</sup>. These contrasts indicate that it is worth analyzing the factors that, historically, have helped to produce resistance to corruption, as well as those that now undermine this resistance. Chapter III elaborates on the problem areas and possible solutions while Chapter IV deals with reform of the public sector as a whole.

12. At the same time, it should be recognized that, overall, Poland has made tremendous progress towards full constitutional separation of powers and the development of new institutions. The country is seen as a leader in Central and Eastern Europe and is in the front rank for accession to the European Union. It has a free and lively press. The record of macroeconomic management and growth is strong, the foreign exchange market is liberalized, banking regulation is in line with the Basle convention, and progress with structural reforms is well advanced. What is reported in this paper should not be seen as detracting from these striking achievements. Yet the legacy of the past is still powerful. Politicians and public servants are mistrusted. The credibility of the state is low and links between political and economic spheres are too close. There is little respect for the judiciary. The organizations needed to ensure accountability, transparency and audit are still finding their feet. In the public administration and public services, the vacuum created by the loss of old rules and controls has not yet been filled by new mechanisms of accountability, and habits of work are slow to change. And the new democratic principles – including the key concept of conflict of interest – are either not well understood or not well respected. Meanwhile, according to all reports, high level corruption and corruption in public services are serious and getting worse<sup>4</sup>.

13. These conclusions are supported by reports of the Supreme Audit Chamber (NIK), scholarly publications, public opinion surveys, numerous press reports and by the Ministry of Internal Affairs Report of May 1999 which attests that “corruption has escalated in the 90s”. The Ministry also considers that organized crime is on the rise, and that “influence over representatives of the administration is an integral component of this process”. The Statistics Office estimates that bribes by households total PLN 900 million annually<sup>5</sup>, while a number of academic and other commentators view this as a serious under-estimate. Public opinion polls indicate that two-thirds of the population believe officials frequently accept bribes and one half think that high-ranking civil servants use

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<sup>3</sup> Ministry of Interior report; many interviews.

<sup>4</sup> CBOS surveys. Also, on the basis of police statistics alone, bribery and corruption-related offences doubled between 1992 and 1998. While some of this increase may reflect improvements in policing, it is unlikely that this factor could account for more than a small part of the increase. This view is supported by other sources including the Ministry of Interior report to the Parliamentary Commission on Internal Affairs and Administration of April 1999.

<sup>5</sup> Quoted in Wprost, no. 17, 25 April, 1999, pp 30 and 50.

their positions to derive private benefits. People think that the state administration, the highest state authorities and the administration of justice are at the top of the list of most corrupt institutions, followed by the health service, police, and political parties<sup>6</sup>. These data indicate that a determined effort is warranted if Poland is to minimize corruption in politics and public administration and develop confidence in state organizations.

### **The international dimension**

14. The question will be asked: how does Poland compare with other countries? Inter-country comparisons are always problematic, and the difficulty of achieving a robust ranking of countries is very great<sup>7</sup>. Comparisons on single variables are somewhat less hazardous, however. Annex 3 presents the results of a survey of entrepreneurs carried out for the World Bank 1997 World Development Report on The State in a Changing World, in which Poland's position can be seen relative to others in the region.

15. Corruption is not only a domestic affair. All over the world, many foreign companies are known to offer payments and other benefits in order to secure deals and government contracts. Foreign companies may also try to grease their contacts at the political level, and Poland is not exempt from this. It will be important to establish a dividing line between legitimate lobbying and corruption – at present this distinction is not made or enforced. Until very recently, only the United States prohibited its companies and nationals from bribing the nationals of another country<sup>8</sup>, while in a number of countries, including in Western Europe, bribes to foreigners were not only permitted but tax deductible. Pressure to remove this laxity is now mounting, as exemplified in the OECD Convention on Combating Bribery in International Business Transactions which entered into force on 16 February 1999 and under which 15 countries have already passed legislation to outlaw this practice. Poland is a signatory to the Convention but is not yet in a position to ratify it, as its own legislation under the Convention is still awaiting submission to the Council of Ministers and to Parliament. Recent Council of Europe work in the corruption area (including on political party financing) also indicates that international concern is rising and that the time is ripe for a coordinated approach. It is in Poland's interest to support this international movement to stem and criminalize corruption.

### **Efforts to reduce corruption – the record so far**

16. Efforts to reduce corruption have so far focused on attempts to introduce formal ethics standards at Parliamentary level; passage of laws including a law on financial disclosure, and reliance on police and enforcement efforts. A "Clean Hands" campaign in the early 1990s made a strong start but effective implementation and follow through unfortunately did not materialize. A deregulation task force was set up but has not yet

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<sup>6</sup> Surveys quoted in Warsaw Voice, April 18, 1999.

<sup>7</sup> "...although it is possible to robustly identify twenty or so countries with the best and worst governance in the world, it is much more difficult to identify statistically significant differences in governance among the majority of countries." Kaufmann, Kraay and Zoido-Lobaton: "Aggregating Governance Indicators", World Bank, May 1999.

<sup>8</sup> The Foreign Corrupt Practices Act.

been able to make a significant difference<sup>9</sup>. These efforts are commendable in themselves but have missed the broad middle ground in which political elites and the state administration actually operate – and where many have a strong interest in resisting change. There is a need to strengthen the legislative framework with some specific, closely defined pieces of legislation<sup>10</sup>, but in general the emphasis has tended to be too much on passing laws rather than on implementing them effectively. Overall, Poland has most of the instruments it needs but not yet enough will and capacity to use them well. However, the recent strategy document released by the government recognizes that corruption endangers the proper functioning of the state and indicates that some appropriate measures will be put in hand.

### **The present challenge**

17. The brief scan of priority areas and issues that follows indicates that corruption is imposing costs in all four dimensions on Poland – macro-fiscal, efficiency and investment, costs to the poor, and credibility of the state. We hope that this paper will contribute a starting point for a strategy that can produce results and generate confidence that change is possible. But it should be recognized that the weakness of the new state institutions and the apathy and cynicism of the population are formidable handicaps to putting together an effective strategy to reduce corruption. These two problems must be explicitly tackled if the strategy is to be effective.

## **III MAIN AREAS OF CORRUPTION IN POLAND:**

18. Chapter III is organized as follows. The first three sections focus on corruption at the center of the State and among elected officials, starting with high level corruption and proceeding through the judicial and enforcement area to subnational government. These are the areas in which abuse of public trust is arguably the most serious. The next sections identify the most serious manifestations of corruption in terms of areas of government administration, regulation, financial management and services.

### **1. High level corruption<sup>11</sup>**

19. The integrity of the highest officials of the state sets the tone for the government and the country, so the impact of high level corruption, where it occurs, reaches far beyond the immediate case. All those interviewed identified high level corruption as the most serious corruption problem that Poland faces, and considered that it was growing. It will be essential to tackle this problem if the project for honest government is to be credible and to make an impact.

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<sup>9</sup> See also chapter III, 9. on Concessions and Licenses.

<sup>10</sup> Nepotism and favors in exchange for monetary bribes can be prosecuted, but cannot where the inducement is non-monetary – such as the offer of a post. Recent changes in the penal code have reduced the range of prosecutable offences and reduced penalties for nepotism in return for bribes. Amendments are also needed to the procurement law.

<sup>11</sup> High level corruption is defined as corruption practiced by high and elected officials of the state including Parliamentarians, the President, Ministers, Prosecutors and judges.

20. The central feature of high level corruption appears to be close links and feedback between political and economic groups, between public and private sector: it is reportedly a widespread practice to supply funds in return for favors<sup>12</sup>. The vehicle is often the supply of political party financing for which favors and preferences of various kinds are exchanged, but the bribe can also take the form of cash or benefits in kind to individuals, such as cars, and guarantees of employment for a politician or his/her friends or family.

21. The main channels of delivery are:

- Promoting or blocking new laws or amendments to laws;
- Malpractice in public procurement (government contracts);
- Manipulation of privatization;
- Interference in the award of concessions, licenses and tax exemptions;
- Conflict of interest in appointments to boards of State-owned enterprises and consequent links with contracts issued by these enterprises;
- Improper pressure on Customs enforcement.

22. A typical example would be the creation by a Ministry of an agency that would extend contracts to companies that would in turn funnel money back to the relevant Minister, officials, or political party. Members of privatization commissions can help to depress price and/or ensure that favored candidates win, with the understanding that the winner will then express his gratitude to the person or the party concerned. Similarly for procurement contracts and the award of valuable concessions and licenses. Parliamentarians have also interfered to protect those responsible for corruption in state-owned enterprises (SOEs).

23. Unconstrained lobbying is also an issue. Reportedly, the bribes paid by lobbyists have risen markedly<sup>13</sup>. Such lobbying, reinforced by the private interests of ministers, appears to lie behind the failure of Parliament or other state bodies to take effective action in the face of NIK reports and other evidence of corruption and abuse of public funds.

24. Other forms of high level corruption are manifested in nepotism in public sector appointments, and trading favors generally throughout the arena of public decision-making. This tendency is exacerbated by the practice of making political appointments down to medium levels in the administration. World Bank research<sup>14</sup> has shown that states with a high level of politicization of the public service are more prone to corruption, as well as vulnerable to loss of expertise and institutional memory.

#### Conflict of interest and political party financing

25. Two key issues on which action is needed are (i) conflict of interest and (ii) political party financing.

<sup>12</sup> For instance, media companies have financed a number of members of Parliament and their campaigns, with corresponding benefits through the Parliamentary Committee on Cultural Matters that advises on radio and television broadcasting. The Committee has recently voted to restrict competition.

<sup>13</sup> In 1992 the price of blocking amendments to the Law on Casinos was reported as \$500,000; more recently, it was the equivalent of approximately \$3 million (interview with Parliamentarian).

<sup>14</sup> Cited in WB *The State in a Changing World*; OUP 1997

(i) Failure to deal adequately with issues involving *conflict of interest* is at the heart of high level corruption. As mentioned above, this concept is neither well recognized<sup>15</sup> nor well respected, despite the passage of a law on financial disclosure. This law embodies good intentions but is ineffective. There are no mechanisms for checking asset declarations or ensuring that officials do not act in a situation of conflict of interest. A review of both law and implementation mechanisms should be included in any future anti-corruption program. However, the law on its own will not be enough: it will be important to disseminate information and guidance on situations involving actual or apparent conflict of interest and appropriate courses of action to take; and, more important still, politicians will need to set a clear example if these efforts are to have any credibility. This suggests that efforts to reduce corruption will need to have a cross-party character. Identification of anti-corruption efforts with only one party carries the risk that this issue will be turned into a political football or seen as an attempt to apportion blame in a partisan way. It is an issue that should be common ground for all parties and perceived as such.

(ii) The second key issue concerns regulation of *political party financing*. The Parliamentary Internal Affairs Committee is now considering what actions to recommend on party political financing and the election process. A number of models exist, including budget financing, caps on total campaign funds, caps on individual donations, and publication of lists of donors and sponsors<sup>16</sup>. Whatever the precise model chosen, the essential features are transparency, the capacity to identify donors and audit receipts<sup>17</sup>, and the existence of convincing penalties when the law is broken.

26. Other efforts to combat high level corruption include the progress that Parliament has made towards self-regulation, with the establishment of an Ethics Committee with power to hold hearings and to consider breaches of standards; and a “reglement” committee for serious infringements of rules. A register of benefits for Ministers and heads of offices has also been set up, that will be open to view on the internet; and there is a restriction on activities for a minimum of one year after leaving office. However, the political and organizational culture takes time to change, and it appears that these efforts have not yet borne significant fruit, and will need reinforcing. It is reported also that the police and the Intelligence Service are wary of investigating Parliamentarians, for reasons that include fear of retaliation. Police powers and responsibilities in this area should be clarified. It would also be advisable to review Parliamentary monitoring bodies and safeguards against corruption and seek ways to make them stronger.

27. Among the measures that would be worth considering are:

- A law on political party financing, together with effective audit and enforcement;
- A law on lobbying and registration of lobbyists;

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<sup>15</sup> We were told that the head of the NIK, the Supreme Audit body, is not prohibited from holding shares in companies that NIK audits.

<sup>16</sup> The Council of Europe has information on methods of regulating political party financing used in different countries.

<sup>17</sup> The widespread use of cash in the Polish economy makes it harder to create audit trails.

- Strengthening of the law on financial disclosure and introduction of effective mechanisms for implementation;
- Strengthening of Parliamentary codes of practice and monitoring and enforcement bodies;
- Codes of ethics for Ministers, judges, and other high officials of the state (including a definition of improper interests including those relating to activities of spouse and other close family members in the area of jurisdiction or political relevance);
- Strict regulation and clear standards to minimize acceptance of gifts and donations, and prohibition in areas where gifts and donations are never appropriate (e.g. to judges, police services);
- Clear criteria for appointments and transparency in appointment procedures;
- Mechanisms to ensure follow-up on NIK reports.

### Political parties

28. Political parties would also be well advised to adopt codes of conduct accompanied by sanctions, such as exclusion from office, against party members who have compromised themselves. Where it occurs, it will also be important to eliminate the practice of party members making payments to obtain high positions on the party lists so as to improve their chances of getting into Parliament.

## **2. Judicial, prosecutorial and enforcement bodies**

29. An independent, trustworthy and effective judicial system is an essential pillar of a democratic state. The possibility of recourse to the courts is an essential discipline on other structures of the State and thereby underpins their credibility. The judicial system is also a guarantor of property rights and a mechanism of dispute resolution, and is crucial to the achievement of good corporate governance in the private sector.

30. A number of our respondents noted that sentences can be bought, with members of the legal profession acting as intermediaries; in other cases the lawyer pockets the bribe, which never reaches the judge, while the client is led to believe that the judge is amenable to corruption. Respondents also noted the slowness, lack of efficiency, and lack of credibility of the courts, which are overwhelmed by cumbersome procedures, and are subject to long delays, sometimes of years. Many judges reportedly sit short hours, often from 10am to 1pm, three days a week. Apparently the judiciary has resisted previous attempts to improve and computerize procedures. Recourse to the courts is seen as impractical and outcomes are seen as unpredictable, partly because of incompetence and in some cases because of corruption. For these reasons, a number of private sector respondents said they did not try to take legal action against crooked procurement and other contracts.

31. Failure or delay in execution of both administrative and criminal court sentences is a long-standing problem. These delays allow ample time to dispose of assets and escape monetary penalties.

32. Registration of companies and land transactions was cited many times as a problem area. The situation appears to be worse in Warsaw, where there is only one court to service 35,000 companies which need to register or to obtain extracts from court documents to prove registration. It appears that all courts are assigned the same size and capacity of court administration and secretariat, although the type of business conducted by the Registration Court and its needs for administrative staff are entirely different from those of other courts. Turnover of court clerks is high, and few bring professionalism and expertise to their jobs. Facilities including reading rooms are too small, which creates control rights over access, and document search is slow because registries are not computerized (with some exceptions: there was a partial computerization, which does not appear to have been successful). Lawyers and other parties with legal interests frequently find they must bribe to obtain access to the reading rooms and to registry documents that should be on open files.

33. The same problems arise at the Land and Mortgage Registries. Waiting times of up to two years have been recorded in making entries in the Perpetual Books. This fosters corruption and also offences such as the simultaneous sale of property to more than one purchaser, as registration of transactions is not up to date and inspection of title deeds is impossible. Officially, cases cannot be accelerated without legal grounds, but in practice there are both “special” and “ordinary” waiting lists. Lawyers who become expert in negotiating this non-transparent terrain can expect to be highly rewarded.

#### Key factors

34. Consideration should be given very soon to the status, training and pay of the judicial profession. Rather than being seen as the crown of the legal profession and an essential arm of the state, judges are low-paid and not well-respected. The low pay of judges and court officials creates incentives for corruption, and the low status of the profession undermines efforts to make professional standing and reputation for integrity a disincentive to corrupt behavior. The profession is seen as a haven for unambitious part-timers or as a holding pen for those who wish to become lawyers.

35. In some cases, judges seem to be unaware of what would constitute conflict of interest. Court administrative practices, inadequate facilities and equipment, and delays also foster corruption, and the complicity in corruption of some members of the legal profession is clearly a serious problem.

36. It would be worth involving key members of the judicial and legal professions in discussions on the way forward and in formulating an action plan that would include consultation with the public and users of the Courts. It will be important to deal with the growing caseload and to train judges in economic law and regulations; and to modernize and expand judicial registries to reduce corruption and high transactions costs in property and credit markets. As courts and their administration are the responsibility of the Ministry of Justice, it could also be appropriate to ask for an analysis and recommendations for an action plan from that Ministry.

### Office of the Prosecutor-General

37. The Prosecutor-General's Office is headed by an active politician. This creates at least the appearance of an improper link with the decisions that have been taken to remove prosecutors believed to be honest from particular cases. The rate of follow-up on NIK reports is low. Doubts were also expressed about the staff of the Office. There are perceptions that papers get lost, and that some genuine cases against highly placed individuals are not prosecuted, or when prosecuted, are not concluded. Consideration should be given to distancing the Office from the political process and creating an independent and well-organized prosecutorial function.

### Security and enforcement bodies

38. A number of cases were reported in which the State Security Office appeared to be acting for private benefit. It is also reported that the State Security Office is subject to political influence in its operations and on the cases that it refers to prosecutors. (see also chapter III, 3 below on subnational government).

39. Disturbing cases have also been reported among the Police force, most recently the "Octopus" case in Lodz, where possible links between police officers and organized crime are being investigated. The Police Report of the EU, in the context of Poland's preparation for accession, has pointed out risks to the security of the EU arising from low pay, a poor career structure, and associated corruption in the police.<sup>18</sup> According to press reports, every year about 200 police officers are fired for bribery offences, and the police have now set up an internal department to deal with disciplinary offences involving bribery, which dealt with 500 cases in 1998<sup>19</sup>.

40. Opinion polls repeatedly identify the Road Police as bribe-takers. This may appear as low-grade petty corruption but it is a serious matter for individuals in a free society and a heavy burden for those on low incomes. These practices undermine public safety and the authority of the state.

## **3. Subnational government**

41. Many concerns were expressed to us about the prevalence and probable future growth of corruption at subnational government levels. Opportunities and incentives for corruption will grow steeply as the territorial reform becomes established and the massive shift in disbursement of funds from central to subnational level takes place. Under the reform, it is estimated that subnational government disbursements will double from 23.5 percent of public expenditure in 1998 to 47 percent in the future. In addition, substantial EU pre-accession, structural and cohesion funds will be channeled through subnational bodies. Risks and opportunities for corruption will also be greater where voivod, powiat and gmina<sup>20</sup> powers exist in the same area, complicating and reducing transparency in lines of responsibility and decision paths.

<sup>18</sup> As cited in Zycie, October 11, 1999, p1 and p7.

<sup>19</sup> Pawel Biedziak, quoted in Zycie, October 11, 1999, p7.

<sup>20</sup> Regional, county and municipality levels of administration.

42. Widespread corruption in subnational administrations undermines efforts to promote local and regional development, improve services and reduce local and rural poverty. It mirrors many of the issues that arise at Parliamentary and high political levels of the central government administration. Local administrations tend to be highly politicized, with close links between political parties, elected councilors, and administrative staffing and pay decisions<sup>21</sup>. Staff numbers have been rising from well before the territorial reform<sup>22</sup>. In big cities, it is reported that members of the public need political party support to schedule meetings with influential officials. In Warsaw, Board meetings that used to be open to the public are reportedly now closed.

43. The control rights that local governments exercise over zoning decisions, licenses and permits for economic activity, contracts for construction works, goods and services, property rent controls and other distortions in setting tariffs, furnish ample opportunities to extract bribes and trade favors. These activities have an adverse impact on local revenues and expenditures, and also result in serious misallocation of resources, with consequent damage to the local economy and society

44. Municipal ownership of large amounts of land and real estate aggravates the situation and adds to the opportunities and incentives for corrupt behavior. The law passed two years ago forbidding elected representatives from having contracts with the City or doing business with Council assets is honored in the breach - approximately half of the Warsaw councilors or members of their families are reportedly involved in business using municipally owned land and shops<sup>23</sup>. The provision preventing councilors from simultaneously holding management positions in municipal companies was removed before the territorial reform legislation was passed by Parliament. Corruption linked to election funds is also a problem at subnational level. Companies that refuse to cooperate may be excluded from the procurement process.<sup>24</sup> In bigger cities, there is strong pressure from potential investors, including foreign investors, who can afford substantial party donations. In smaller cities and at village level, there is a risk that local elites develop, creating a network that controls the town and can influence bank credit and other decisions affecting both businesses and private individuals.

45. Key vulnerable areas are:

- Political party financing
- Real estate transactions: privatization, leasing, construction and other permits
- Public procurement
- Allocation of apartments
- Abuse of documents: ID, passport and driving license issue.

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<sup>21</sup> For instance, high pay for the starosta is believed to be the quid pro quo for high per diem allowances for councilors. In one local administration, the going rate for appointments as managers of municipal companies was reported to be three times the Mayor's salary.

<sup>22</sup> See Annex 1.

<sup>23</sup> Interviews with Warsaw councilors and officials.

<sup>24</sup> Interview with representative of a foreign construction company, September 6, 1999.

### Land and real estate

46. Many self-governments own large amounts of land and real estate. For instance, Gmina Centrum in Warsaw owns one million square meters of commercial space. This gives local administrations significant leverage over urban development, business opportunities, and kickbacks. There appears to be a strong correlation between improvements that raise land values and the location of residences of city officials. In addition, there are reportedly many cases of Council members or their spouses renting from the Council, often at low rents set in 1990/91 (some rents are not indexed at all, some are indexed but remain below market levels). The possessor of the lease then sub-leases illegally at market rents, reaping the difference. Other cases involve the creation of special conditions for sale, such that the land or real estate can be sold only to those now leasing, or only at an authorized price, or transactions take place on the day of announcement so that only those in the know can participate. The result is below market returns on public assets and high gains for well-placed private interests. Revenues from public assets are further lowered when rents from municipal shops and buildings go into the pocket of the municipal manager rather than into municipal revenues.

47. Corruption in the allocation of apartments is also a problem. Leverage over people who are anxious to keep their apartments and their jobs, and who do not see alternatives, adds to the power of local administrations. In addition, some apartments are set aside to be allocated at the personal gift of the Mayor. Investigations indicate that these apartments are not always used for the poor or other cases of social need.

### Licenses and permits

48. As noted above, licenses and permits confer control rights on officials and with them a source of corruption. Most significant are those relating to architecture, construction, land registration, land survey, and any other matters to do with municipal land and buildings. The consequences are inefficient allocation of resources, delay in investments, a sub-optimal level of economic activity, and potential damage to public health and safety.

### Municipal procurement

49. Public procurement at municipal level is reported to be notorious (see also chapter 3. on Public Procurement). Reported malpractice includes: bribe rates set as percentages of the winning bid; contracts given to companies belonging to the family of council members; all companies bidding having the same owner or the same address, or fictitious addresses.

50. Procurement abuses appear to be a particular problem where construction projects are concerned, such as those involving bridges or office buildings. Many cases cited showed that further costs of corruption occurred in the form of the serious delays that result<sup>25</sup>. Corruption in public contracts, whether during the bidding process or during contract

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<sup>25</sup> For example, the case of the Warsaw mass transit ticket system, for which bids were opened in 1994; it appears that the contract was finally resolved in 1999.

execution, can also result in poor quality of construction and inadequate safety standards. The risks to public safety are even higher where there is also corruption in inspection procedures.

#### Links with Police and State Security

51. Links between municipal authorities, on one hand, and police and state security forces on the other, were also reported. Cases exist where these forces have demanded blank passports, ID documents and driving licenses, with no documentation of the transaction. It was also reported that the threats and pressure associated with this practice are hard for local officials to withstand: some succumb, some have resigned.

#### Key factors

52. As with high level corruption, much of self-government corruption is fuelled by close links between public officials and economic interests. The same kinds of safeguards mentioned in the section on high level corruption are therefore relevant. But conflict of interest and cronyism are much harder to avoid in small communities. It is therefore all the more important that work is organized so that is open to scrutiny, and that decisions are taken in meetings that are open to the public and the press. An updated Ethics Code, and training and illustrations of what good practice means in procurement, licensing and other relevant situations would also be helpful – many respondents stressed that officials do not always know what it would take to do it properly, having had no good models. It would be useful to develop guides of good practice, explaining for instance when officials should identify conflicts of interest or recuse themselves, or that councilors should not participate in tender evaluation (see also the section on Public Procurement). Self-governments could also be encouraged to adopt administrative procedure codes with the force of law. Finally, it will be important to adopt clear allocation rules for both external and central budget funds and strong financial management and accountability at both national and subnational levels.

#### **4. Public procurement<sup>26</sup>**

53. Misprocurements on large state contracts, that sometimes exceed market prices by a factor of 2 or 3, cost the State millions of zloty. Particularly grave problems, both in the bidding process and during contract execution, were identified with large IT contracts (e.g. ZUS, Customs, Poltax, Post Office), and in roads and other construction projects (around 70 percent of public procurement is in construction). Corruption in procurement of services is also reported. It is possible that some of the problems were caused by incompetence, but most reports clearly related to corruption. It would be surprising if incompetence were an issue in Poland. After more than a decade of transition, the experience of Western procurement practices exists, and the technical expertise to design contract documents and evaluate bids has existed for much longer than that. The question arises of why such expertise is not more frequently used.

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<sup>26</sup> The Country Procurement Assessment currently being conducted by a World Bank team will supply further details, analysis and recommendations on public procurement.

54. Significant abuses occur before the tender is issued: bribes to ensure early access to information on the technical requirements and the specification of criteria for the points system were frequently cited as a decisive factor. Conditions can be constructed in such a way as to favor one particular bidder, and are sometimes subject to change after bidding has started. Procurement abuses are also enabled by weak bidding documents and poor evaluation practices. Characteristics (such as financial standing) that should be used to include or exclude firms from the bidding process altogether are instead used as part of the evaluation, and are slanted in numerous ways to favor a predetermined winner: e.g. the successful bidder can be defined by a requirement of profitability of precisely 12 percent.

55. Various other techniques used to bypass proper public procurement methods include the addition of large additional contracts to the contract of the winning bidder after an initial small contract has been let. In some cases, other tenderers are informed of the lowest bid so that they can adjust their prices and inducements accordingly. Winning firms can also be allowed to negotiate the tender price upwards after the contract has been awarded. Access to confidential information in advance appears to be the key feature of these abuses. Collusion among bidders (i.e. non-competition agreements between firms that segment the market) also serves to raise prices and subvert the procurement process.

56. Misprocurements raise questions about the adequacy of fiscal and governance controls and accountability mechanisms in other spheres of government responsibility. This issue is highlighted, for instance, by the cases of contracts awarded by large bankrupt state-owned enterprises (SOEs).

#### Key factors

- The public procurement law
- The role of NIK
- The role of the Public Procurement Office (PPO) and the quality of standard documents
- Development of technical expertise and training

57. The present procurement law represented a significant step forward but needs to be strengthened in various respects. Coverage of the law should be explicitly extended to services, the complaints and appeals procedures should be better specified, reasonable time periods should be defined for bid submission (at present they are only defined for contracts over 200,000 euro), and delays in bid-opening should be prohibited.

58. Efforts by NIK and the Regional NIK Clearing Offices in compliance auditing will need to be strengthened if state contracts are to be audited adequately. The task is enormous and is growing further under the territorial reform and with the creation of Health Funds. Strengthening audit capacity is therefore urgent. Introduction of a more in-depth procedural audit function would also be useful, as simple compliance audit cannot go deeply enough below the surface.

59. The Public Procurement Office also needs to improve the model documents and procedures that it disseminates. It is therefore urgent to supply:

- Well-designed standard bidding documents, at least for goods and construction works<sup>27</sup>
- Reform of the points system in awarding contracts and strict procedures for bid evaluation.

60. Other safeguards to consider are the introduction of a two level decision procedure – one for evaluation and recommendation, one for decision; and a minimum number of people on bid and evaluation committees, to make collusion more difficult. Disclosure of tender and price should also be in the public domain. We understand that the reform of the criteria used to award contracts to remove manipulation and excessive discretion is now under consideration. If effectively implemented, this will be a much needed improvement.

61. The Public Procurement Office will also need to improve the technical expertise available to arbitrators and promote the development of a well-trained procurement profession. Although the Office is too small to provide training on the scale needed countrywide, it could usefully develop accreditation standards for training institutes so that specialists can be properly trained and certificated. This is particularly important in the light of the territorial reform and the large numbers of people new to the task who will need to be trained in public procurement.

## **5. Control and supervisory bodies<sup>28</sup>**

62. Autonomy and impartiality in control and supervisory bodies are not yet well established. Nepotism in appointments results in too many political appointees, and too few professionally and technically well qualified members. In consequence, there is little incentive to use the considerable powers of the control bodies to stamp out bribery and other forms of corruption or to ensure high professional standards of entry to the profession and in the conduct of its activities.

63. To strengthen the independence and technical qualifications of supervisors, job descriptions will need to specify high levels of technical qualifications and professional probity. Appointment committees will need to operate in the open, with clear criteria and documentation of the decision-making process. These documents will need to be produced in the event of future investigations or appeals. Safeguards will also be needed

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<sup>27</sup> The existing Public Procurement Law does not explicitly cover procurement of services. A new law is now in preparation.

<sup>28</sup> Supervisory bodies: apart from NIK, the Supreme Chamber of Supervision, these are: ABiEA - Agency for Highway Building and Operations; GIOŚ - General Inspectorate for Environment Protection; GUNB - General Construction Supervisory Office; KPWiG - Securities and Stock Exchange Commission; KRRiTV - National Council for Radio and TV Broadcasting; PIP - State Labor Inspection; PITiP - State Telecommunication and Postal Inspection; PUNU - State Supervisory Office for Insurance; UNFE - Pension Funds Supervisory Office; UNUZ - Health Insurance Supervisory Office; RIOs - Regional Audit Chambers; UDT - Technical Supervision Office; URE - Energy Regulation Office.

to protect the security and independence of supervisory bodies and improve remuneration. Introduction of an audit mechanism would be useful. And it would be worth reconsidering the current procedures whereby a supervisor can be dismissed instantly by high political decision, and introducing protections including formal complaint procedures and due process for dismissals. To guard against political pressure, there should also be a requirement that any communications, influence or recommendations to members of control bodies must be put in writing. And it could be helpful to introduce two levels of procedure for decision-making: one level would prepare the information and options, a second and separate body would take the decision. This method was pioneered by the Securities Commission of the Warsaw Stock Exchange.

## **6. Privatization**

64. Widespread nepotism, cronyism and other forms of corruption are reported in appointments to privatization commissions and selection committees. It appears that some Ministry representatives and their connections are appointed in order to ensure particular outcomes of the privatization process, ensure that funds are channeled back to particular individuals or political parties, contribute to a complex network of traded favors, and/or to manipulate prices downwards.<sup>29</sup> For instance, NIK estimates that the state lost at least PLN 85 million in the privatization of the Centrum department store complex in Warsaw<sup>30</sup>. In some cases there can be direct bribery: figures of 5-10 percent of the total value of the asset were mentioned. This situation thrives on lack of transparency about appointment criteria, qualifications for membership of committees, and members' connections and interests.

## **7. Role of the Ministry of Treasury**

65. The opportunities for corrupt practices described above are exacerbated by the low pay and inadequate experience and qualifications of many of the officials of the Ministry of Treasury who steer the privatization process. It should be recognized that the Treasury has successfully managed a number of complex privatizations. However, people on very low wages are conducting valuable deals and are not well placed to ward off corruption. Various ways of introducing safeguards and reducing incentives to corruption could be considered, such as improved audit, better training, more transparent procedures, and higher pay.

66. Despite recent privatization and restructuring activities, SOEs, including big enterprises in the coal, steel, pharmaceuticals and arms industries, and others such as the Ursus tractor factory, remain a substantial drain on the national budget. These enterprises are in many cases insulated from market disciplines and the sanction of bankruptcy. This, together with their links into political networks and closely related companies in the private sector create incentives and opportunities for corruption, especially regarding cronyism in procurement, contracting, and marketing practices and procedures. Control and monitoring appear to be weak and external audit reports do not protect against such

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<sup>29</sup> It must be recognized however that market prices may not correspond to balance sheet historical costs.

<sup>30</sup> NIK report to the Sejm, reported in the Polish News Bulletin, June 23, 1999.

practices. It seems clear that the capacity of the Treasury to exercise effective governance and financial control over SOEs is in urgent need of strengthening.

## **8. Extra-budgetary funds**

67. The existence of extra-budgetary and special funds means that a large part of the budget is beyond effective Parliamentary scrutiny or scrutiny by the Ministry of Finance. Special funds of various kinds are in charge of 38-41 percent of expenditure and approximately 30 percent of revenues<sup>31</sup>. The largest funds are the Social Insurance Fund, Farmers' Social Security (KRUS) and the Labor Fund, which together comprise over 90 percent of the total. The funds that command the largest amounts of the remainder (and a growing share of revenues) are the Fund for the Rehabilitation of the Disabled (PFRON) and the Environment Protection Fund (NFOS). The fund expenditure and revenue figures just cited understate their financial impact, as a number of funds also engage in credit operations.

### 68. Key factors

- Loss of fiscal flexibility
- Unmonitored lending activities
- Revenue forgone
- Inadequate controls on expenditure including procurement and other fund activities
- Lack of transparency.

69. Funds that are earmarked or tied undermine Government's flexibility to allocate expenditure in response to changing priorities, constraining allocative efficiency and reducing incentives for financial discipline. (Funds based on social contributions are designed to be exempt from fiscal flexibility but other governance and financial management considerations remain relevant.) Tax expenditures (forgone revenue) are also significant, and reported waste of public funds through misprocurements<sup>32</sup> and other abuses is enormous. In some cases, Funds have been known to lend for purposes beyond their mandates.

70. In this context it is understandable that a number of respondents drew attention to the existence of "states within states": public sector agencies that control, and in some cases, also lend substantial funds, have important links with the private sector and with political parties, and whose operations may not always be transparent. Of these, the most frequently cited were the Fund for Environmental Protection, the agricultural agencies, ARMA, ARR, and APA; the Coal Restructuring Agency; and PFRON. PFRON management recognizes that reforms are needed and is currently cooperating with the World Bank on a review of its legislation and activities.

71. More general concerns relate to the ability of agencies with extrabudgetary funds, and not only those mentioned above, to operate in unorthodox ways. It appears that

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<sup>31</sup> A more detailed account of Extrabudgetary funds can be found in Annex II.

<sup>32</sup> The case reported in Rzeczpospolita of the purchase by the Lodz branch of ZUS of a building for PLN 21 million, which had sold six weeks before for PLN 9.5 million, from a company for which the ZUS vice-president in Lodz acted, appears to be a striking example.

companies, which can reportedly include officials of the parent ministry or their connections, are sometimes formed around these agencies in order to benefit from their activities including contracts. This is clear conflict of interest and abuse of public funds. These and other forms of malpractice also highlight inadequate policy control and weak internal audit by the parent ministry, as well as inadequate fiscal monitoring and control.

72. There is a need to bring agencies back under clear policy control, and institute detailed financial reports and more effective monitoring. All revenues and expenditures of agencies and extra-budgetary funds should be integrated into a unified budget and so become subject to the Budget Law. As previously mentioned, funds based on social contributions can be excepted from this recommendation, but all special funds including those related to social insurance should be subject to effective scrutiny over both revenues and expenditure.

73. We hope that the assessment of extra-budgetary funds mandated by the new Public Finance Law, and now underway, will generate a reconsideration of the status and privileges of these funds as well as improvements in their governance and financial management.

## **9. Customs and tax administrations**

### Customs

74. Customs is in many countries a service which is vulnerable to corruption and to connections with organized crime, and Poland is no exception. This vulnerability is reinforced by its position on important trade and transit routes. Corruption is a problem on both western and eastern borders, and is reportedly worse on the western border, associated with the entry of smuggled goods destined for countries further east.

75. Incentives for corruption in customs transactions are greater when tariffs and customs duties are high and when rates for different categories of goods vary a great deal, creating incentives to reclassify goods between categories. These incentives are greatly reduced now that Poland charges a zero tariff on non-agricultural imports from the EU, but it still charges an average tariff of 18.2 percent for agricultural products. The average tariff rate is 2.3 percent on total imports from the EU - which constitute about 70 percent of all Polish imports. Poland also has a free trade area for industrial products with the EFTA<sup>33</sup> and CEFTA<sup>34</sup> countries (excluding cars, steel products and crude oil and oil products). Notwithstanding the relative absence of non-tariff barriers to trade<sup>35</sup> and recent reductions in tax and duty rates, there are still sizeable divergences between MFN and other rates, and between agricultural and other goods. The existence of ad hoc and temporary exemptions and “duty suspensions” aggravates the potential for corruption. There is a hierarchy of corrupt transactions, from “clear jobs”, or bribes of up to around

<sup>33</sup> European Free Trade Association: Iceland, Liechtenstein, Norway and Switzerland.

<sup>34</sup> Central European Free Trade Association: Bulgaria, Czech Republic, Hungary, Romania, Slovak Republic, and Slovenia.

<sup>35</sup> In 1996, the proportion of tariff lines affected by a non-tariff barrier was 1.6 percent, as compared with 14.2 percent in the EU: see Poland Country Economic Memorandum, Report no,16858-POL, World Bank, July 1997.

PLN 200 to enable queue jumping, to “black jobs”, which are more serious activities such as turning a blind eye to falsified documents or invoices or being complicit in smuggling of illegal and dangerous goods or traffic in people.

76. Corruption is exacerbated by extremely low salaries relative to the high stakes available, as well as social and peer pressure in small working communities on the border, many of whose facilities and infrastructure have benefited from the flow of bribes.

77. The Customs management is making efforts to upgrade the administration and minimize corruption. There is now a new Customs Code (1/1/98), and Customs management has introduced internal audit and also post-audits in cooperation with the tax administration. A Customs Advisory Group has been set up for consultations with the private sector. Customs are preparing a new Ethics Code, and plan to launch risk analysis in January 2000, which will remove a significant area of discretion from individual officers. There is a new law on rotation of staff, and the Customs police now have a stronger mandate.

78. However, much remains to be done. There is a need to standardize policy and administrative practices as well as computer applications among the 19 customs offices, introduce a centralized surveillance system, and ensure that Regional Directors play a more effective role. The system of declarations and financial disclosure needs to be implemented more effectively. And it will be a challenge to change the mindset of officers, many of whom have been trained under the old system. Customs is now recruiting some able young graduates but finds it hard to retain them given the low pay levels.

### Tax administration

79. The challenges facing the tax administration are typical of those facing a transitional country which must move from a system based on a centralized economy and a small number of large enterprise taxpayers to a decentralized economy and a proliferation of private sector and individual taxpayers. Difficulties are compounded by the widespread use of cash transactions<sup>36</sup>, including the payment of wages in cash so as to avoid social security and personal income taxes.

80. Money laundering remains a problem<sup>37</sup>, and proceeds from organized crime reportedly pass through sectors that are hard to monitor, such as the restaurant, bar and entertainment sectors. However, tax authorities still appear to concentrate on large taxpayers, rather than on strengthening the tax net throughout the economy.

81. According to NIK<sup>38</sup>, tax legislation is unstable and imprecise. The most significant sources of corruption in the tax system appear to be the extensive system of discretionary exemptions (though these are now being reduced) and the discretionary power to annul

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<sup>36</sup> The size of the gray economy is variously estimated at between 15 and 25 percent of GDP.

<sup>37</sup> A draft law against money laundering is now in preparation.

<sup>38</sup> NIK Review of the Tax System, reported in PNB on June 24, 1999.

tax arrears for selected taxpayers. NIK has calculated that the value of income tax breaks in 1996 corresponded to 22 percent of personal and 40 percent of corporate tax revenue. The large potential gains involved and the imprecise and discretionary criteria for tax exemptions both create incentives for corruption. The central administration also has difficulties in imposing uniform tax policy, interpretations of laws, and administrative practices throughout a large country with strong regional tax chambers. Reportedly, corruption in the tax administration is worse in small cities and towns, where effective supervision and control by Head Office is harder, especially in the absence of a fully automated information system or of a fully codified explanation of tax obligations available to all taxpayers. An in-depth analysis and recommendations can be found in the report of the joint IMF/World Bank mission of October 1998.

## **10. Concessions and licenses**

82. As in many countries, the award of concessions and licenses is fertile ground for corruption. In Poland, more than 50 types of economic activity are regulated by administrative decision. Among the many licenses and permits required to conduct economic activity, the most problematic areas cited to us were:

- licenses to broadcast television and radio
- telecommunications concessions
- transport licenses, especially MoT-administered international transportation licenses for trucks to enter Germany and countries beyond
- permits linked to construction, real estate, and commercial activity.

83. The draft Law on Economic Activity now before Parliament is a welcome development. This Law explicitly defines the areas that should remain subject to license, such as sale of alcoholic beverages and the arms trade, but liberalizes the majority of areas that currently require licenses. In some of these areas, a permit would be the right solution (to obtain a permit a company must only meet the relevant criteria, hence the issue of permits involves much less discretion). The draft law proposes that only six areas of economic activity would remain subject to license, and also states that licenses would be issued for periods between 2 and 50 years. It would be helpful to define the criteria on which the six areas have been selected, and also the criteria for determining the types of activity to be licensed as well as the term of a license. An interesting issue is the question of “self-governance” by industry associations or chambers of commerce. Proponents of concessions sometime argue that in areas where there are no business self-governance organizations, entrepreneurs have to be controlled by the State in order to protect the rights of consumers. Conversely, they wish to assign these control rights to the self-governance organizations when they do exist. This debate appears to be one of the main constraints to passage by Parliament of the Law on Economic Activity. Professional associations can play a valuable role in defining and raising standards and in peer review. Business organizations also have a role to play. However, where regulation of business activity is concerned, their role should be regarded as complementary to that of the state. It would be unfortunate if the state ceded its legal rights in this matter to an industry association or chamber of commerce.

## 11. Health

84. Health services and markets are characterized by interdependence of supply and demand, asymmetric information, gatekeeper power, divergence between public and private interests and incentives, and other characteristics which provide fertile ground for corruption. Patients are in a uniquely weak position to counter these difficulties, especially if they are poor, reinforcing the dangers of corruption. In Poland, the situation is further complicated by:

- the overhang of mentality and practices – including frequent bribery, lack of financial discipline and an arrears habit - inherited from the previous regime;
- inexperience and weakness of new institutions created by the 1998 health reform;
- the vast sums – over PLN 22 billion in 1999 - that will now be transferred to and disbursed by the new Regional Health Funds;
- inadequate pay of doctors and other medical personnel.

85. A number of our respondents felt that corruption in the health sector was so great that the health reforms would not work. Even if the impact falls short of this, it seems clear that access to health services and also their efficiency and effectiveness are compromised by corruption, and attention to this area is therefore a high priority.

### 86. Key factors

- Management and supervision of health funds
- Asset management and privatization
- Incentives for corruption by doctors
- Interface between hospitals, doctors and the pharmaceutical industry and incentives for abuse by pharmacies and pharmaceutical companies
- Informal payments
- Fraudulent certificates

87. The health reform has set up 16 regional Health Funds which are responsible for allocating insurance funds, for making contracts with health providers, and ensuring that budget ceilings are respected. A Health Insurance Supervisory Office has also been established. In general, standards and mechanisms have yet to be developed to ensure the smooth and transparent working of the new system, and there is scope for well-intentioned mistakes as well as willful abuse. Effective monitoring mechanisms and clear contracting rules will need to be developed.

88. Under the reform subnational governments have acquired substantial valuable assets. While some are making commendable efforts at sound asset management and expenditure control, obvious risks remain as many local administrations are prone to corruption particularly in important areas such as financial management and public procurement (see chapter III3 above). Many hospital directors are habituated to operating in arrears, which compounds the financial risks. Debts of PLN 7 billion were cleared on January 1, 1999 to enable the reform to start clear and to prevent a secondary market in debt which could have transferred public assets and their use to private hands in an unregulated way. It is conceivable that the moral hazard evoked by previous debt cancellations may lead to lax financial management, enabling corruption which might

otherwise have been minimized by stronger budget discipline. In the event of another debt build-up, hard choices would have to be made between relaxing budget limits and denying care.

89. As well as respect for aggregate expenditure ceilings, stronger budget discipline in hospitals will need to take the form of efficiency in equipment procurement and in allocation of resources to different kinds of treatment and to length of hospital stay. Many cases in contravention of the public procurement law<sup>39</sup> have been reported, frequently of vendors pushing purchases of expensive machinery, information technology and laboratory equipment, using bribes, discounts and donations to get particular types and brands accepted that will then lock in the hospital to future, much larger purchases from the same company or brand. Some of this equipment is apparently so valuable, unused and/or so remote from patients' needs, that "it will never depreciate". Doctors are sometimes accessories in such purchases of equipment for the public system, in order to use it for the benefit of private interests. In addition, hospital expenditure decisions are hard to monitor because of the absence as yet of established treatment standards.

90. Self-governments' attitudes to privatization of health assets vary widely. Some wish to hold on to assets blindly, rather than consider rationalization; others wish to privatize them in an ill-considered way. Although Poland supports private sector primary care, hospitals raise more difficult issues, and reasonable fears have been expressed about "wild privatization" in the absence of a strong regulatory framework, effective monitoring capacity, and provisions to ensure access for the poor. Cases have been reported of hospital management deliberately bankrupting hospitals so that the assets can be sold cheaply to them or their connections. The Health Insurance Supervisory Office will need to develop capacity to detect and prevent such abuses, and to help determine in what cases hospitals should be closed or can be privatized without detriment to public care.

91. It is well-known that doctors' private interests can diverge substantially from public and patient interests, whether this takes the form of prescribing unnecessarily expensive treatments that will be technically or financially interesting to the doctor, skimping on time spent, collusion with drug and other suppliers, or supplying false documents in return for bribes. Mechanisms for restraining these tendencies range from the inculcation of strong professional ethics and active use of peer review, to various public and private sector methods of regulating costs and treatment standards. Development of such mechanisms should be a high priority.

92. The interface with the pharmaceuticals industry is prone to corruption almost everywhere in the world and has been characterized as "an invasion" in Poland. Methods will need to be found to regulate sponsorship of overseas trips and other favors from drug companies and to prevent bias in prescribing and the use of unnecessarily expensive drugs. As yet there is little financial control over ambulatory care and prescriptions, or to prevent collusion between doctors and pharmacies over kickbacks and amounts of the drug actually dispensed. This situation should improve now that a list of approved drugs

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<sup>39</sup> The responsibilities of the Health Insurance Supervisory Office do not cover public procurement. This is an area in which NIK or its regional offices will need to develop greater audit capacity.

has been promulgated and a mechanism is being put in place to identify costs by doctor at pharmacy level.

93. Informal payments pervade the Polish medical and health care system, and can range from small gifts ex post to poorly-paid carers, to “speed money” for faster treatment, to extortion of large bribes on an informally established tariff for surgery and other treatments. Research for this paper and early evidence from the forthcoming World Bank study “Informal Payments for Health Care in Poland” indicate that informal payments introduce perverse incentives in the health system, distort priorities, limit access, and compromise efforts to improve efficiency, accountability and equity. They make it impossible to assess the actual total cost of health care. Many cases have been reported of medical personnel including orderlies and nurses refusing standard daily care for immobile hospital patients if bribes are not forthcoming. In this situation, mobile patients and family members can sometimes fill the gap, but this is an unreliable and unacceptable solution. To some extent, the prevalence of informal payments can be related to extremely low pay in the health sector, but many of the recipients are already on high incomes. There are indications that the pathology appears to have grown beyond compensation for low pay and become predatory. Pressure to eliminate informal payments can be expected to rise as people become unwilling – and/or unable - to pay both their formal health contribution and make informal payments, but it will take more than pressure to solve this problem. Individual hospital directors who have attempted to eliminate informal payments have been unable to do so. The first priority will be to ensure that no one is denied emergency or life-saving treatment in the absence of bribes. Then there will need to be a concerted effort to design and implement an integrated package that combines regulatory and pay reform with effective monitoring and penalties while simultaneously raising professional ethics and standards of health care.

94. Some doctors also stand accused of supplying fraudulent certificates for absence from work and for sickness and disability benefits. This practice results in the loss of public funds for cash benefits, and will also need to be tackled by a combination of regulation, monitoring, peer review, and professional ethics.

## **12. Other areas**

95. Other areas susceptible to corruption were reported to us, such as bribery in driving tests, in some interactions with police, and in education, particularly concerning extra payments required at school, and bribes required to enter particular schools and universities. There are probably many other areas that could be identified: this report is certainly not the last word on the subject.

96. Most important of all are the public administration and financial management systems of the state. These cannot be regarded as specific problem areas so much as part of the whole fabric that constitutes an effective state. Their reform is important and should be launched soon, but will take considerable time: the ship of state turns slowly. These broader reforms are noted in the chapter below: Medium-Term Issues.

#### IV MEDIUM-TERM ISSUES – PUBLIC SECTOR REFORM

97. The integrity, efficiency and transparency of all the organs of the state throughout all their operations are the main guarantor against corruption. Reform of the State covers Parliament, the judiciary and the executive. Such reforms are complex and time-consuming, and will require sustained political support at the highest level. But it is important to start soon. Improvements in targeted problem areas are unlikely to be sustainable without a strengthening of the public sector more generally. This will need to be complemented by a Freedom of Information Act providing access to public sector information with safeguards for commercial secrets and individual privacy.

98. A central component of an honest and effective state is an efficient, responsive and honest public administration. Despite notable reform efforts, public administration and services have a long way to go. Problems identified include:

- increasing politicization of public administration;
- expansion in numbers employed: the number of jobs in the state administration has increased by nearly 50 percent in the five years to 1998<sup>40</sup> (of which at least some part seems to be related to nepotism and favors);
- an irrational structure of pay differentials combined with excessively low pay in some key positions;
- lack of transparency in financial management
- absence of a professional culture of service.

99. What should be Poland's model for public sector reform? Some people view managerial models that involve substantial discretion, power to award contracts, output accounting and widespread delegation to agencies as the cutting edge in public sector reform. In the context described in this report, it would be unwise to adopt such models before the problems identified above have been eliminated. Poland needs the fundamentals of a dedicated, well-educated, career civil service, transparent remuneration, efficient governance and financial management mechanisms including controls based on inputs, and minimization of discretion and political interference in procurement and appointment procedures. These fundamentals do not preclude – and in fact are pre-conditions for – an effective focus on management by results. But, given the risks associated with managerial discretion and power over contracts, it will be advisable to establish centralized controls and financial management before further devolution and delegation are attempted. The implementation of the new Civil Service Act now underway is a positive beginning to the transformation of the state that is needed.

100. Development of the *new career Civil Service* under this Act will help to bring much-needed stability, enabling a build-up of critical expertise. At present, political appointments down to low levels destabilize the service, undermining continuity and the development of standards, institutional values and memory, and opening the way to conflict of interest, misprocurement and theft of public funds. Another source of

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<sup>40</sup> See Annex 1.

instability and insecurity is the short term nature of many appointments and the lack of a clear career path.

101. *Pay reform* should be a high priority. Pay differentials which appear unrelated to the responsibilities or complexity of the task or to its importance in State structures, and the lack of a well defined structure of pay and incentives, are a hindrance to attracting and retaining high quality staff and undermine the development of a career service. In many cases, low pay also creates incentives for corruption. A new pay structure should minimize bonuses and ad hoc allowances that have grown up as short-term responses to the deficiencies of the pay structure, incorporating them into a transparent broad-banded pay scale that would be associated with clear criteria for pay rates for different occupations and skills and for promotions. Introducing such a pay reform would require that job descriptions and competences needed for specific jobs would have to be defined.

102. While higher pay is unlikely on its own to reduce corruption, it would be an important part of an integrated package designed to strengthen professionalism, efficiency and transparency in public service.

103. On a large scale, pay levels could not be raised within budget ceilings without significant *streamlining of functions* and slimming down overstaffing in some areas of the public service. While this would be desirable, it cannot be achieved efficiently by arbitrary cuts. Rather it requires analysis of ministerial and agency functions to identify those that can be eliminated, streamlined, or left to the private sector, together with an analysis of jobs required to perform the functions to be retained. This initial stage would need to be followed by consultation and negotiation, and elaboration of an Action Plan to implement the required changes humanely and in a way that would not be too disruptive of the normal functioning of the administration.

104. *Review of governance structures* in ministries and agencies should also be a high priority. There is currently a bias towards private sector structures requiring Presidents, Vice-Presidents, and Board members to govern agencies. These structures create an unnecessarily large number of well-paid supervisory jobs which can serve to multiply political contacts and affiliations while muddying the lines of policy direction and accountability between the parent ministry and the agency. There is also a small but important category of agencies which should not be subject to political direction and whose independent functioning needs to be safeguarded, such as the Committee on Statistics. These agencies need separate statutory protection, elimination of party political appointments, professional management, and freedom from political interference.

105. *Financial management* is another high priority area. The Government needs to have access to up to date public sector financial statistics that will enable it to monitor expenditures and other financial transactions and create a basis for checking whether the public sector is achieving value for money. The quality of budget analysis will need to be raised so that policy proposals can be more accurately costed. Plans are now well in hand to institute a single Treasury account. This will improve control and monitoring capacity, but if this reform is to be fully effective it will need to be accompanied by standardized accounting procedures and transparent financial management practices throughout ministries and agencies. As noted above, extra-budgetary funds should be

integrated into the budget, with a minimum of exceptions. Special regulations and supervisory procedures will be needed to control agencies that are permitted to lend and borrow.

106. *Control and audit capacity* will need to be upgraded. Ministries will need to strengthen their own internal control and audit, and there is also a case in the very short term for raising the pay scale for internal auditors (their present pay levels are reportedly unlikely to attract anyone with an accounting qualification). However, this cannot be a substitute for external audit. NIK's reports provide a valuable service to Poland, and it would be useful to review ways in which its role and capacity could be strengthened, in particular to cover the SOE sector and extra-budgetary funds more closely and to respond to the demands created by the health sector reform and the territorial reform. It may possibly be worth considering whether its work program should be determined independently of Parliament, and to enquire into the low response rate to its reports, whether by prosecutors, Parliament, or other responsible public bodies. Strengthening of NIK capacity will also require staff development and training. Consideration should also be given to developing a capacity to review overall probity and effectiveness in the public administration, rather than compliance audit in the narrow sense. This function could be placed with NIK or in a separate public organization created to watch over the integrity and efficiency of state institutions.

107. The role of the Office of Civil Service will be an important one in developing *human resource management* and in supporting and guiding public administration reforms. In addition, the National School of Public Administration could be asked to help strengthen ethics and professionalism beyond the students in its current scope, introduce a new culture of public service and also transparent procedures – such as the use of the written record, instead of unwritten “understandings”. At present, the School's graduates appear to be pepper-potted through the administration, and although a few head key public sector bodies, they do not appear to create a critical mass in any area, which generally means that the existing organizational culture remains dominant. The School could be asked to cooperate with the Office of Civil Service in providing manuals and guidance on administrative procedure, and in organizing workshops on relevant topics. It would also be useful to extend the Parliamentary Ethics Committee concept to ministries, agencies and subnational governments, and to introduce an enforceable administrative procedure code.

## **V INITIAL PROPOSALS FOR A PROGRAM TO PREVENT AND REDUCE CORRUPTION**

108. We hope that this analysis and the scan of priority areas to tackle corruption in Poland will provide the starting point for a strategy that can produce results and generate confidence that change is possible. Given the significance of high level corruption in Poland and the apparently deeply entrenched cynicism of the population a broad-based approach will be needed which demonstrates enough cooperation among elites to indicate that reality and not only rhetoric will change. The identification of an anti-corruption strategy with any one political party is likely to provoke accusations of score-settling and will not be wholly credible.

109. For these reasons, we recommend that the next step should be **to convene a small group of leaders in their fields**, drawn from a range of state bodies and political parties, who could together review the evidence of corruption, and draw up an initial strategy and program. Some of our respondents could be helpful members of this group.

110. In determining the strategy it may be useful to bear in mind that it is not always practical to tackle the worst areas first. It can be more important to identify committed leaders in areas where practical results can be achieved, creating demonstration effects and raising the credibility of the anti-corruption program before more challenging areas of the program are tackled. Given the perceived significance of high level corruption, it will also be important to include in the program some measures designed to tackle problems in this area. The form that this should take is a judgement that should be made by others, however.

111. Some of the sources of corruption could be tackled by technical improvements in various laws and administrative and financial mechanisms, and these should be set in motion immediately. They include, for instance, introduction of laws on political party financing and on lobbying and registration of lobbyists; acceleration and effective implementation of an improved procurement law; strengthening of the law on conflict of interest, financial disclosure and receipt of gifts by state officials; review of the legal framework covering corruption offences (which is currently too narrow); passage of the new Law on Economic Activity; a Law on Freedom of Information; and improvements in financial oversight of SOEs and extra-budgetary funds. Other examples can be found in the text.

112. However, a technical approach on its own will be of limited use if it is not accompanied by strong leadership and commitment to results. It is well-known that even the most precise law or apparently watertight procedures can be circumvented unless there is a will and drive to make them work.

### **Role of civil society**

113. Anti-corruption efforts will be more effective if they involve civil society, including those on the receiving end of the services concerned, whether businesses or individuals. With their assistance it will be important to establish priorities and modes of operation. And it will also be important to tackle public apathy if anti-corruption efforts are to have any credibility and command the support they need to be successful.

114. Once the strategy proposal is defined, a public conference could be convened to discuss it and ask for the input of a wider group including business, churches, NGOs, professional associations, media and the academic community. This would identify corruption as a mainstream public concern, provide important information on the nature and costs of corruption to the economy and society, and help frame priorities for the strategy. In the light of the conference findings, the strategy would be revised and a program and timetable of action drawn up.

**Resources for implementation of the anti-corruption strategy**

115. If the strategy and program are to be credible it will be important to allocate resources, identify administrative and other support that would be crucial to implementation, and to set up a monitoring mechanism. The group may also wish to consider commissioning surveys to identify priorities more closely or to examine particular sectors in more depth. Finally, an effective communications strategy will be crucial. For this, it would be helpful to involve interested members of the media in the conference and in the ensuing work on the program.

116. The World Bank would be able to supply examples of cross-country experience, program components, and technical support that could be useful for administrative reforms and reforms in such areas as the courts and judiciary, regulatory process, licensing and inspections, procurement, budget management, service delivery; and technical support for surveys and civil society monitoring.

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## GLOSSARY

**Corruption** - the abuse of public office for private gain. It includes paid favoritism, nepotism, cronyism, abuse of function to gain an advantage, bribery, trading in influence, theft of public assets or public funds, bookkeeping offences, laundering money derived from corruption activities.

**Conflict of interest** - a conflict between the private interest and the official responsibilities of a person in a position of trust

**Favoritism** - giving an unfair advantage to a person for private gain or other favors

**Nepotism** - favoritism based on kinship

**Cronyism** - favoritism based on informal networks

**Money laundering** - transferring illegally obtained money or investments through an outside party to conceal the true source

**Self-government** – an elected subnational government at regional, county or municipal level.

## ANNEXES

- Annex 1 Analysis of public administration staffing and pay
- Annex 2 Note on extra-budgetary funds
- Annex 3 WDR 97 cross-country survey of entrepreneurs

# **ANNEX 1**

## **Analysis of public administration staffing and pay**

### **Employment**

The employment of civil servants (both elected and those employed at all levels of the administration) increased by 24.5 percent from 282,700 in 1994 to 352,000 in 1998. Employment in state and local administration increased by 25.1 percent from 230,200 in 1994 to 287,900 in 1998.

#### **Elected civil servants.**

Since 1989 in Poland there are 460 Members of the Lower House of the Parliament – the Sejm and 100 Senators. The number of gmina councilors declined from 52,037 in 1990, when the first local elections were held, to 51,926 in 1994 and 49,458 in 1998. In 1998, however, the administration reform created two new levels of elected sub-national administrations – powiat and voivodship. The number of voivodship parliamentarians amounts to 855 people, while on the powiat level there are 10,290 councilors and 2,921 city-powiat councilors. The aggregate number of 1998 elected civil servants amounts to 63,524 people, some 11,600 or 22.3 percent more than in 1994.

#### **State administration.**

Employment in state administration rose 48.4 percent in five years (from 115,400 in 1993 to 171,200 in 1998). Employment in central state administration increased from 88,600 to 126,200 in the respective period. The fastest increases in employment (by 67.9 percent) occurred in territorial bodies of general government administration (voivodship and local offices, auxiliary servicing institutions) from 26,800 to 45,000.

#### **Territorial self government administration.**

Employment in local self-government administration has risen much more moderately over the course of last five years, growing from 96,800 in 1994 to 116,700 in 1998 (by 20.6 percent). The fastest increases in employment occurred in urban areas, the slowest in mixed urban-rural ones.

### **Level of wages and salaries.**

In the period 1994-1998 the average level of wages and salaries in administration (at all levels) was approximately 30% higher than the national average. The level of wages and salaries was the highest in urban local administration. In 1994 it exceeded the national average by 67 percent, in 1998 by 109.6 percent. During 1995-1998, administration wages and salaries rose on average annually in real terms (CPI deflated) by 5.4 percent (cumulative increase 23.6 percent), while the national average rose by 4.8 percent (cumulatively 20.4 percent). The highest increases occurred for employees (not councilors) at the local level of administration, especially in urban areas, as well as in self-government regional councils.

## **Costs of employment in administration (wages and wages related costs)**

Wages and wage-related costs (Social Security and Labor Fund contributions represent 48.5% of gross wages) of the administration have risen due to increases in employment, as well as increases in wage and salary levels. In 1994 total administration wage costs amounted to 2.76 billion PLN, in 1998 8.41 billion PLN. (Subtracting tax revenues from PIT the costs amounted to 2.26 billion PLN and respectively 6.89 billion PLN). Between 1995 and 1998 they rose (cumulatively) in real terms by 54.5 percent (cumulative real GDP growth in the respective period amounted to 26.9 percent). The highest increase occurred in local administration – 60.3 percent, especially in urban areas. In central administration it amounted to 46.8 percent.

### ***Tailpiece:***

*Rising employment in the administration may soon become a problem. In order to analyze this more deeply and identify which institutions are especially overstaffed, more detailed data on functions and employment would be necessary. The costs of administration are rising very fast (due to increases in employment and wages), which means that, while budgets shrink, administration becomes a higher and higher portion of expenditure.*

## ANNEX 2

### Note on extra-budgetary funds

#### Size of public finances

Between 1993 and 1998, revenues declined from 47.6 percent of GDP to 41.4 percent and expenditure from nearly 50 to 43.9 percent. The size of central budget revenues declined in the same period from 29.5 percent of GDP to 23.2 percent (expenditure from 32.3 to 25.4 percent). Revenues of extra-budgetary funds shrank from 22.2 percent of GDP in 1993 to 17.4 percent in 1998, and the portion of central budget subsidies in these revenues declined from 7.7 percent to 3.8 percent of GDP. The only part of public finances whose share in GDP has been constantly growing were local budgets (until 1998 these referred only to gminas) – revenues from 6.2 percent to 8.4 percent and expenditure from 6.2 percent to 8.6 percent. The share of central budget subsidies in local government revenues also increased from 3.3 percent of GDP in 1993 to 5.3 percent in 1998.

#### Extra-budgetary funds

The size of extra-budgetary funds in GDP shrank in line with the general reduction of public finances relative to GDP, but their share in total public finances remained at approximately 30 percent (in terms of revenues, excluding central budget subsidies) or 38-41 percent (in terms of expenditure). In 1998 the total revenues of funds exceeded 96 billion PLN (central budget subsidy – 21 billion), while expenditures were well above 92 billion PLN.

The three biggest extra-budgetary funds (FUS – the Social Security Fund, KRUS – the Farmers' Social Security and the Labor Fund) constituted between 1993 and 1998 around 95-99 percent of the total extra-budgetary funds' size (in terms of revenues, share of central budget subsidies in total revenues and expenditure). The improvement on the labor market in 1993-1997 enabled central budget subsidies for FUS to be reduced from 55.3 percent of total subsidies for extra-budgetary funds to 34.3 percent (in 1998 the share increased again to 41.8 percent). By contrast the Farmers' Social Security KRUS consumed growing subsidy financing from 25.8 percent (of total subsidies for funds) in 1993 to 50.7 percent in 1998.

The next two funds in terms of size are PFRON (Disabled Rehabilitation Fund) and NFOŚ (Environment Protection Fund). Neither receive central budget subsidies (both of them recorded highly positive balances - especially NFOŚ, whose year-end balances constituted 52-62 percent of revenues in the 1995-98 period). Their cumulative share in total funds revenue grew from 2.8 percent in 1995 to 3.2 percent in 1998, while their expenditure increased in the same period from 1.7 percent to 2.2 percent.

#### Financial condition of funds as of end of 1998

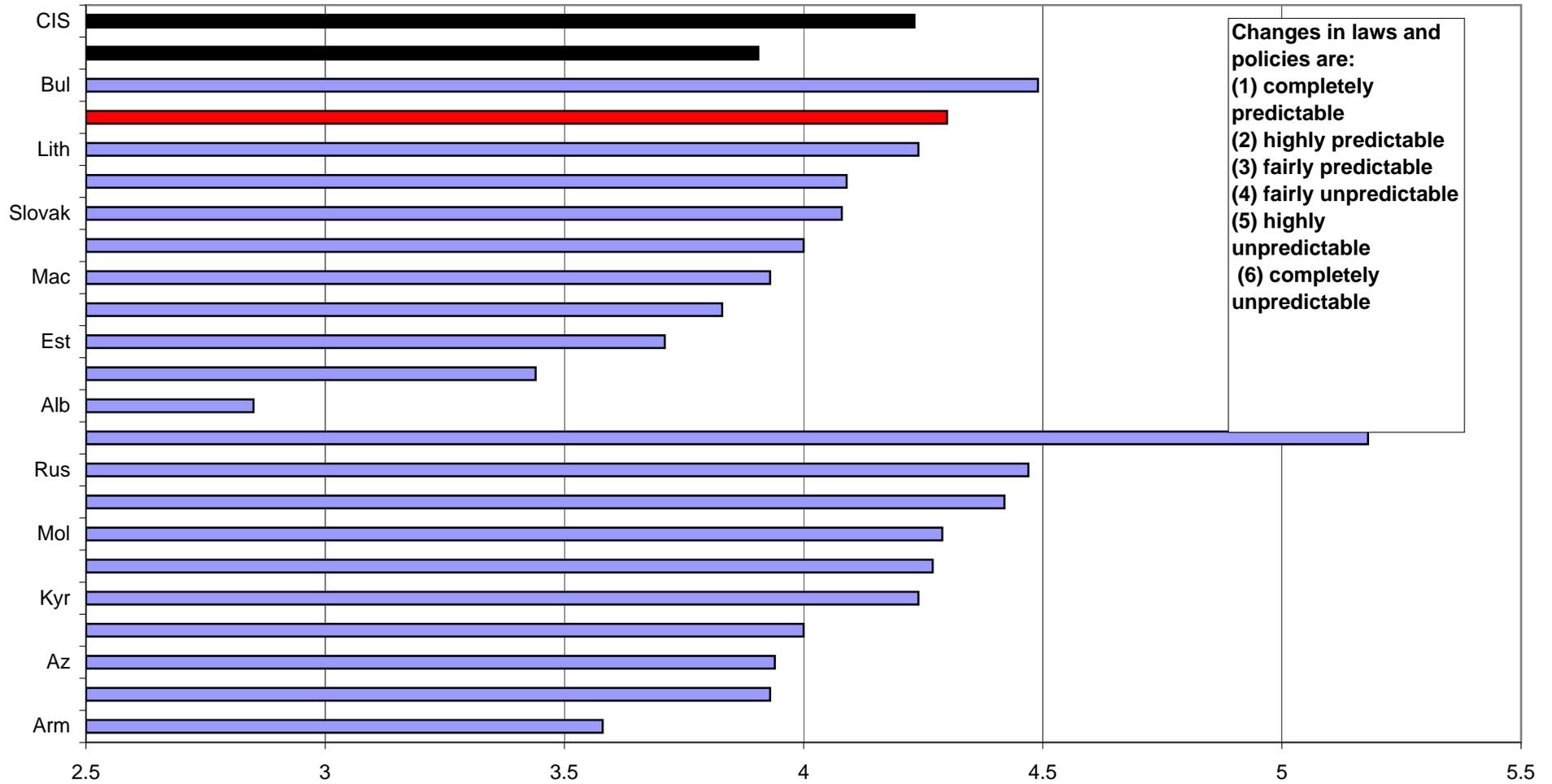
In 1998 extra-budgetary funds recorded a surplus of approximately 3.9 billion PLN (FUS – 1.76 bn PLN, Labor Fund – 303 m PLN, PFRON- 317 m PLN, NFOŚ – 757 m PLN). However arrears of unpaid contributions to FUS amounted in 1998 8.32 billion PLN. Floating capital amounted to 8.15 billion PLN and was constituted of 133.6 million PLN cash (on deposits), 10.24 billion PLN of claims (resulting from arrears) and 2.24 billion of liabilities. Floating capital of the Labor fund amounted to 1.04 billion PLN (including 530.2 m PLN cash, 386.2 m PLN claims on granted loans, 186.3 m PLN shares in the corporate sector and 97.6 m PLN of liabilities). Floating capital of PFRON amounted to 1.07 billion PLN (including 76.6 m PLN cash, 265.8 m PLN State Treasuries, and 330.5 m PLN claims on granted loans).

#### Tailpiece: Claims on granted loans

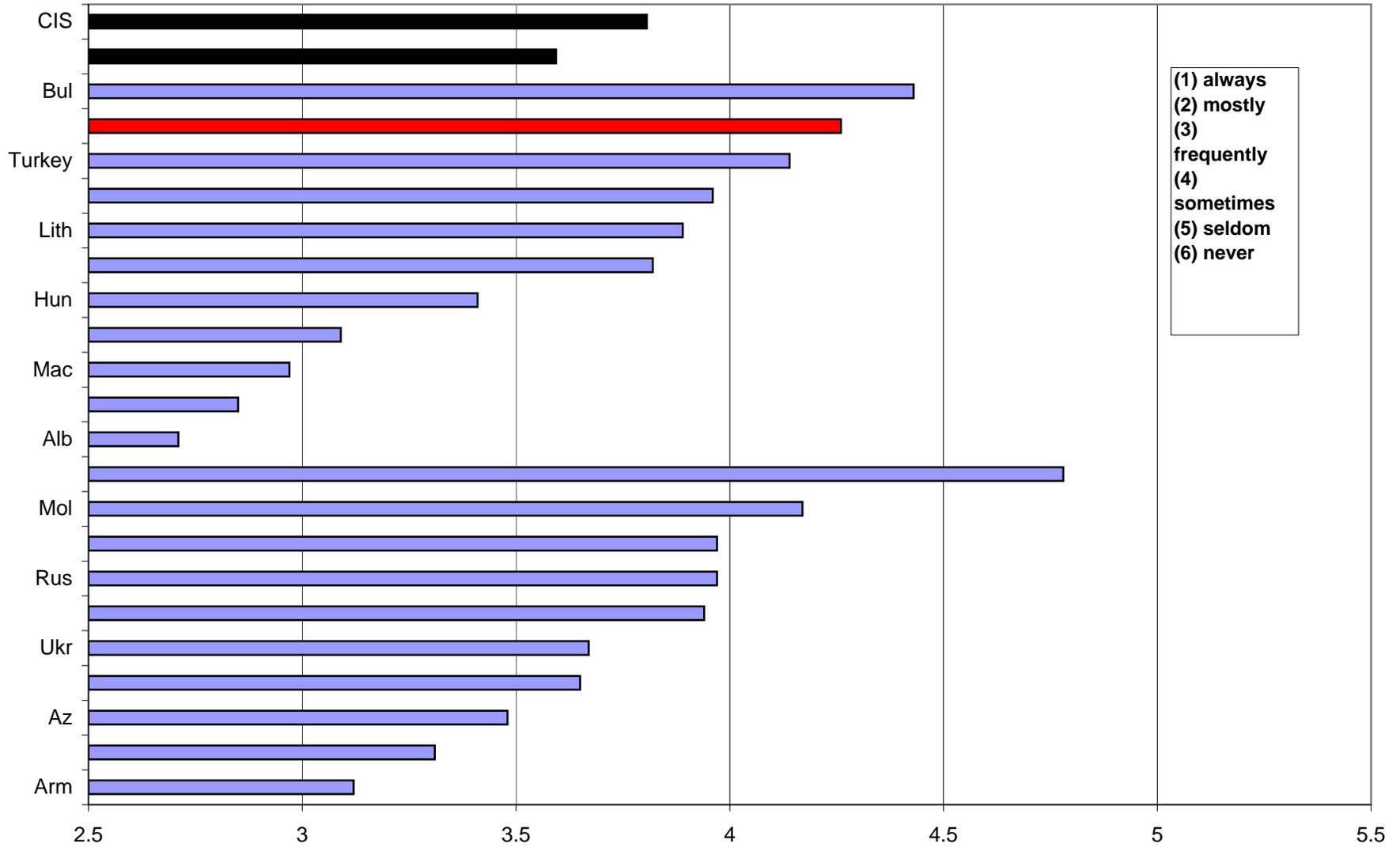
Claims on granted loans represent a significant portion of floating capital of Labor Fund – 37.2 percent, PFRON – 31 percent and especially NFOŚ – 72.8 percent (cumulatively they amount to 3.43 billion PLN). Questions arise on the quality of these loans and lending procedures and the extent to which they are subject to prudential regulations and supervision; and the extent to which extra-budgetary funds are subject to audit in procedural and performance terms as well as legal compliance. Further analysis of the governance and financial management of extra-budgetary funds appears to be warranted.

## **ANNEX 3**

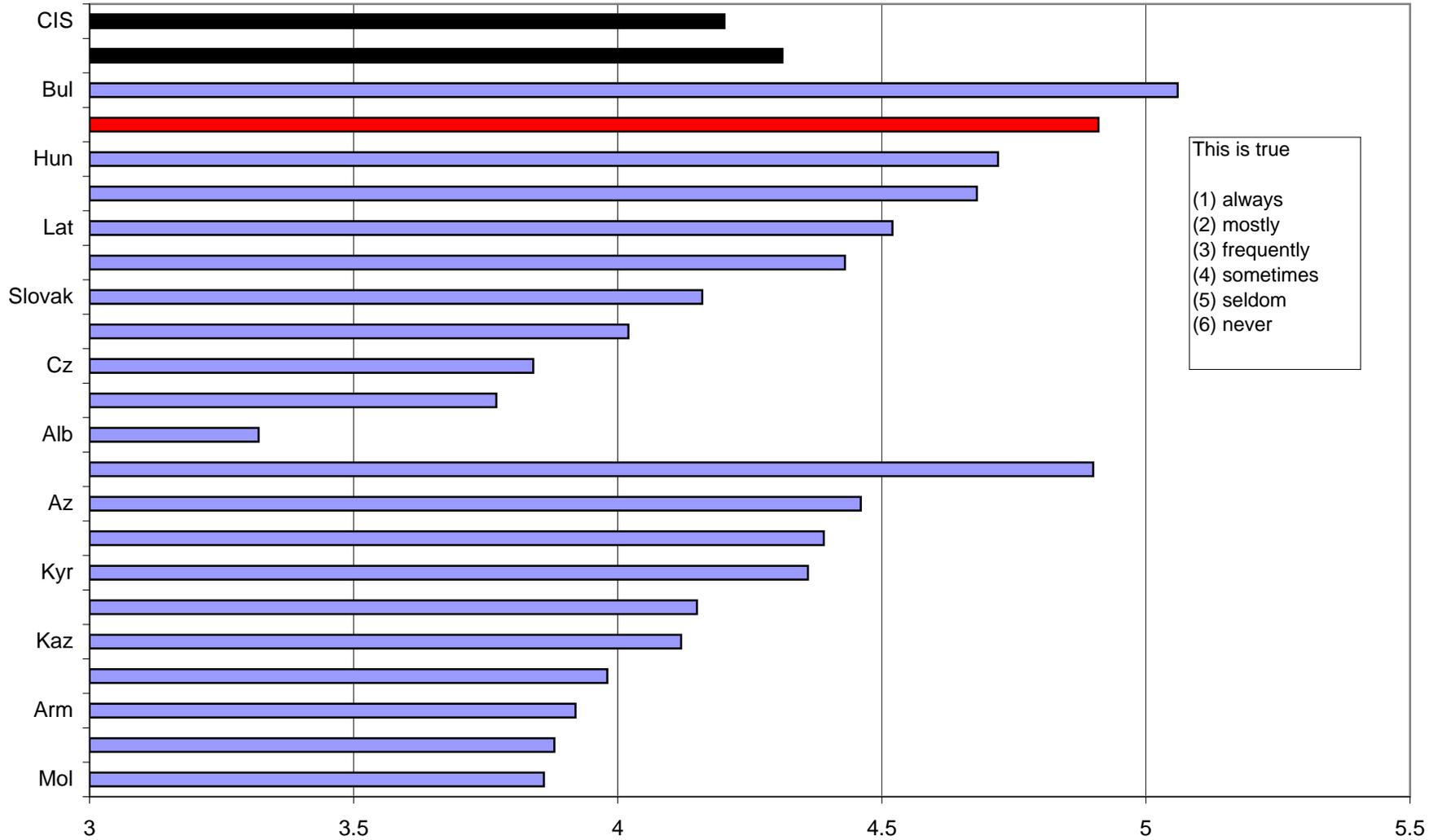
**Do you regularly have to cope with unexpected changes in rules, laws and policies which materially affect your business?**



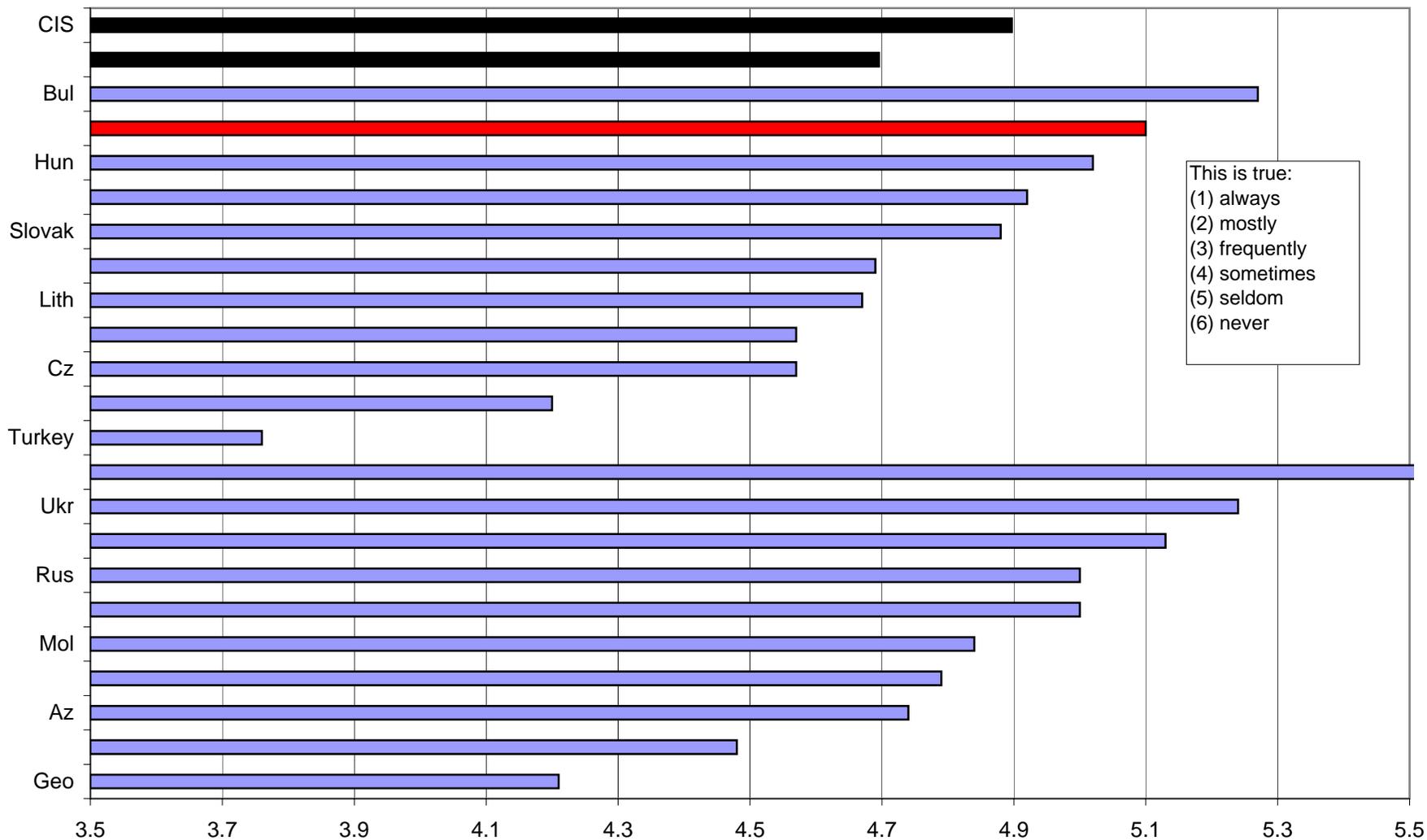
### Do you expect the government to stick to announced major policies?



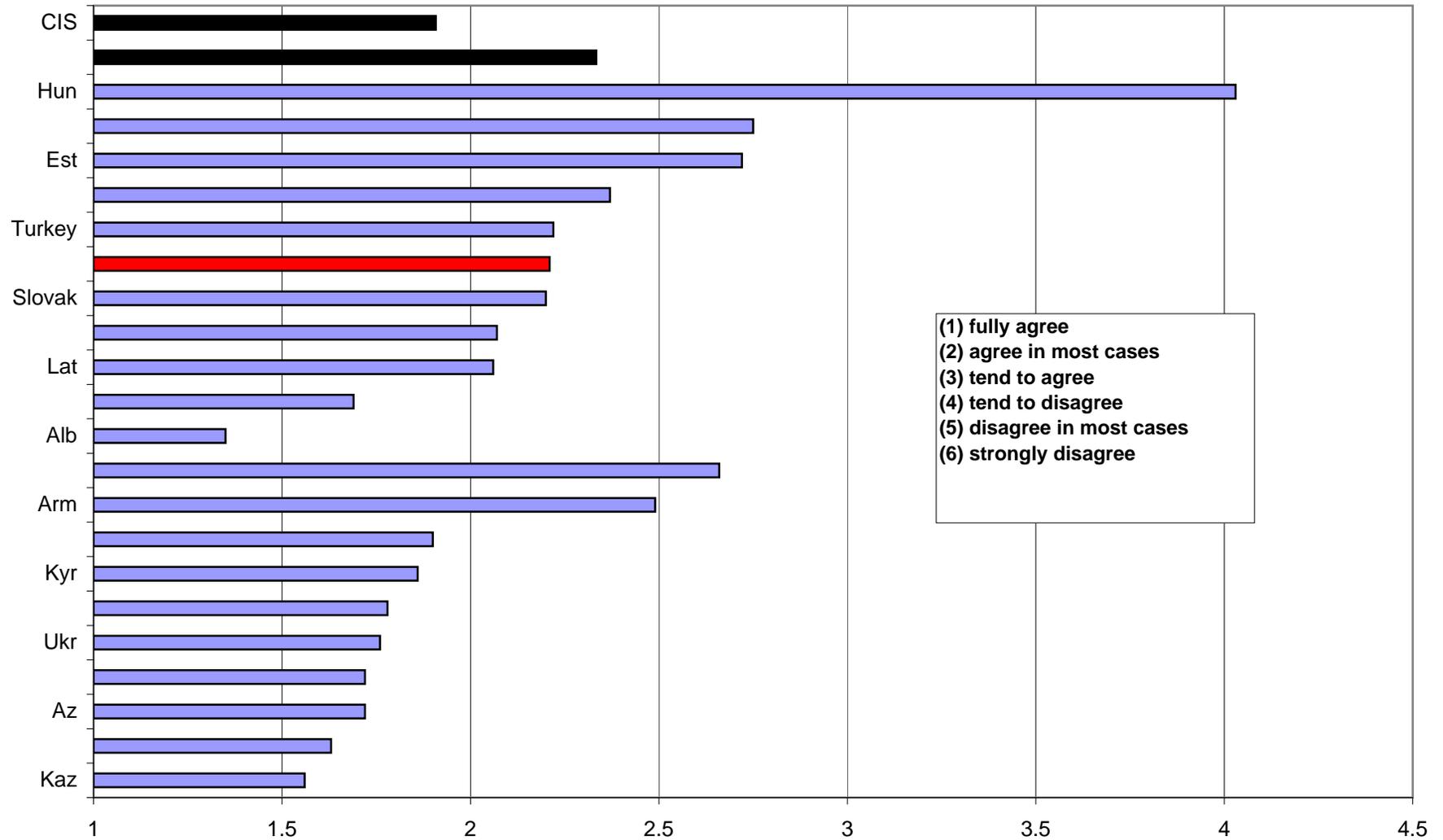
**"The process of developing new rules or policies is usually such that affected businesses are informed"**



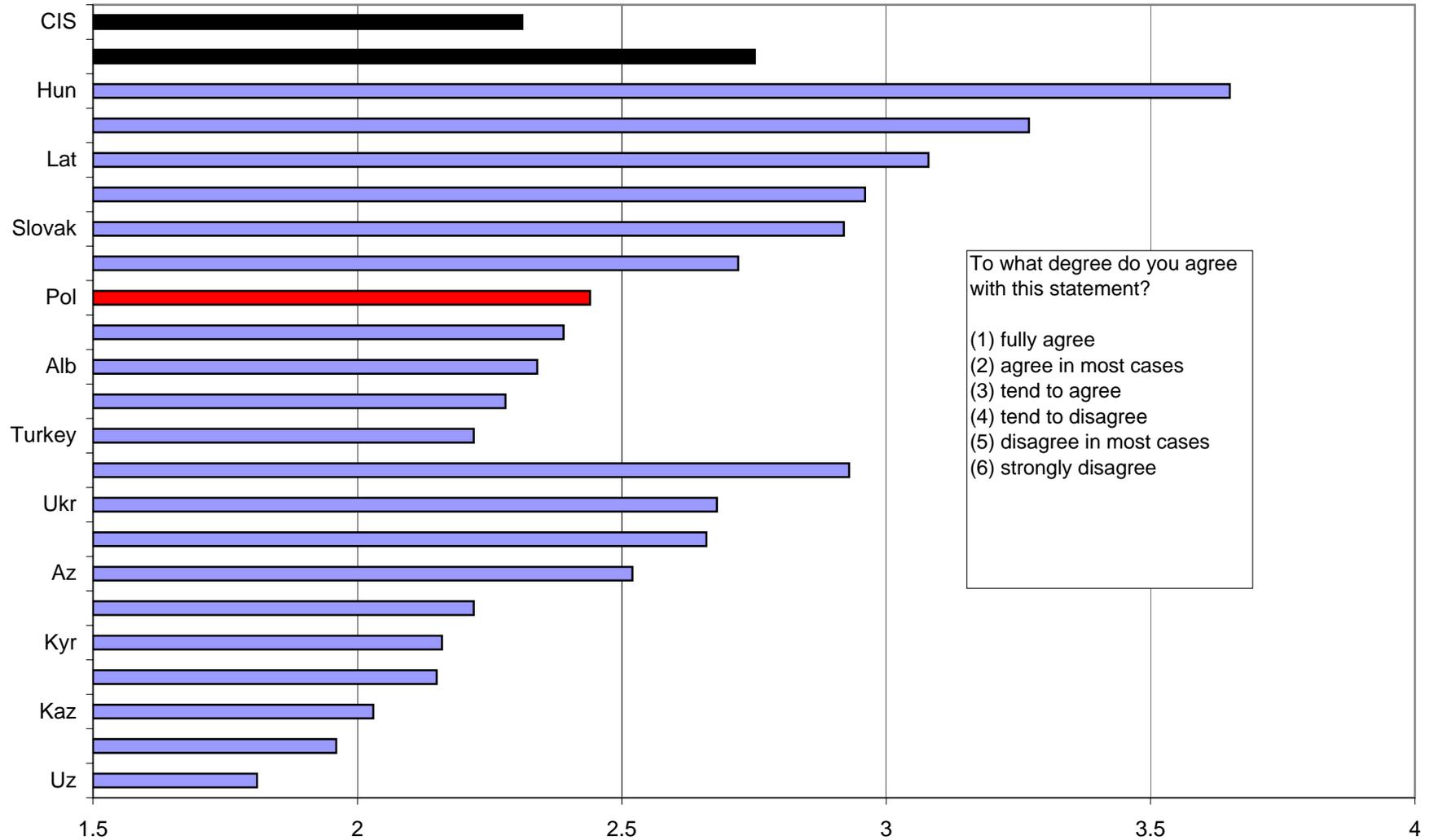
**"In case of important changes in laws or policies affecting my business operation the government takes into account concerns voiced either by me or by my business association"**



**"Theft and crime are serious problems that can substantially increase the costs of doing business" (Now)**



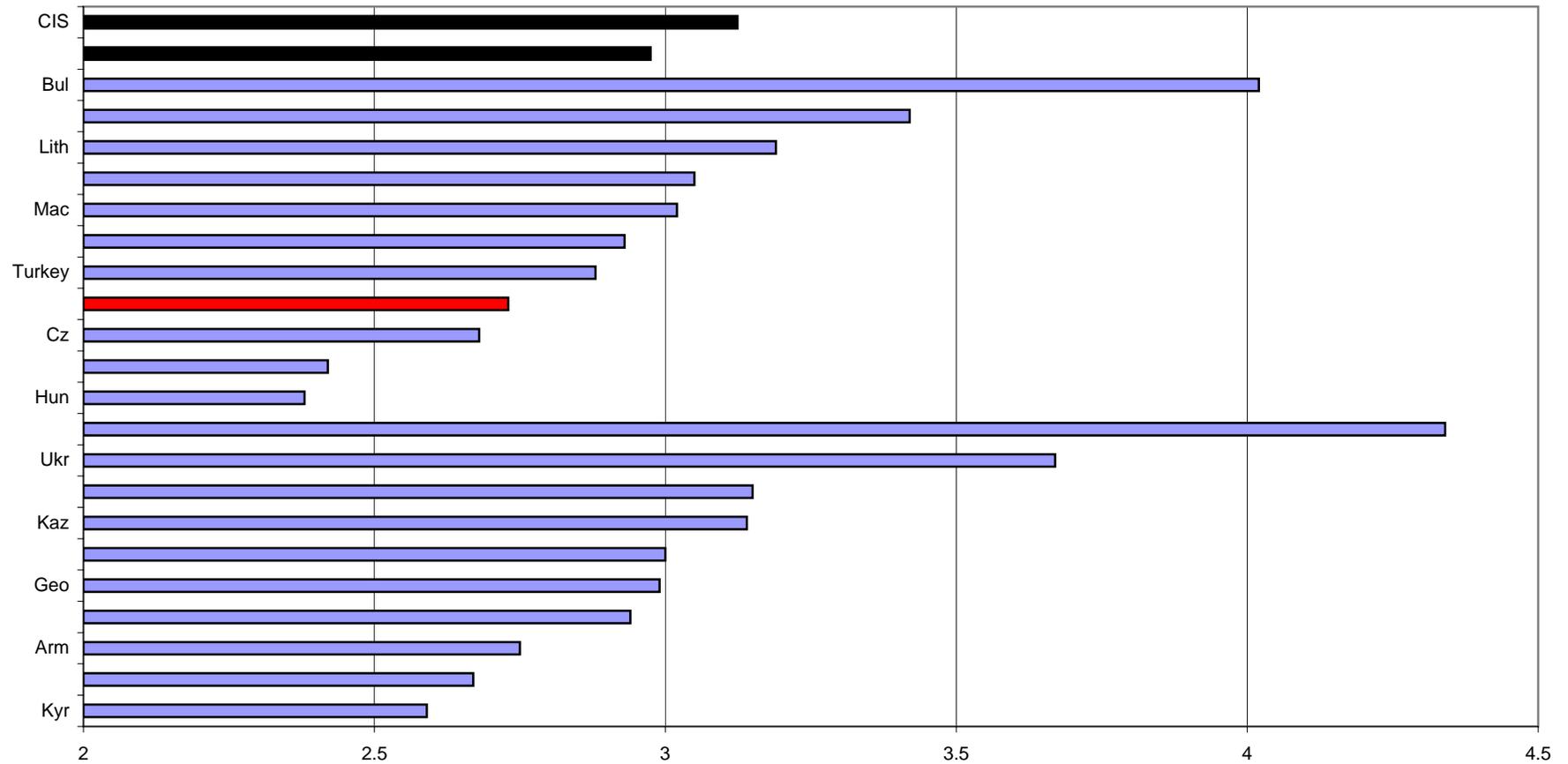
**"Unpredictability of the judiciary presents a major problem for my business operations."  
(Now)**



Please judge on a six point scale how problematic these different policy areas are for doing business

NO  
1 2      Moderate  
3 4      Very strong  
5 6

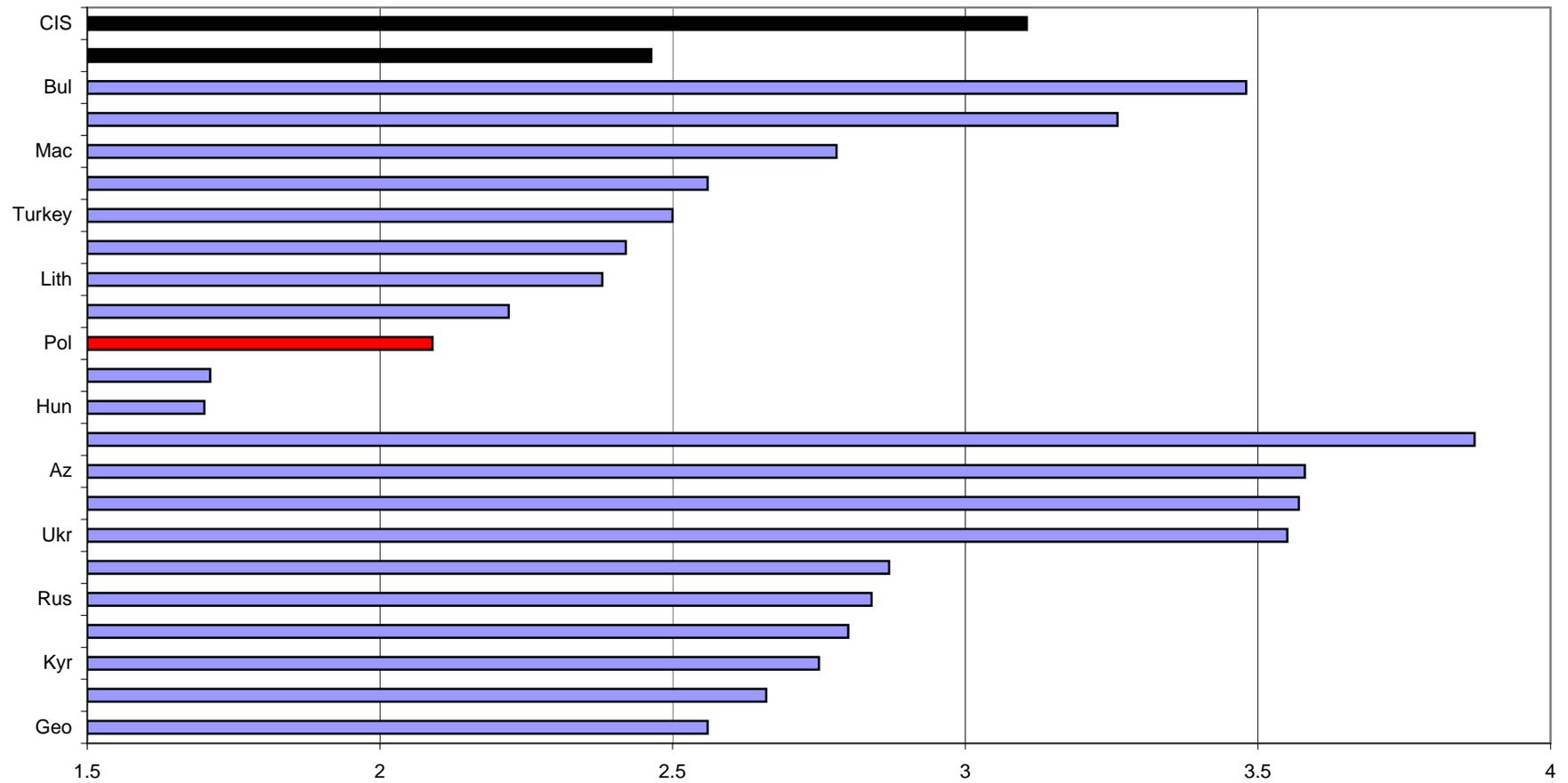
### Regulations for starting business/new operations



Please judge on a six point scale how problematic these different policy areas are for doing business

NO  
1 2      Moderate  
3 4      Very strong  
5 6

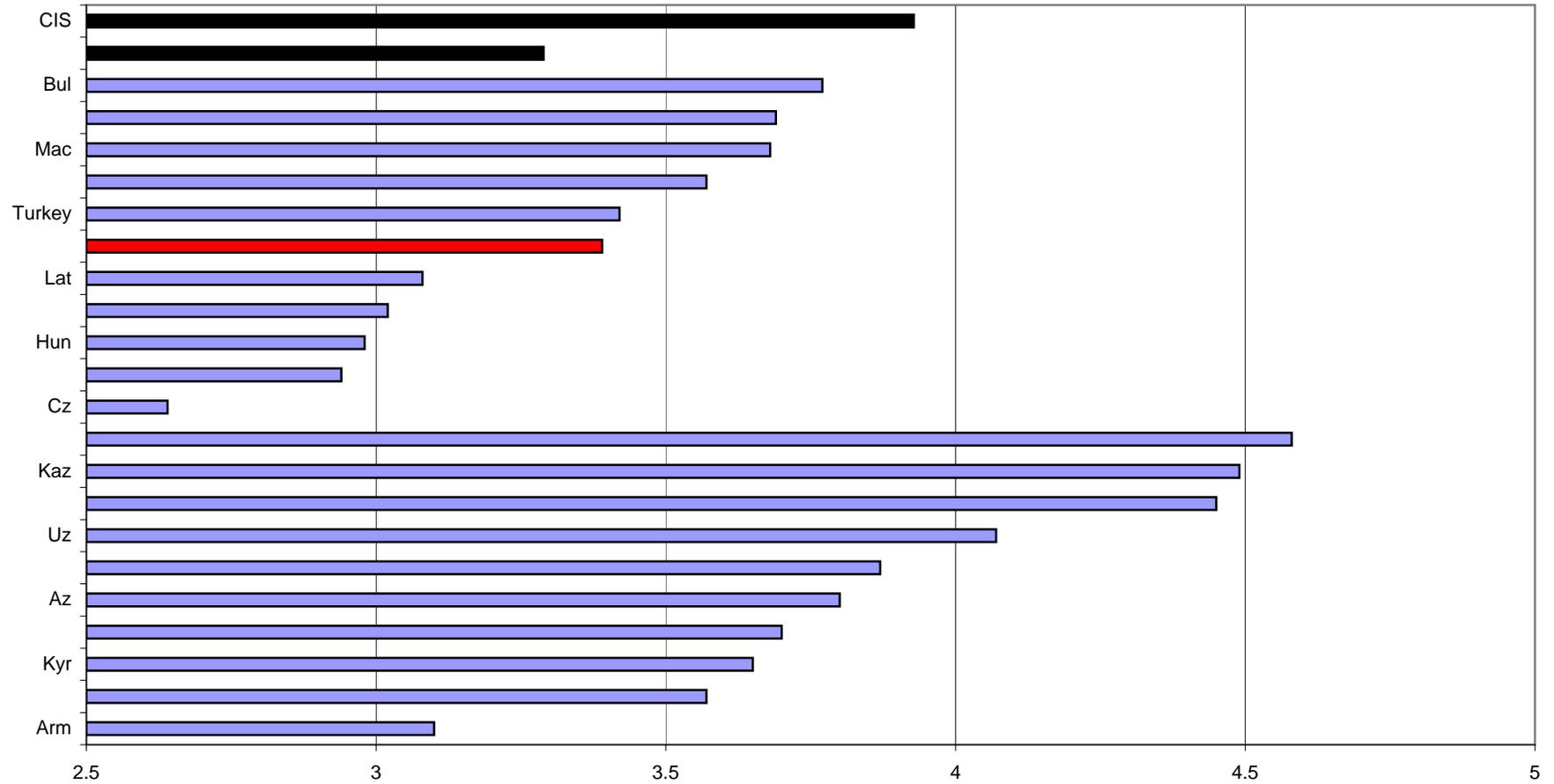
### Price controls



Please judge on a six point scale how problematic these different policy areas are for doing business

NO  
1 2      Moderate  
3 4      Very strong  
5 6

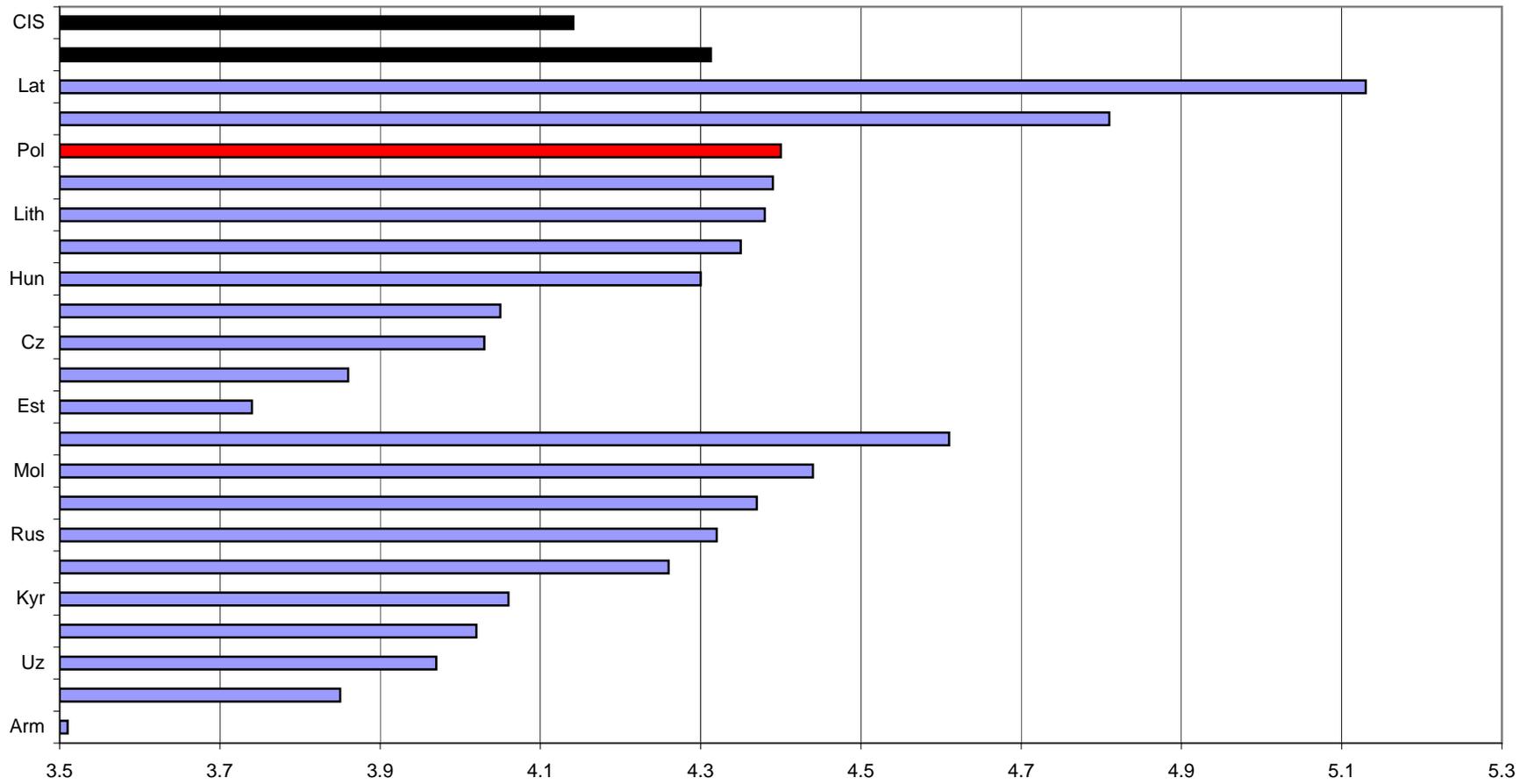
### Regulations on foreign trade (exports, imports)



Please judge on a six point scale how problematic these different policy areas are for doing business

NO  
1 2      Moderate  
3 4      Very strong  
5 6

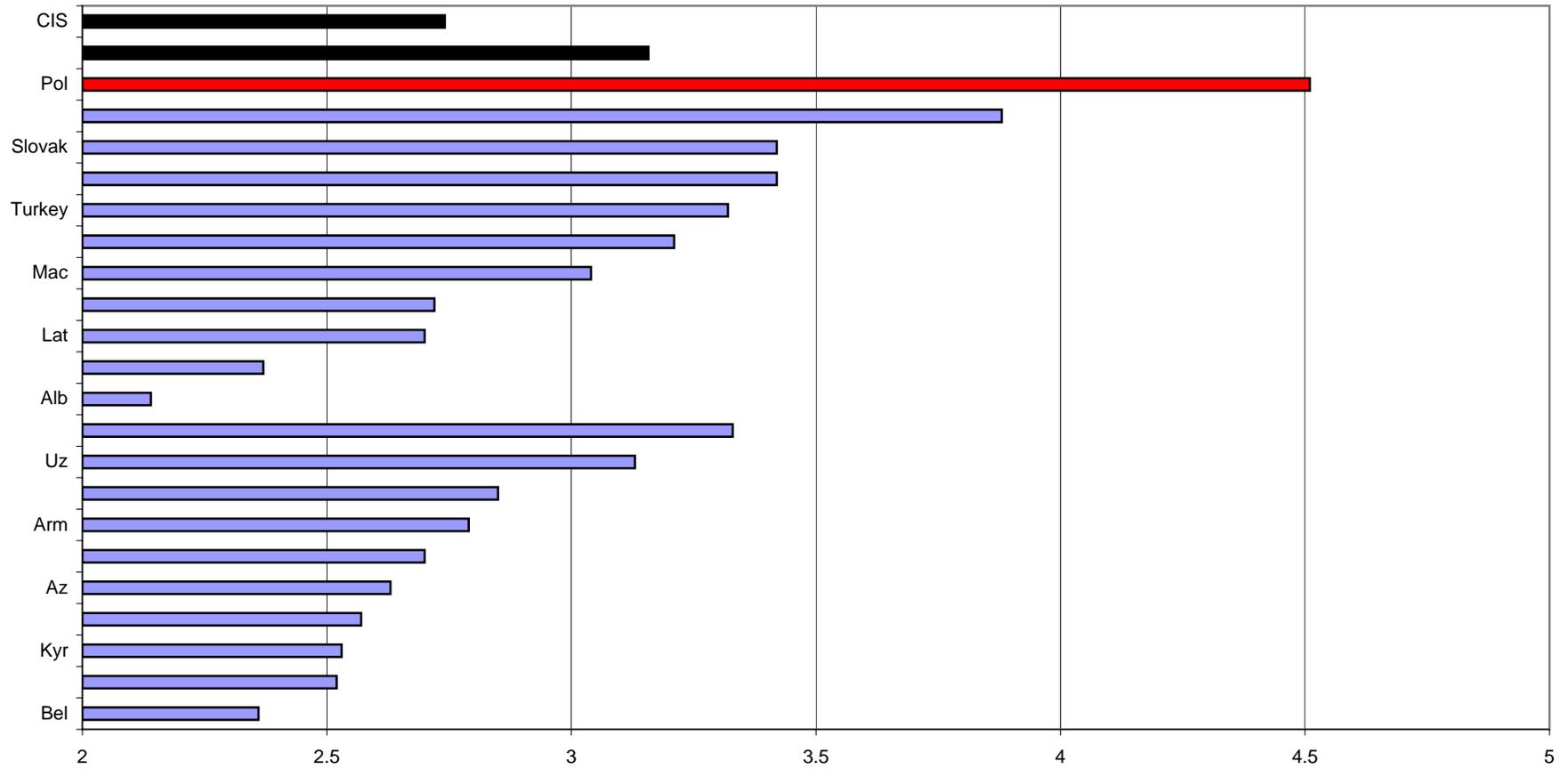
### Financing



Please judge on a six point scale how problematic these different policy areas are for doing business

NO  
1 2      Moderate  
3 4      Very strong  
5 6

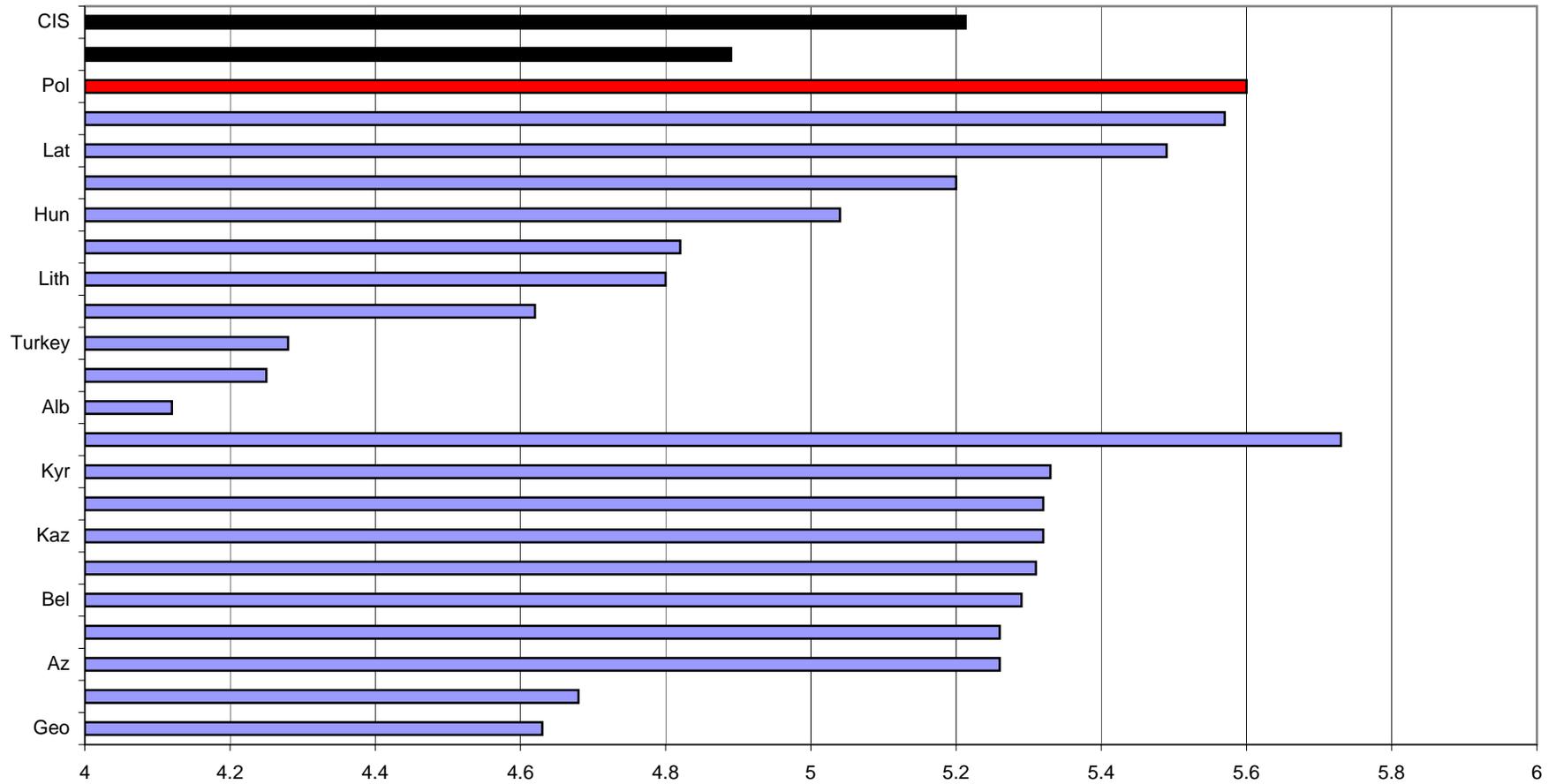
### Labor regulations



Please judge on a six point scale how problematic these different policy areas are for doing business

NO  
1 2      Moderate  
3 4      Very strong  
5 6

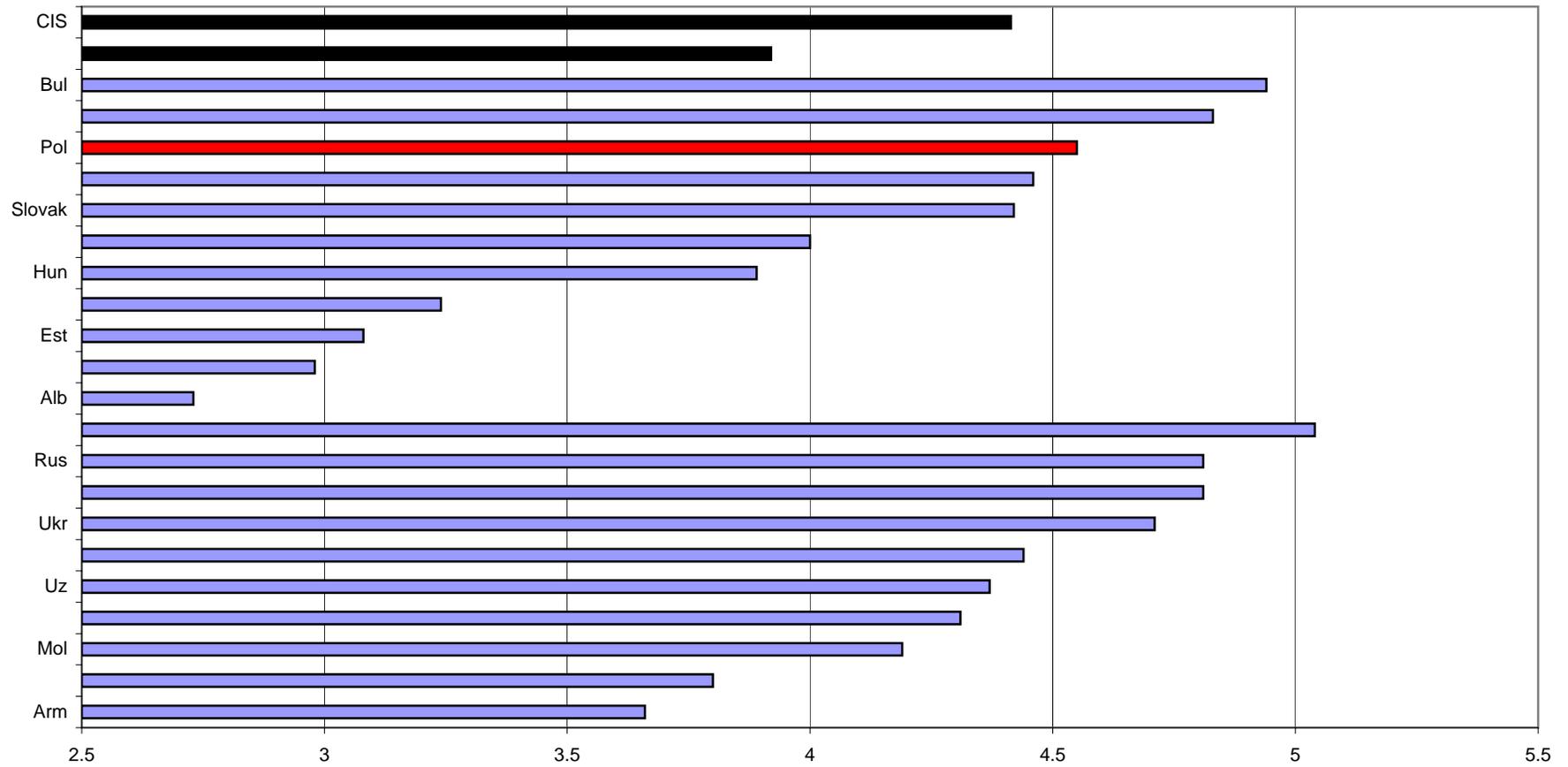
### Tax regulations and/or high taxes



Please judge on a six point scale how problematic these different policy areas are for doing business

NO  
1 2      Moderate  
3 4      Very strong  
5 6

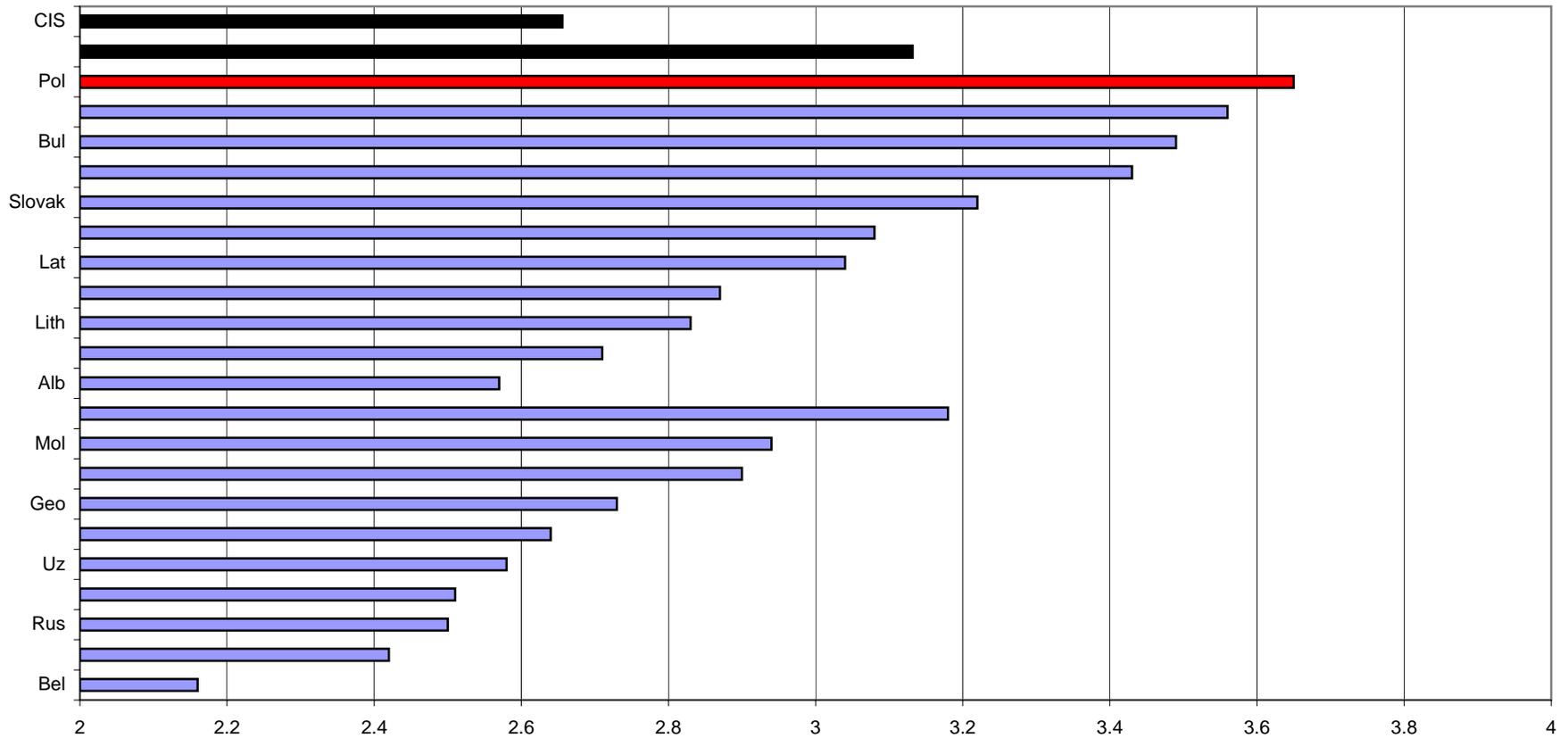
### Policy instability



Please judge on a six point scale how problematic these different policy areas are for doing business

NO  
1 2      Moderate  
3 4      Very strong  
5 6

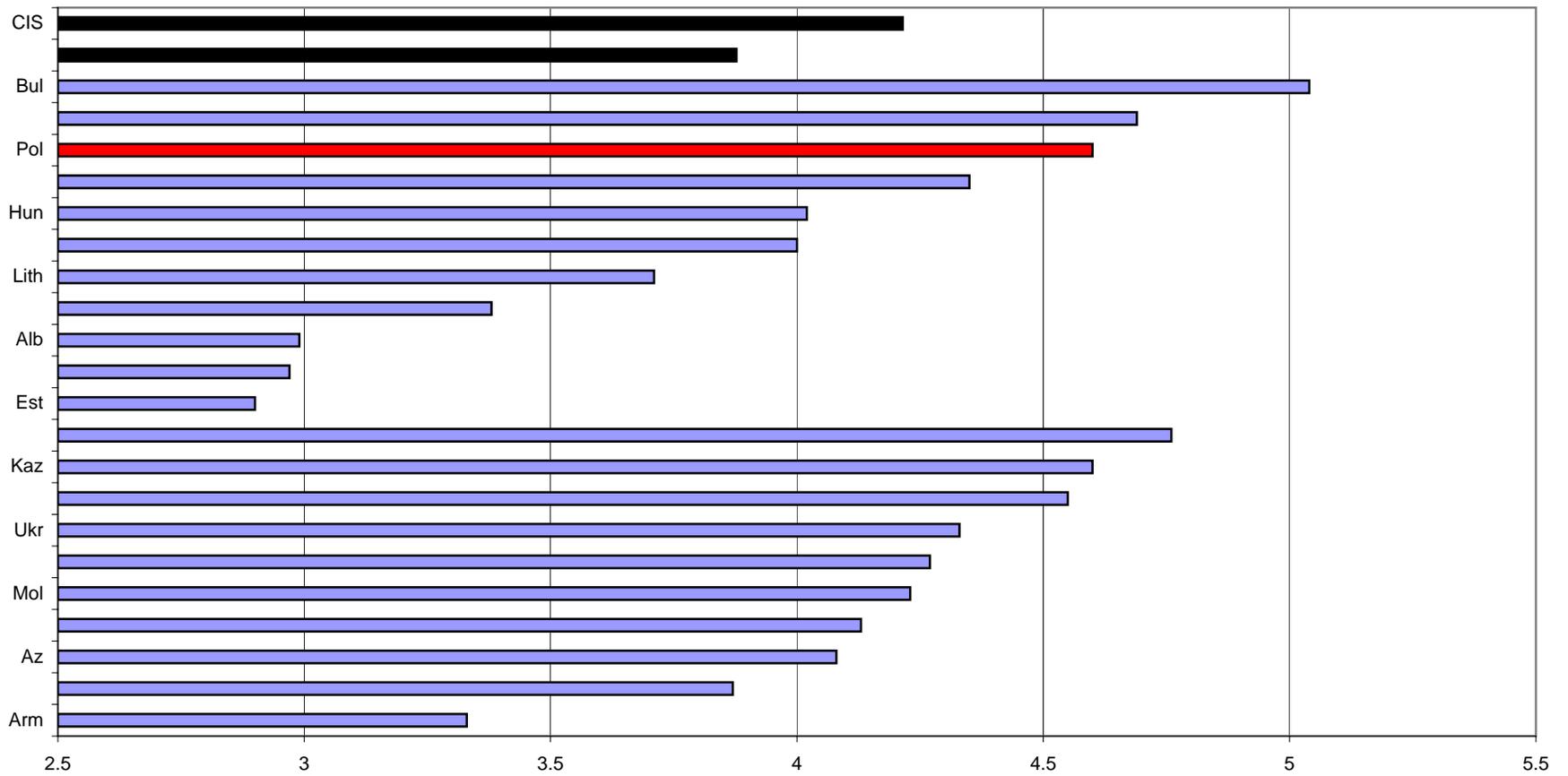
### Safety or environmental regulations



Please judge on a six point scale how problematic these different policy areas are for doing business

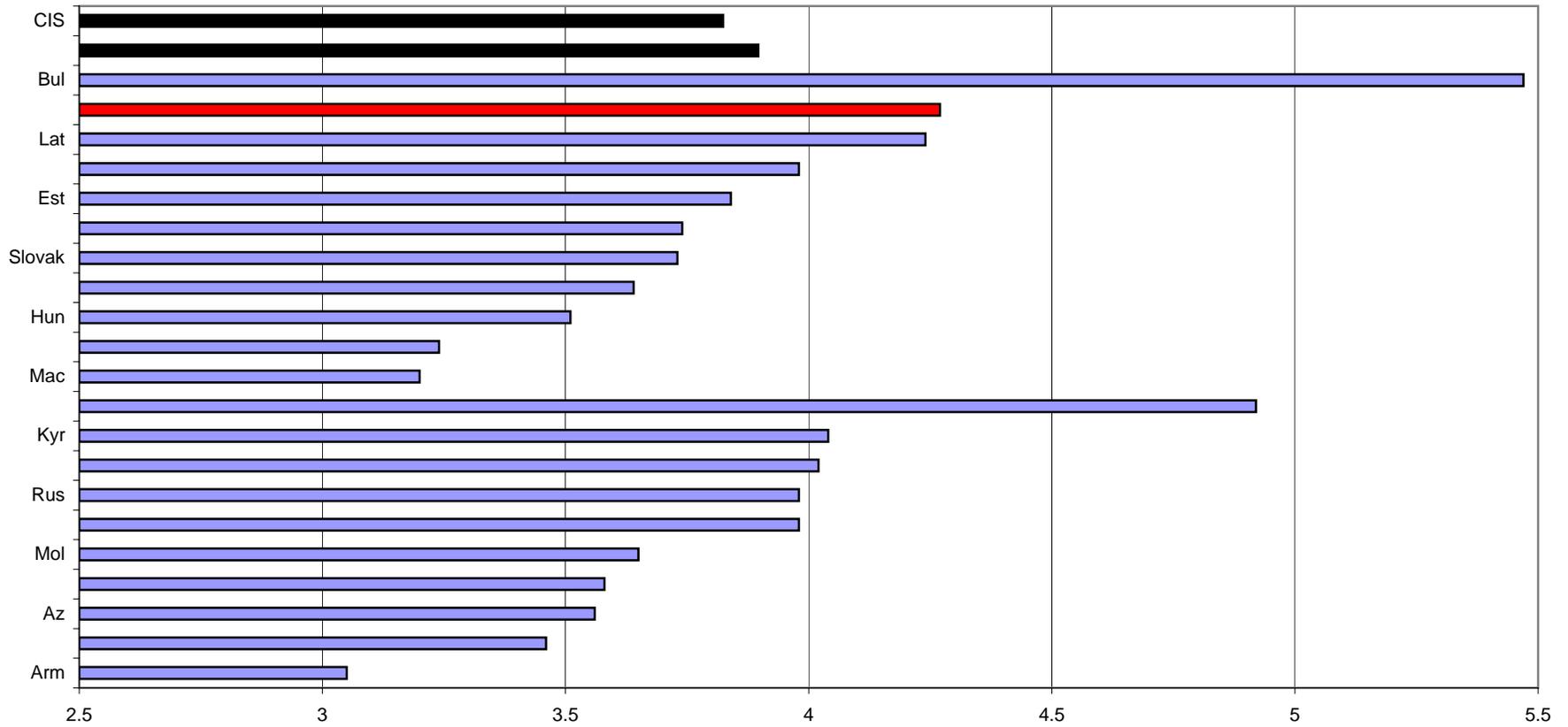
NO  
1 2      Moderate  
3 4      Very strong  
5 6

### General uncertainty on costs of regulations



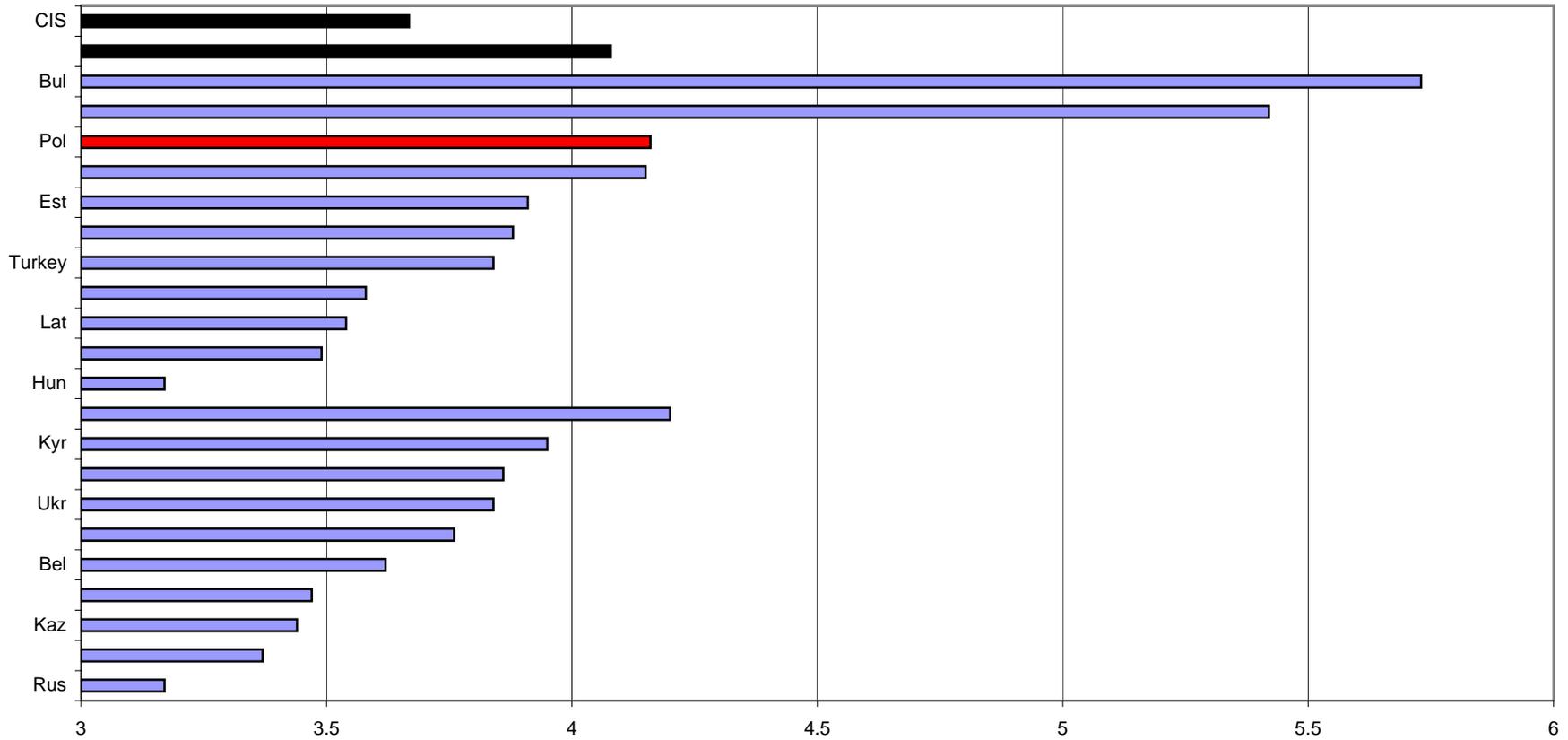
**Please rate your overall perception of the relation between government and/or bureaucracy and private firms on the scale. (Now)**

Helping	Neutral	Opponent
hand	agent	
1 2	3 4	5 6

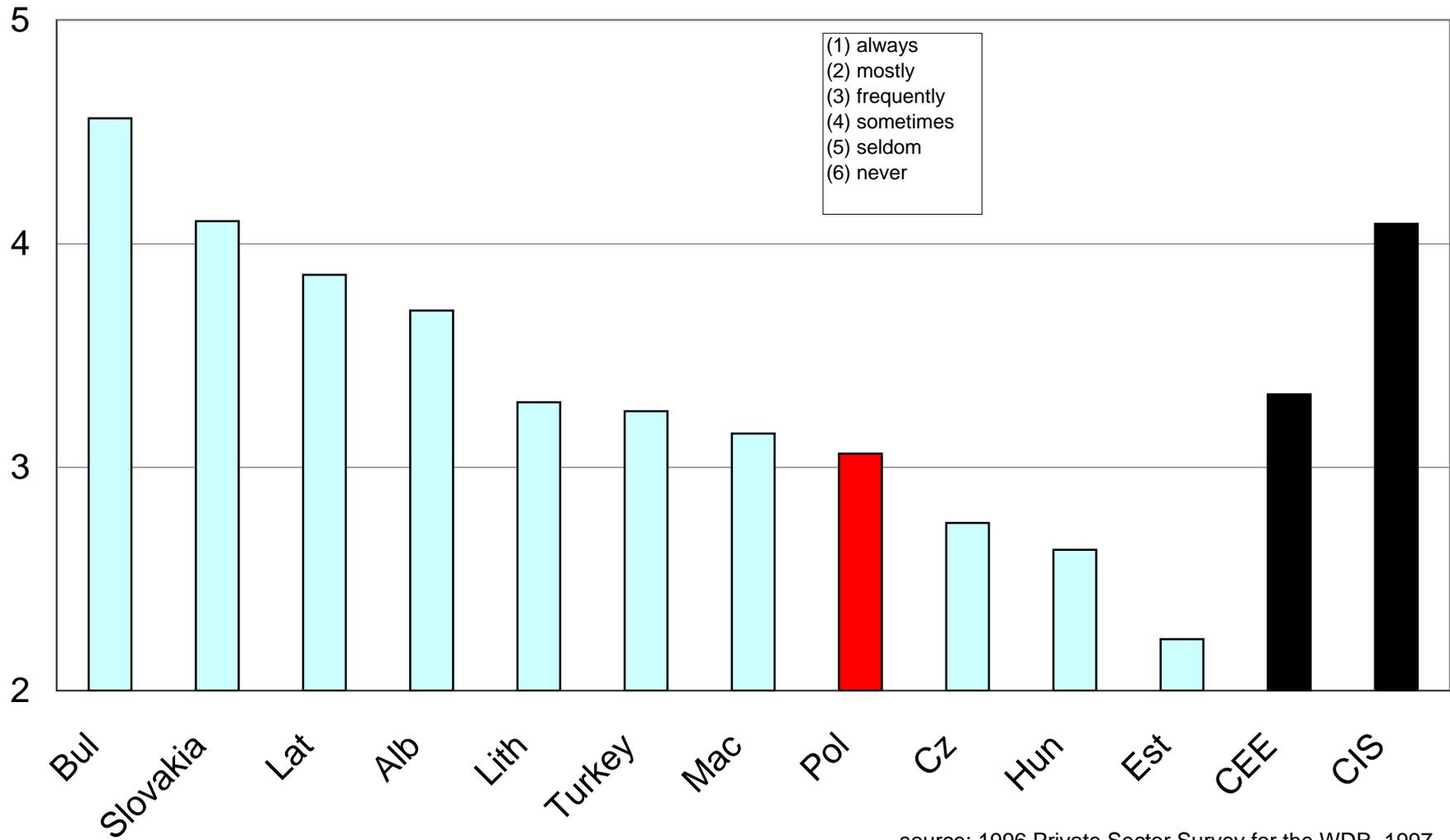


Please rate your overall perception of the relation between government and/or bureaucracy and private firms on the scale. (ten years ago)

Helping	Neutral	Opponent
hand	agent	
1 2	3 4	5 6

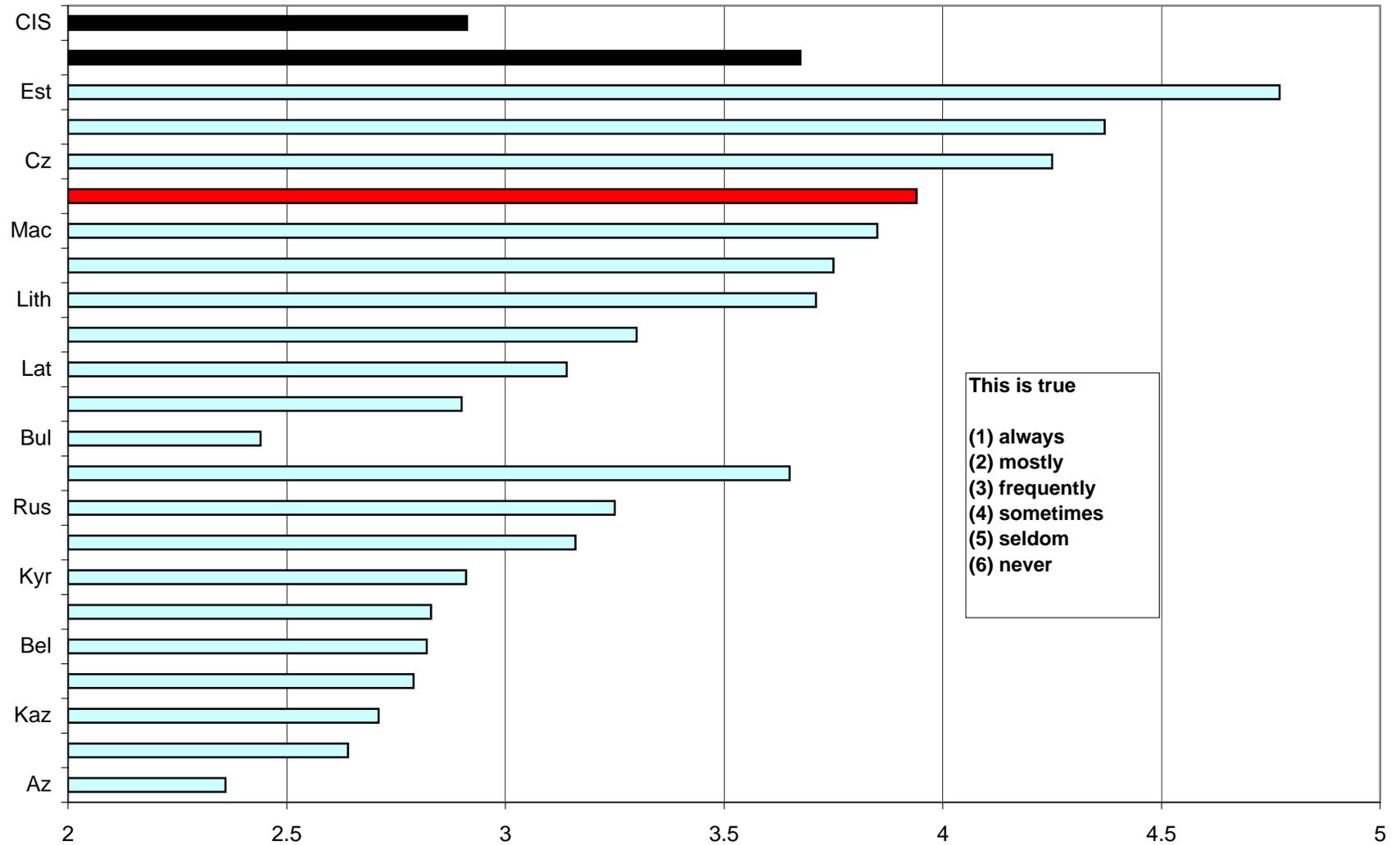


## Necessity for Firms to Make Unofficial Payments

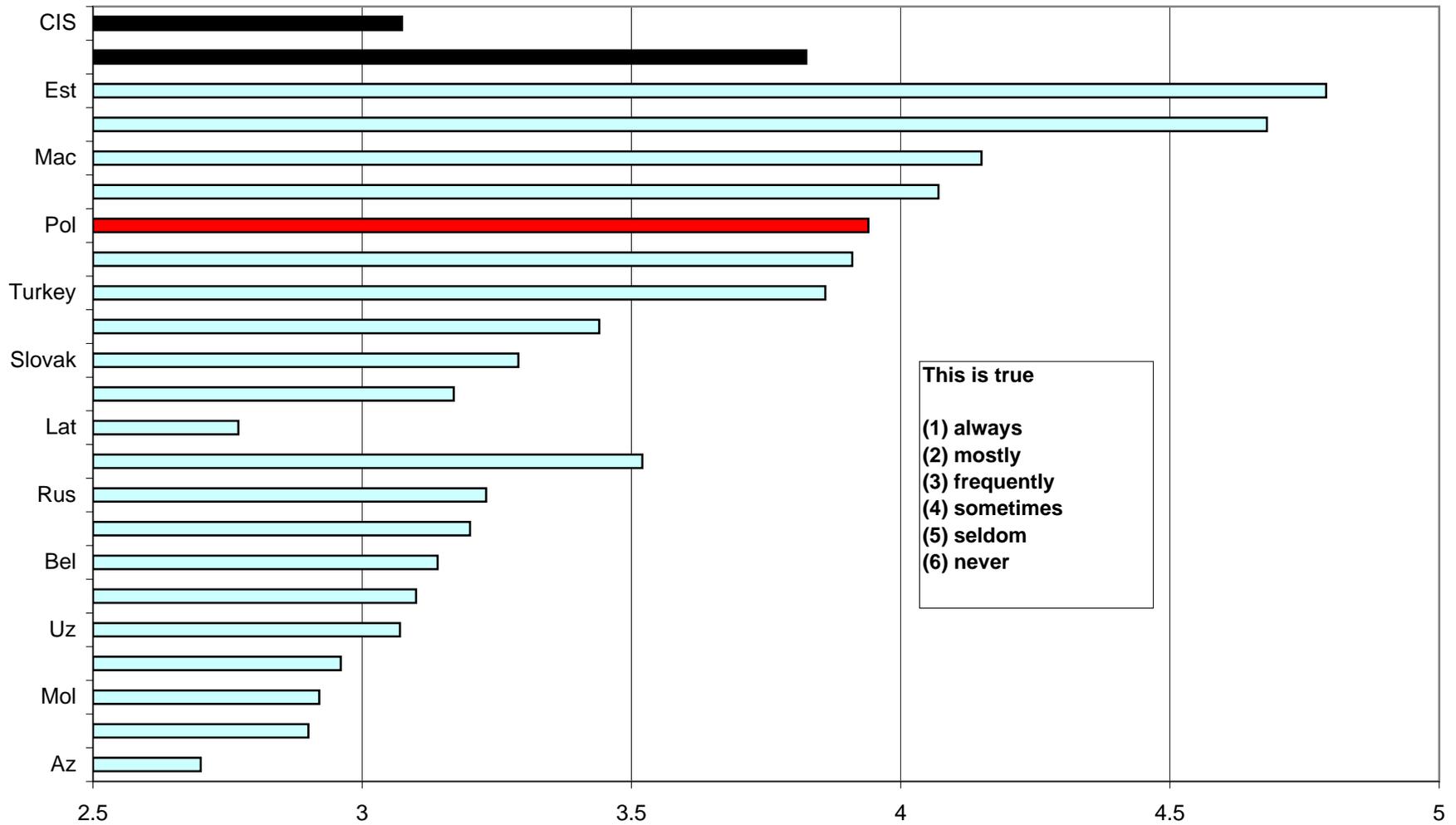


source: 1996 Private Sector Survey for the WDR, 1997.

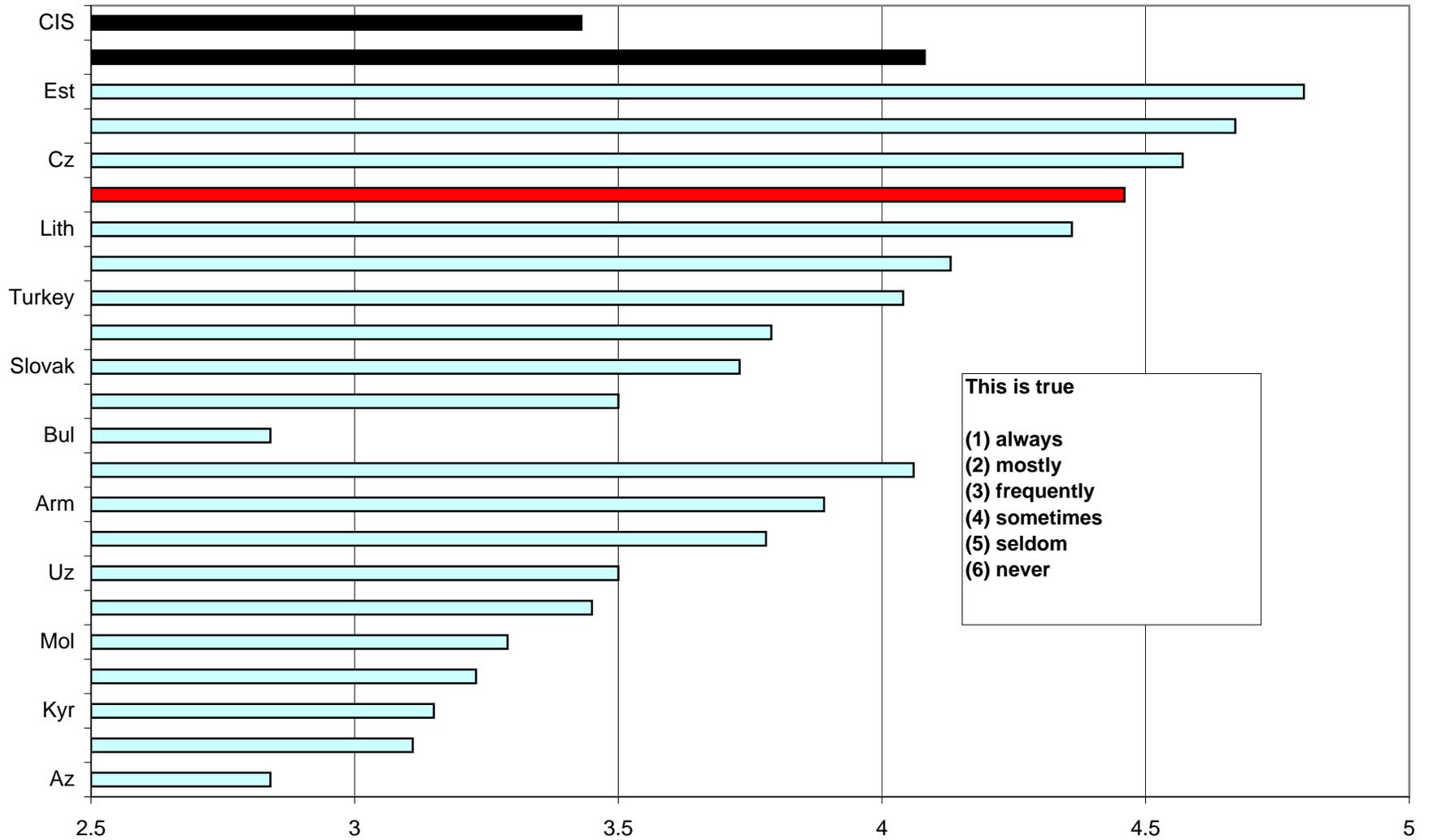
**"It is common for firms in my line of business to have to pay some irregular "additional payments" to get things done."**



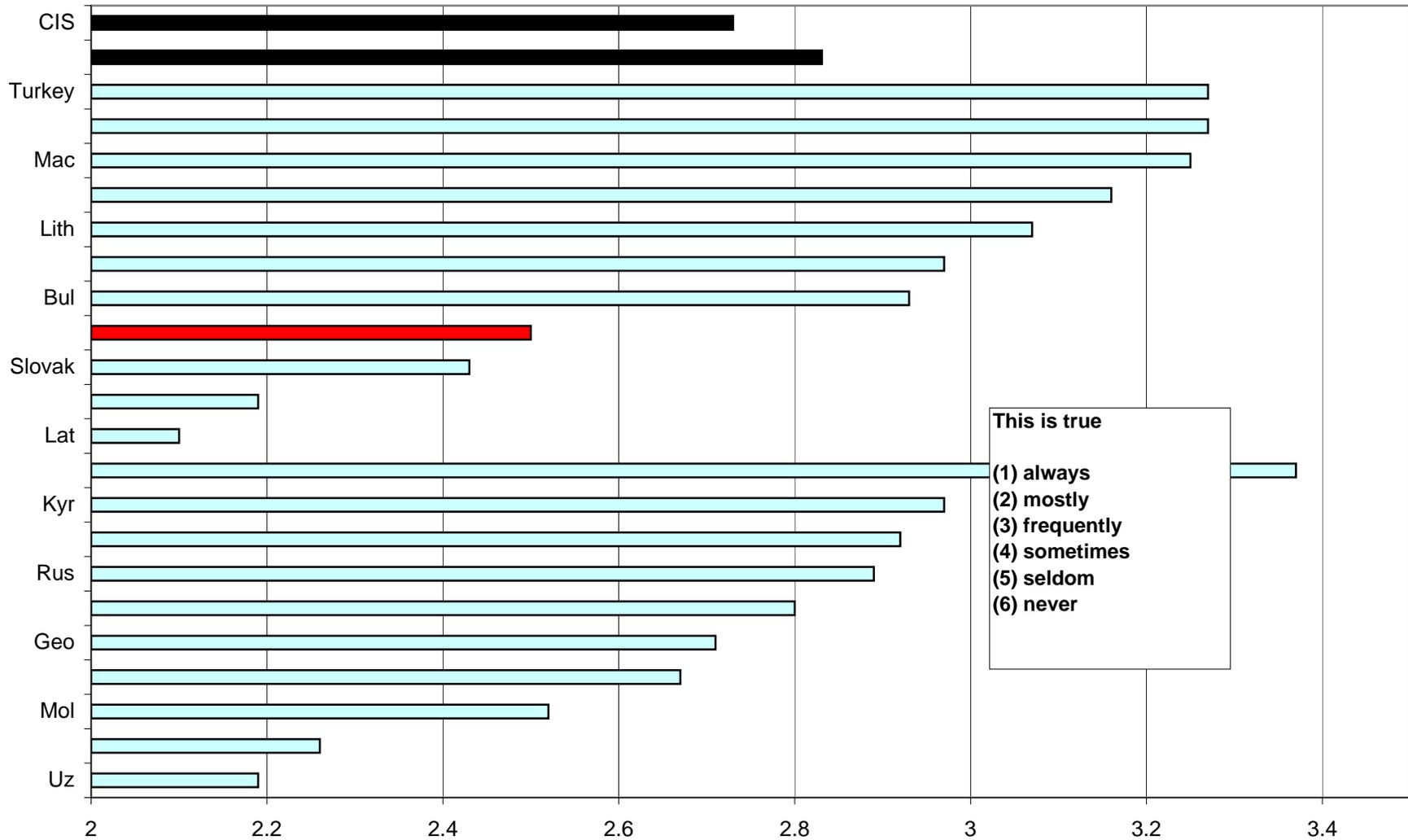
**"Firms in my line of business usually know in advance about how much this "additional payments" is."**



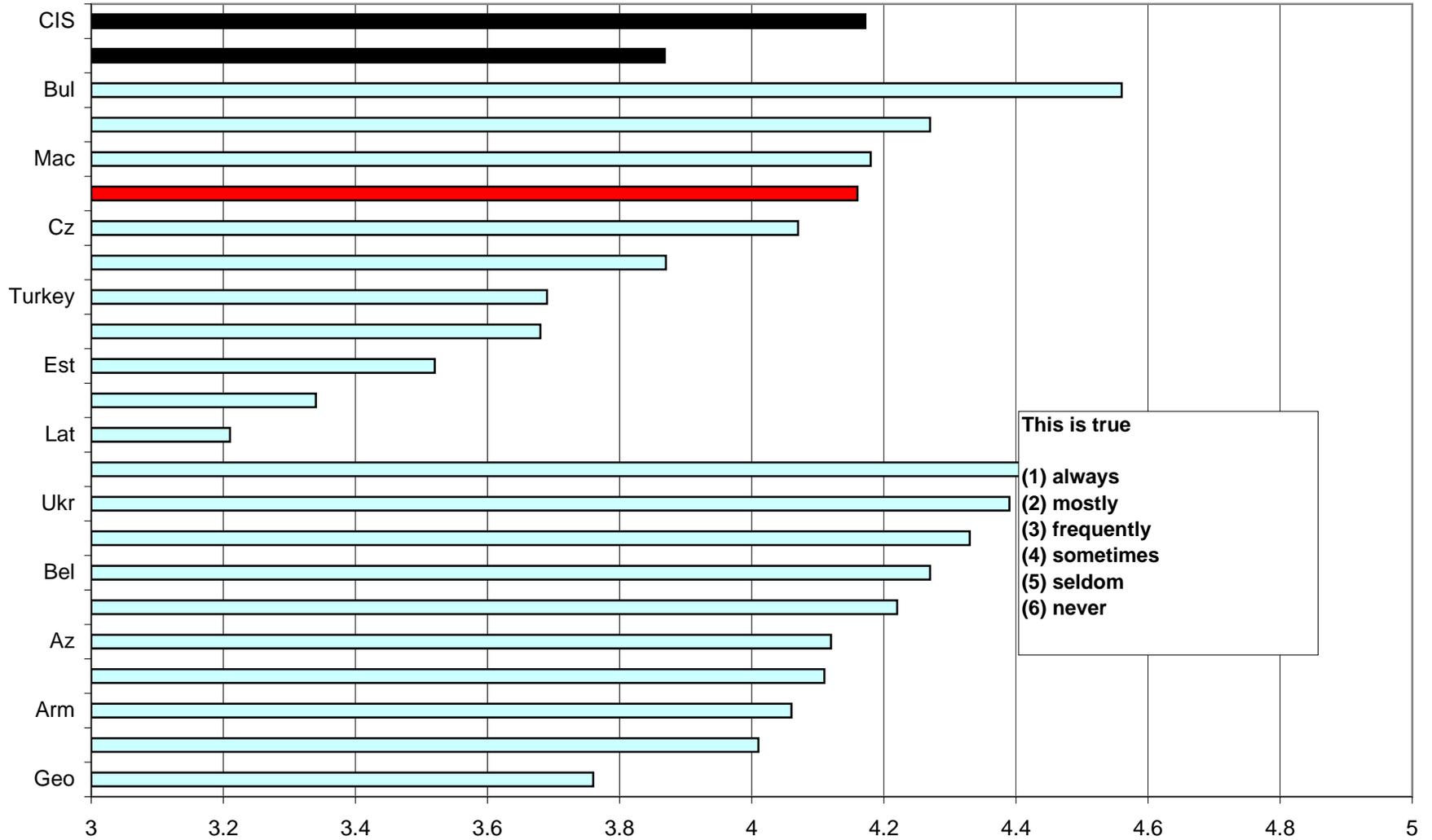
**"Even if a firm has to make an "additional payments" it always has to fear that it will be asked for more, e.g. by another official."**



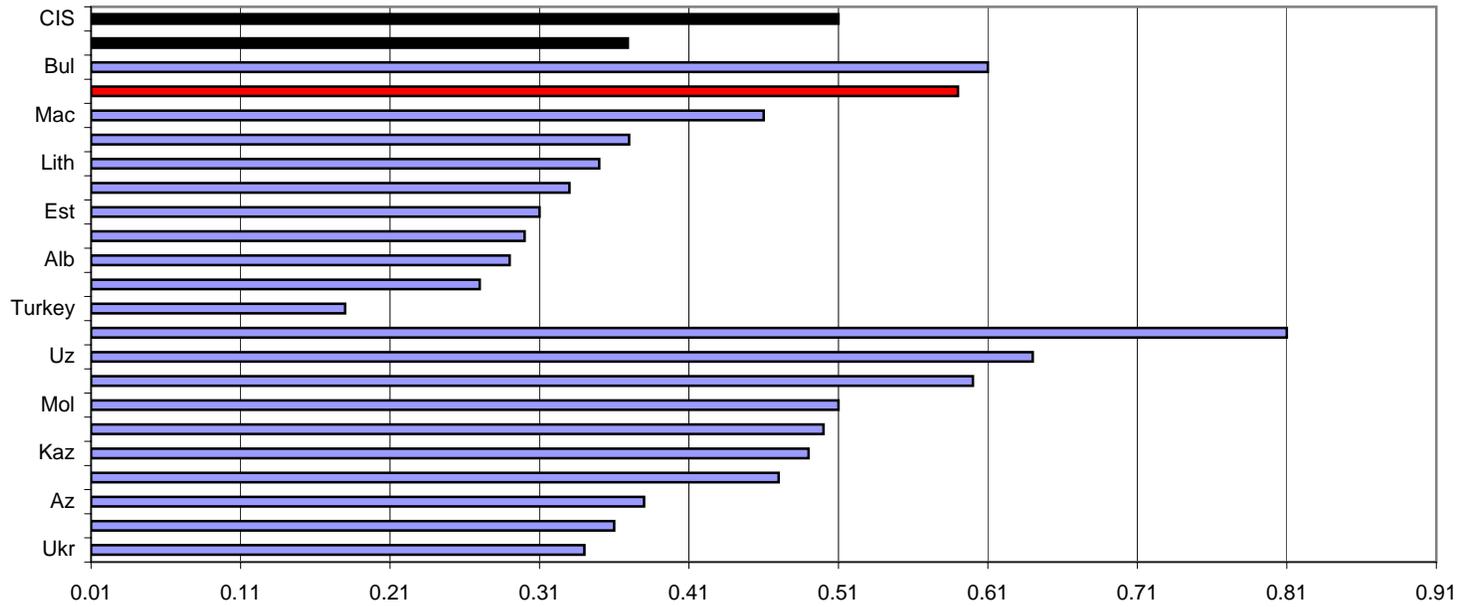
**"If a firm pays the required "additional payment" the services are usually also delivered as agreed."**



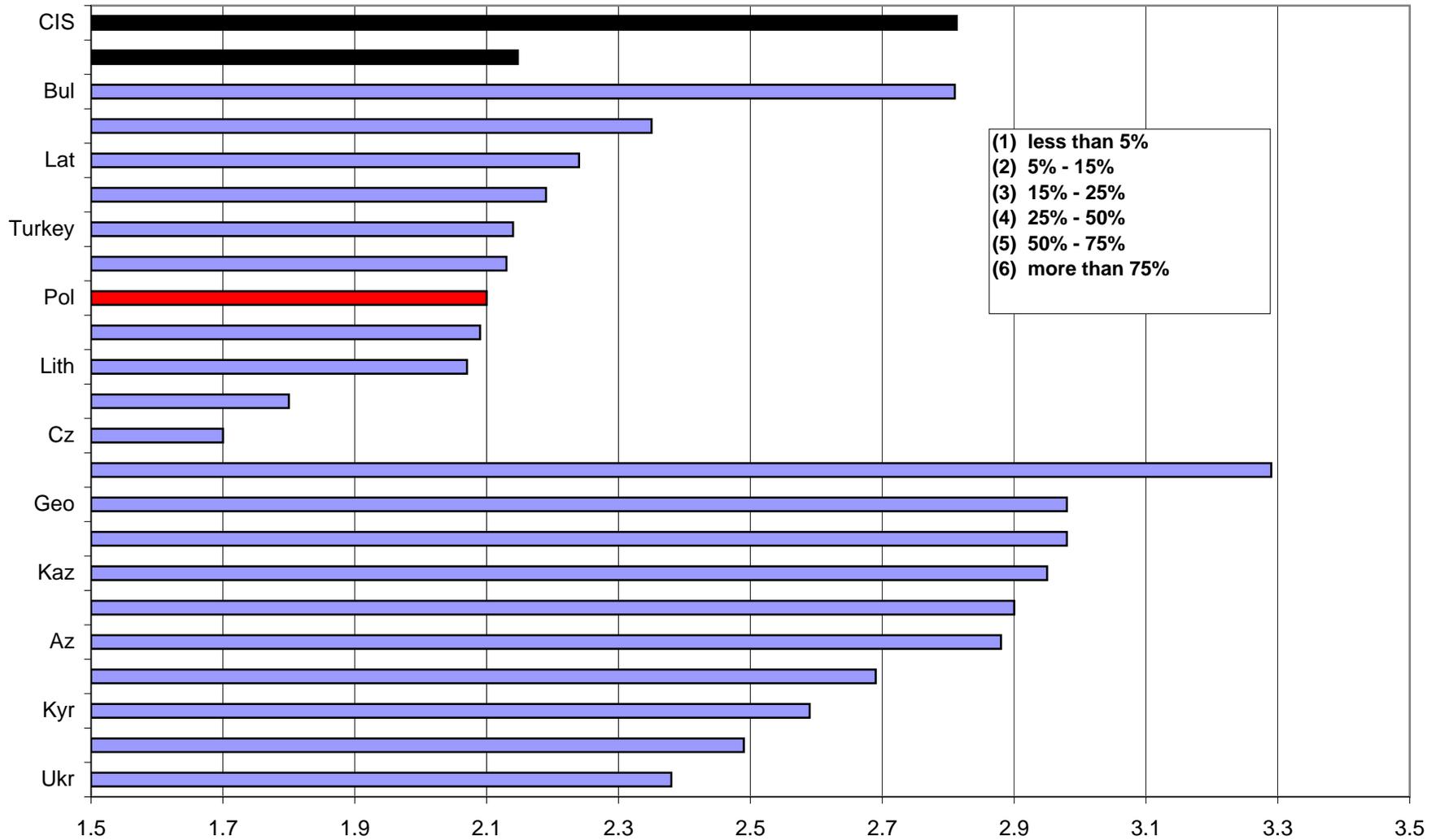
**"If a government agents acts against the rules I cab usually go to another official or to his superior and get the correct treatment."**



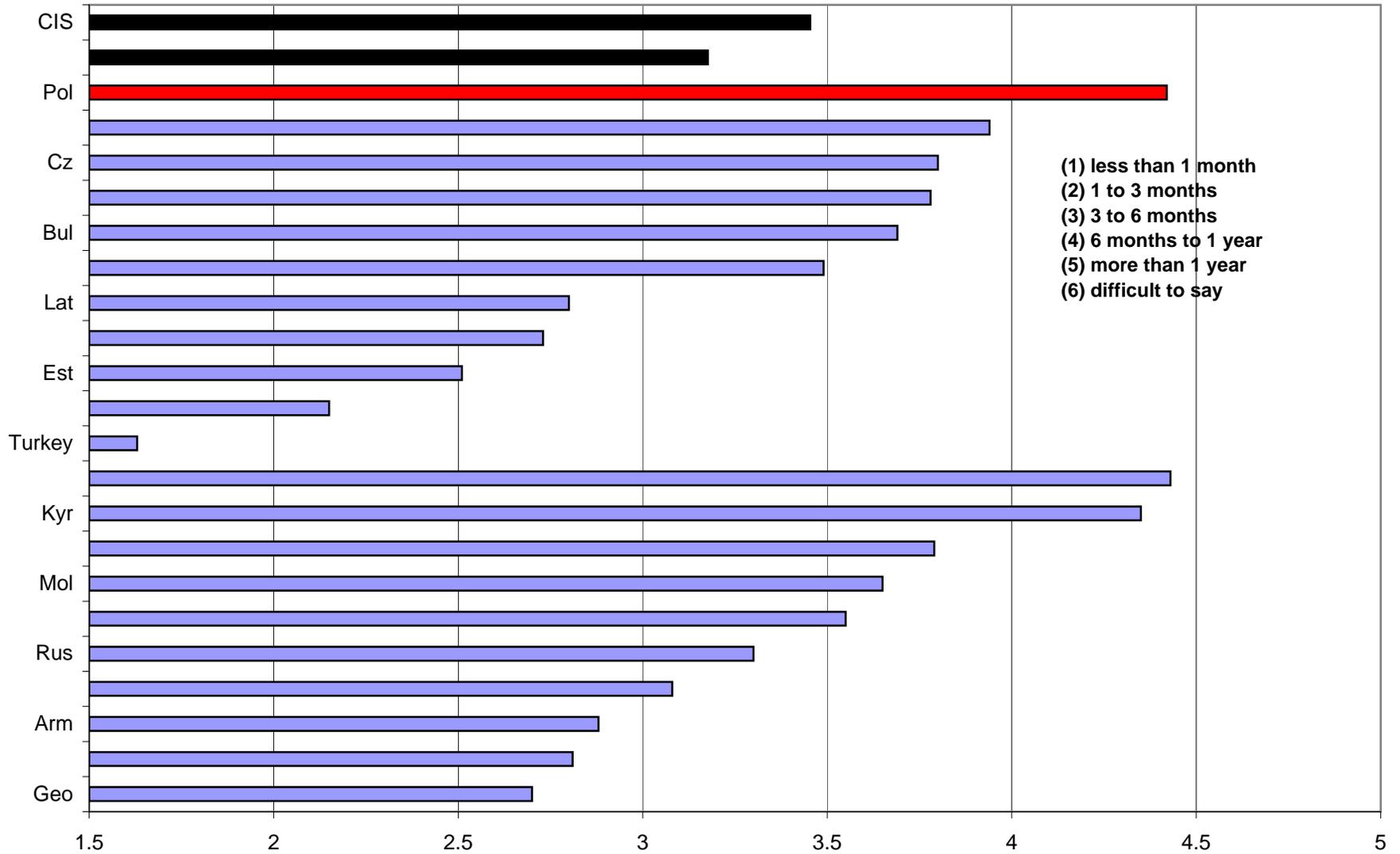
Have you ever decided not to make a major investment because of problems relating to complying with government regulations? Yes/no )



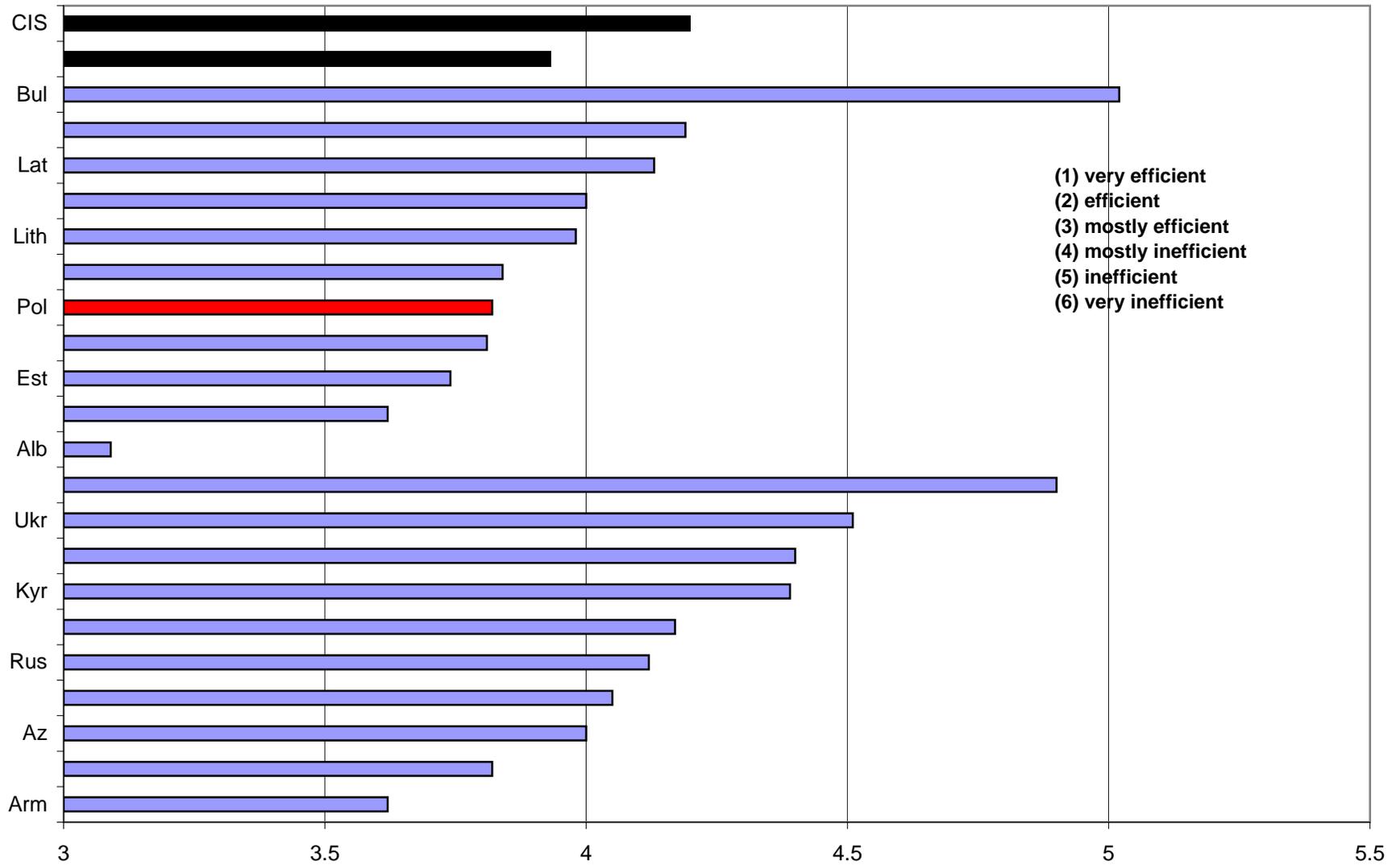
**What percentage of senior management's time is spent on negotiation with officials about changes and interpretations of laws and regulations?**



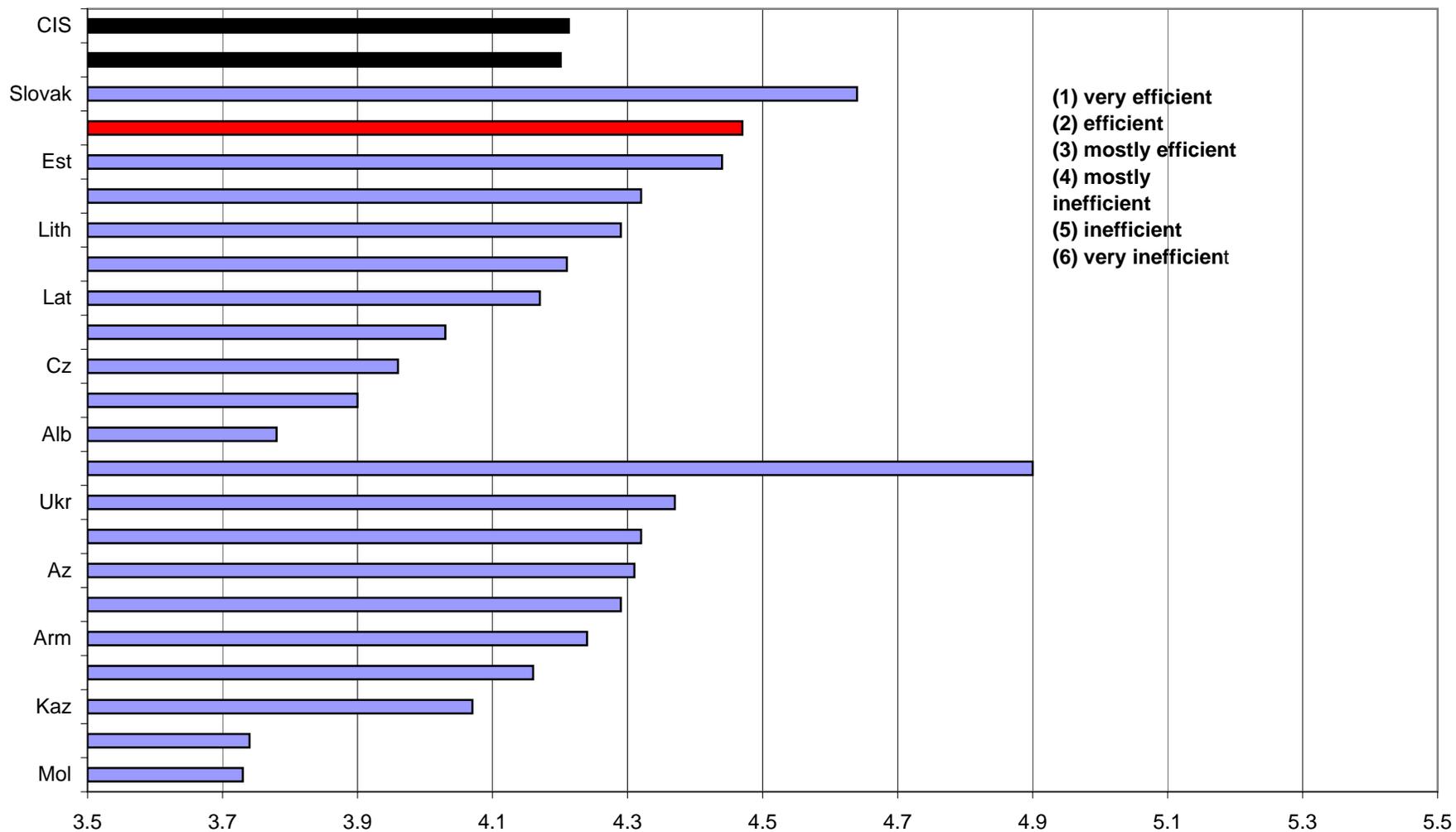
### How long does it take to get a public telephone line connected?



### How would you generally rate the efficiency of government in delivering services? (Now)



### How would you generally rate the efficiency of government in delivering services? (10 years ago)



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