I. Abstract

Latvia is one of the transition economies that came in existence after the end of Soviet reign. During late 1990s, the corruption and the lack of efficiency and proper mechanisms in the government system were the biggest obstacles in transition process. There was a need to improve service delivery mechanisms. People suffered because of high levels of corruption in the system that primarily existed in the form of state-capture. Bringing transparency and improving the working of government at macro level was important to ensure improved service delivery to citizens, and public access to information was necessary in order to bring accountability to the system.

The Programmatic Structural Adjustment Loan (PSAL) project was initiated in 2000 by the World Bank to address these issues and to strengthen the reform process in Latvia. The program focused on public sector reform, the privatization process, and creating a legislative basis for other reforms. The PSAL project attempted to bring certain changes through necessary reforms to reduce corruption and bring accountability in the system. Simultaneously, new mechanisms were introduced for improved service delivery and information access to the citizens.

The project outcome is satisfactory, its sustainability likely, and the institutional development impact (within the government) is considerable. Although the World Bank Research suggests substantial poverty reduction through PSAL,1 the public governance issues under PSAL operations seem difficult to assess at present, as the change process will require time.

II. Background

During the late 1990s, Latvia was in the final stages of transformation to a market economy. This involved major steps, like the privatization of state-owned firms. Ninety-five percent of the companies under Latvia's privatization program were privatized by the end of 1998. Privatization of small- and medium-size enterprises, although started only in 1994, was basically completed by mid-1998. However, privatization of the remaining huge state-owned firms, such as Lattelekom, Latvia Shipping Company, and Latvenergo was delayed due to unclear sector policies and legislation, lack of a consistent and stable regulatory framework, and lack of political commitment. The anticorruption surveys

---

1 This case study was prepared by a team comprising Prof. Deepti Bhatnagar and Animesh Rathore at the Indian Institute of Management (Ahmedabad) and Magüi Moreno Torres and Parameeta Kanungo at the World Bank (Washington DC).

showed that foreign investors and the Latvian people considered transparency extremely important for privatization and regulatory stability.2

The corruption was seen as being deep-rooted, and the government system lacked efficiency and effectiveness. Besides privatization, it was important to bring transparency and to improve the working of government at a macro level in order to improve service delivery to citizens. In order to address these concerns and to strengthen the reform process in Latvia, the Programmatic Structural Adjustment Loan (PSAL) project was initiated by the World Bank to provide three PSALs over a three-year period.

Under the PSAL program, the government outlined a three-year reform agenda aimed at establishing a macroeconomic framework that would facilitate growth and improve the public sector performance through the following:

- Correcting macro imbalances
- Strengthening the credibility of the public sector
- Improving institutional capacity to deliver public services
- Encouraging private sector development through finalizing the privatization process and defining a clear and transparent regulatory framework.

The World Bank granted PSAL I, worth US$40.41 million, in March 2000, followed by PSAL II of US$20 million in September 2002. The PSAL program intended to support sustained and rapid growth of the economy and improved welfare of citizens through reforms improving government efficiency and effectiveness. Governance and institutional reforms formed the backbone of reform program. The reform program was initiated under the first SAL (Structural Adjustment Loan) and after completion of the first SAL the program continued to get World Bank's support through such programs as Institutional Development Funds (IDFs) on public sector reform and infrastructure regulation, and its comprehensive anticorruption agenda.

Specific reforms were initiated in the areas of pensions, public sector management, human resource management, public expenditure management, privatization and regulation of public utilities, and private business. To assist the government's comprehensive anticorruption effort and to streamline business regulation, the PSAL helped introduce measures such as a regulation for Corruption Prevention Council (CPC) to publish the status of anticorruption program on a quarterly basis. The reforms would enhance Latvia's prospects for timely European Union accession and provide a positive signal to international institutions and investors regarding the government's commitment to reform and the transition to a full-fledged market economy.

The PSAL aimed to make a significant impact on poverty, as it was planned to support growth objectives in a stable environment as well as measures to improve service delivery and social assistance of government, and to reform the pension system.

The PSAL program could prevent further erosion in the actual living standard of the poor by contributing to low levels of inflation. The objectives of improving public administration and management of resources could make possible improvements in the cost effectiveness of government’s exclusive social programs for the poor.

III. Impact/Results

The PSAL assisted government in establishing more efficient institutional arrangements for making strategic policy decisions and in establishing accountability for their implementation.

The project outcome was considered satisfactorily and its sustainability likely. Substantial institutional development was observed in the government and the government’s commitment to accountability and transparency in the system could be seen in practice. However, the public governance issues under structural adjustment operations will be difficult both to implement and to evaluate, as the change is only expected to occur in small steps and over a number of years. The benefits are rarely noticeable in the short run and formal achievement of benchmarks is meaningless, unless embodied in deep-rooted and lasting institutional changes. The reform program has helped Latvia deal with the after-effects of the Russia crisis.

Impact on the Ground

The PSAL, with the main theme of “good governance” promoted reforms across the board including public administration, social issues, health, privatization, macroeconomic framework, utilities, etc. The PSAL has resulted in substantial poverty reduction.

1. Pension reform

With the assistance of the World Bank, a progressive “three pillar” pension system has been established in the country. The system is financially sustainable in the long-term creating a privately funded and managed pillar, which became operational in July 2001. The funding scheme creates a direct link between individual contributions and old age benefits.

---

4 Useful links: www.fm.gov.lv
7 Useful links: www.lm.gov.lv
2. **Improved public administration**

A package of laws to strengthen public administration has been adopted. It includes laws on administrative framework, administrative procedures, civil service, and agencies. The package provided a platform to build a professional army of civil servants and a more effective and accountable public administration structure. Nonprofit state enterprises, earlier created in a specialized manner to escape controls, are now being converted into accountable agencies with clear objectives.

3. **Anticorruption program developed**

Latvia has adopted a package of new laws aimed at more transparent and accountable party finances, and at preventing conflict of interest and illicit enrichment. A new independent bureau to fight corruption has been established.

The role of NGOs (nongovernmental organizations) and civil society development have been promoted through the PSAL project. The NGOs are now involved in activities like monitoring the privatization of remaining enterprises, and are also encouraged to participate in drafting legislation.

**IV. Key Elements of Empowerment**

**Access to Information**

Information access for the public was necessary to assure vertical (bottom to top and citizens to government) accountability in the system. The government passed the Law on Information Access in 1998, but the law alone could not fulfill the information needs of the public. Thus, the cabinet of ministers adopted certain regulations to classify the information and to ensure the institutional arrangements for people’s access to information. The government set up a unit within the Ministry of Justice to do the following:

1. Establish an action plan to:
   a. Build capacity in public sector bodies to respond to public requests for information
   b. Report on compliance with the law
   c. Educate the public on procedures for obtaining government documents.

2. Develop a system to monitor the implementation of the law, including:
   a. A mechanism for measuring fulfillment of public requests for information
   b. The publication of these measures in public sector annual reports.

3. Ensure that the annual reports of public sector bodies include information on:
   a. Rights of the public to information
   b. Procedures for the public to access information

---

8 For more information, please see: www.delna.lv
c. Measures for fulfillment of public requests for information.

The inclusion of this information in the annual reports of public sector bodies has been made mandatory. All public institutions, including regulatory bodies and inspectorates, must prepare an annual report on their activities (from the year 2000 onwards) as per the instruction issued by the cabinet of ministers. The government has developed guidelines for the content of annual reports, requiring them to have a greater performance focus.

**Inclusion and Participation**

The involvement of civil society has increased in the anticorruption efforts particularly in related monitoring activities. Delna, the local affiliate of Transparency International (an international NGO combating corruption), prepared a progress report of government’s anticorruption program and is also monitoring the privatization process of the remaining large enterprises.\(^9\) In recognition of NGOs role in civil society, the government amended regulations to encourage NGOs’ participation in drafting legislation.\(^10\)

**Accountability**

The PSAL included mechanisms to improve vertical as well as internal accountability of the Latvian government.

1. **Vertical accountability**

**Anticorruption efforts:** In 1997 an interministerial body called the Corruption Prevention Council (CPC) was formed to develop and implement an anticorruption program. The first PSAL provided the CPC secretariat with an executive head and other staff and resources. The council established mechanisms to monitor corruption and piloted the anticorruption efforts, although it experienced some difficulty in effectively establishing its monitoring capacity. In addition, CPC implemented procedures for the public to report on cases of corruption. For transparency within the council and its accountability to the public, a regulation was made requiring the council to publish the status of all measures identified in the anticorruption program. As a result, CPC started publishing the status of anticorruption program on a quarterly and report on corruption in the public sector on a yearly basis.

Another effort was a law on political parties with provisions about transparency, oversight, and auditing. This law was submitted to Saeima (the Latvian parliament) by the cabinet of ministers. In addition to other reforms, the minister of justice drafted an instruction requiring all court decisions and rulings to be made public so as to establish transparency in the judiciary.

---


Public release of Delna’s reports would contribute to monitoring the progress of the PSAL program and preparing for future reforms. This release of information would enable the people to find the loopholes in the reform and to hold the relevant agencies accountable.

2. **Internal accountability**

**Government agency accountability:** Prior to the PSAL project, the public agencies lacked a clearly defined institutional framework of public administration or a legislative framework for agency operations and financial management. To limit the proliferation of such agencies and increase transparency and accountability of the existing public sector agencies, a law on public sector agencies was enacted in March 2001. A law on administrative procedures, to provide a uniform framework of general principles and guidelines for agency’s decision making, was under consideration in October 2001.

3. **Public expenditure management and monitoring**

The Saeima adopted the public sector agency law to improve transparency and accountability for budget resources by defining the financial and accounting framework for public sector agencies. A related law was passed to bring all accounts of budget-financed institutions into the budget and to ensure that all of them held their accounts only with the Treasury. Other measures to improve accountability in budgeting and resource management are also in place, such as the establishment of a Public Accounts Committee of the Saeima to review the state audit office reports. Latvia has also initiated an external audit of its budget carried out by a special government commission.

Because of weak accountability at central and local government levels, the central government has proposed to local governments integrated financial accounting and reporting procedures which would improve access to information on budget execution and resource management.  

4. **Transparency and accountability in civil service pay**

The cabinet of ministers adopted a public sector pay concept supporting the introduction of a broad-banded, transparent, uniform pay scale with performance evaluation mechanisms, though difficulties remain in implementation, phasing, and change management. The Saeima passed a law on in September 2000 to develop a professional and politically neutral civil service. The law also includes provisions for performance evaluation.

5. **Conflict of interest**

An Anticorruption Unit (AU) in the state revenue service was established to develop guidelines to identify conflict of interest and cases of illicit enrichment among public...
officials. The documents and procedures to identify conflict of interest included forms for declarations of income and assets, a manual on processing and assessing declarations, and manuals and training curricula on conflict of interest for public sector employees.

Declarations of income and assets were submitted by the president of the state, the prime minister, parliamentary secretaries, and key government officials, and were published annually. The AU also designed and implemented a system for public officials to report potential cases of conflict of interest.

6. Local Organizational Capacity

Although the World Bank financially promoted NGOs through the Small Grants Program and trust funds, the PSAL project has encouraged NGOs to perform in key areas such as policymaking, privatization, and anticorruption. Delna’s example shows that when given a chance, the local organizations can perform vital tasks such as reporting the progress of anticorruption programs or monitoring the privatization process.

V. Issues and Lessons

Challenges

- The Latvian government passed the Law on Information access in 1998. But, due to absence of law enforcement mechanisms and the inefficiency of ministries to answer information requests by the public, the law could not be implemented properly. To address this issue, the government adopted new regulations under PSAL project to determine the classification of information and the institutional arrangements for ensuring people’s access to information.

- World Bank research prior to PSAL project classified Latvia as a country with medium levels of administrative corruption and high levels of state capture. Inefficiency and corruption in the delivery of public services undermined public welfare and disproportionately hurt the country’s most vulnerable people who could not afford private sector alternatives. Excessive and corrupt regulation of the business community stifled private sector development, while evasion of regulations through bribery resulted in an erosion of safety in the workplace, environmental degradation, and other negative effects. In order to improve this situation, PSAL II focussed more on anticorruption efforts.

- During the 1990s, the government allowed creation of numerous quasi-autonomous agencies without accountability and transparency mechanisms for resources used and services provided. This resulted in much informality and waste, and was a significant source of corruption in the system and loss of control over budgetary resources. The government lacked a strategic planning framework that would allow overall policy commitments, policy priorities of individual ministries, and targets to be linked with budget allocations. The pay system in public sector lacked transparency and did not ensure equal pay for equal work.

12 For further information, see www.politika.lv
Local governments lacked adequate accountability mechanisms as well. Improved performance of the public sector was important for continued progress. Further, attention was needed to strengthen public administration, the judicial system, and expenditure management. These changes could be introduced through the PSAL project.

- Judicial reform was given high priority by the government. However, public opinion polls repeatedly ranked the judicial institutions among the most corrupt and inefficient institutions in Latvia. The ministry of justice issued instructions to bring transparency and accountability to the judicial system. For instance, an instruction was issued to all courts to publish all their decisions and rulings with a cumulative indexing system. Such publications are to be stored electronically and can be made available to the public at low costs. Implementation seems difficult at present, as all the courts do not have computers.
- During the PSAL project, promoting regional development and raising the quality of social services throughout the country was as a challenge.
- Completing the structural reform agenda and successful integration into the European Union are major challenges.

**Key Factors/Issues**

- Public accountability and transparency were key elements of reform to ensure improved efficiency of government institutions in delivering services, and to strengthen citizen’s trust in administration.
- Structural changes at macro level take considerable time to generate positive results at the grassroots and sufficient time needs to elapse for assessing their impact on the empowerment of people.

**VI. Further Information: References and World Wide Web Resources**

Programmatic Structural Adjustment Loan Project (PSAL), URL:

Programmatic Structural Adjustment Loan Project (PSAL 02), URL:


