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How to Reform Business Inspections

Design, Implementation, Challenges

Investment Climate Advisory Services I World Bank Group

IFC International Finance Corporation World Bank Group

MIGA World Bank Group Multilateral Investment Guarantee Agency

THE WORLD BANK

Developed Under Funding from the IFC

How to Reform Business Inspections

Design, Implementation, Challenges

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Investment Climate Advisory Services of the World Bank Group

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About the Investment Climate Advisory Services of the World Bank Group

The Investment Climate Advisory Services of the World Bank Group helps governments implement reforms to improve their business environments and encourage and retain investment, thus fostering competitive markets, growth, and job creation. Funding is provided by the World Bank Group (IFC, MIGA, and the World Bank) and over 15 donor partners working through the multidonor FIAS platform.

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Foreword

Business inspections reform is part of a broader set of products and approaches the World Bank Group Investment Climate Advisory Services uses to improve business regulations, in particular relating to start-up and operation. These products cover such complementary issues as business registration and start-up procedures, licensing and permit practices, inspection procedures, and enforcement.

This handbook should take its place alongside the World Bank Group's (WBG) 2009 guide on "How To Reform Business Licenses." It aims to provide would-be reformers, inside and outside of the WBG, with a comprehensive range of tools that enable them to tackle all essential aspects of regulatory simplification and smarter regulation. It also builds on earlier work the WBG has done on inspections reform, particularly on a number of reform projects the WBG has worked on since the late 1990s, and on a set of knowledge management publications the WBG has produced, most importantly the toolkit "Good Practices for Business Inspections – Guidelines for Reformers" (2006). Other important WBG publications on inspections reform include sets of case studies and overviews of country experiences (in particular a review of international experience published in 2005), a manual on checklist development (2009), and a note on assessment tools for inspections (2009). To keep reformers abreast of the latest developments in good practice, this handbook should be followed up by further reviews of international experience.

The past two decades have seen growing attention given to business inspections throughout the world, in all types of economies and contexts, as awareness has grown both of the burden they can create for businesses and of the fact that a lack of transparency and focus on genuine risks in inspections can harm the public just as much as it harms businesses. Reform has become a growing priority as a result of three different and complementary concerns and needs:

- To decrease the administrative burden businesses face and increase the competitiveness of the private sector.
- To improve public outcomes by protecting food safety, the environment, and workers' health more effectively and by improving state revenue collection.
- To use state resources more efficiently to help control state spending.

Although there is considerable variation in the precise ways reformers in various nations have found to streamline business inspections, a number of good practices and key principles have now found wide acceptance. Those principles form the foundations of this handbook. Many of these precepts have previously been documented in key reports from various governments, perhaps most notably in the 2005 "Hampton Review" prepared under the direction of Sir Philip Hampton for the United Kingdom. A central element of this consensus is that there is no opposition between developing an inspections system that is friendlier to most businesses and safeguarding the public more effectively. The table that follows summarizes some of the misconceptions that still often linger and the alternative conclusions that our analysis of good practices documents. We hope this handbook will be widely used and will help to deliver better outcomes for both businesses and citizens.

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Chapter 1. Introduction: the Inspections Problem

1.1 Inspections are a Complex Topic

1.1.1 Inspections are Near-universal – and Multiform

Business inspections are found in almost every country. They take place under a variety of guises and names (including quasi-synonyms like "audits," "checks," "visits," etc.) and they tend to be a key enforcement mechanism for whatever regulatory system the state maintains. Inspections are rather different from other regulatory procedures such as registration, licensing or permits, however, because, strictly speaking, they are not a *procedure* that a business must go through but an *event* that may or may not happen and that does not always follow the same pattern. While it is normally a certainty that a business will have to obtain whatever licenses, permits, or certificates are required for its work (unless that business remains "informal," i.e. illegal), there is only a probability that a business will undergo an inspection and some businesses may never be inspected. Permit and licensing procedures also tend to follow a set pattern in which business representatives visit government agencies and go through a series of well-defined steps. The way an inspection takes place, however, can vary sharply from one event to the next.

This uncertainty surrounding the inspections process creates several difficulties for reformers:

- Inspections present specific measurement challenges. Since it is difficult to define a "standard" inspection, reformers often need to conduct a survey of the businesses affected to define the burdens inspections impose.
- Although process simplification is often a good way to reform other regulatory procedures, it is not a primary tool for improving inspections. To the contrary, inspections reform often involves making the process *more* regulated or more "procedure-heavy" to decrease the discretion of inspectors that can lead to abuses of power.

In many countries the sheer number of licenses, permits, and other compulsory formalities businesses must undergo means that the vast majority of these requirements are superfluous and can be dismissed as "red tape" – fit to be cut using the "guillotine" approach[1] – but canceling inspections *functions* is rarely a viable option (although reducing the number of inspections of business may be helpful). Although careful review of inspections systems often does suggest that some inspecting agencies can be merged to improve efficiency, this process usually involves consolidating but preserving their functions. While some inspecting functions either are futile or represent gross intrusions into issues that should be left to free enterprise (See Box 1 and Box 2),[2] the vast majority of inspections are connected to legitimate state functions such as enforcing tax legislation, ensuring food safety, protecting the environment, guaranteeing the safety of buildings, etc.

BOX 1 In Mongolia, the Majority of Inspection Functions are Related to Safety but Some Border on the Absurd

In Mongolia, 81 percent of the businesses inspected by the General Agency for Specialized Inspections (GASI) went through one of the following inspections between Q4 2008 and Q3 2009 (a) environmental, sanitary and hygiene inspections, (b) labor sanitary inspections, (c) food sanitary inspections, and (d) labor safety inspections. These inspections are clearly related to safety issues. They need to be improved, not abolished. But Mongolia is also home to more nonsensical (although less frequent) inspections:

a) Trade technology inspections often focus on issues such as how goods are placed on the shelves or the location of the cashiers.
b) The nation's tourism law mandates that tourism inspectors check the accuracy of the information tour operators and guides give out about Mongolia's political and economic situation, traditions, and religion. Enforcing this regulation effectively would require inspectors to follow tours to check the information guides offer, speak several languages and be very knowledgeable about Mongolia's circumstances, traditions, and religion. This requirement is not only impossible to implement but does nothing to protect health, safety, or the environment.
c) Restaurant menus are also subject to ridiculous inspections. Restaurants are required to start menus with appetizers and salads and to finish menus with drinks. One pub we studied had to order new menus, at a very high cost, because its initial menus had started with drinks.

Source: IFC (2010). "Business Inspections in Mongolia."

[1] Under the "guillotine" approach, each ministry lists its business regulations and licensing procedures and those whose retention cannot be justified within a given period of time are automatically rescinded. The FIAS definition of this process is available at http://www.fias.net/ifcext/fias.nsf/Content/BRG_Bibliography_Toolsimproveexistingreg_Guillotine

[2] Absurd regulations abound not only in developing countries but also in OECD member states. For a recent example concerning the regulation of hairdressers, barbers, cosmeticians in the District of Columbia see http://yglesias.thinkprogress.org/2010/08/i-am-an-unlicensed-barber/ and further discussion of how such rules corresponds to "regulatory capture" at http://www.spectator.co.uk/alexmassie/6214130/the-terrible-threat-posed-by-cowboy-barbers.thtml

Such government inspections are in general necessary to promote business compliance with regulations that protect health, safety, and the environment and ensure revenue collection for the state and therefore cannot simply be eliminated. Simplifying or streamlining the regulations that these inspections are intended to enforce may make inspections less burdensome for businesses but will not make them superfluous.

BOX 2 In Ukraine and Kenya, Some Inspectorates Check Compliance with Standards that Should Not Exist

In Ukraine, standardization, metrology, and consumer rights protection authorities inspected one out of every six businesses in 2007. These inspections represent a significant burden for businesses, one that is all the more excessive because inspectors check compliance with many standards that regulate issues unrelated to the safety of the goods and services produced – issues that would be better left to the private sector and, in the end, consumers to decide. Beyond essential safety requirements, standards should be voluntary and businesses should be free to choose whether to comply with them. However, in Ukraine all standards are compulsory and many of them are over-prescriptive. Such standards include regulations mandating production process details such as the recipe of food products or the detailed composition of construction materials. Standards in Ukraine also apply to services in ways that run contrary to international best practices. The country's standardization and consumer protection agency enforces compliance, for example, with a standard regulating the number of hangers that should be in hotel rooms.

In Kenya, mandatory standards are also a problem. All goods produced in Kenya are regulated by mandatory standards set by Kenya's bureau of standards regardless of the level of risk their production represents and without regard to the fact that many of these goods (including most of the high-risk ones) are also regulated by other, more legitimate regulators (e.g. food safety authorities). In addition to setting standards, Kenya's bureau of standards also inspects businesses for compliance with these standards.

Source: IFC (2007). "Business Environment in Ukraine."
IFC (2010). "Inspections Reform in Kenya – proposed directions," Back to office report prepared by Florentin Blanc.

Inspections reform is therefore not primarily about how to eliminate inspections functions or merge inspecting bodies, although both of these reforms can be useful tools. It is primarily about finding ways to improve inspection agencies' effectiveness and efficiency. Inspections should be conducted in a way that (a) maximizes compliance with clear government regulations while it (b) minimizes costs to businesses and (c) optimizes outcomes for government. This goal is summarized well by the slogan of the Dutch inspection reform program: "More effect, less burden."

1.1.2 Misconceptions and Lessons from Experience – an Overview

Common misconception	Findings from experience	Recommended practice
More frequent inspections mean heightened safety.	No correlation has been found between more frequent inspections and better outcomes. When inspections staff are spread too thin, they tend to become ineffective.	Plan and focus inspections based on risk analysis and appropriate choice of appropriate regulatory instruments. Inspect more frequently where risks are higher, use other instruments (e.g., making greater information available to businesses and citizens) to control risk in other circumstances.
Major accidents can only be avoided by inspecting all businesses.	Accidents are not always avoidable. When they are avoidable, and regulatory failure is a factor, that failure often involves poor enforcement of existing rules even after a problem has been spotted.	Regulators need to focus their resources more carefully to address the most critical problems. They also need an effective set of enforcement measures and strong liability rules to deter severe rules violations.
Tougher sanctions deter offenders.	Many violations occur as a result of poor understanding of the rules or of how to comply with those rules. Imposing tough sanctions immediately makes businesses work to hide everything from inspectors.	Proper gradation of sanctions builds trust between the regulators and the regulated and enables businesses to benefit from sound advice. It spares those who make honest mistakes but hits severe or repeated violations hard.
Surprise inspections are the best way to find violations.	Experience shows that skilled inspectors usually detect inspections just as well when they arrive with prior notice. Bad practices usually cannot be easily hidden and advance notification makes inspections easier for businesses and inspectors.	Reserve the possibility of surprise visits for the gravest of situations but move toward announced and planned inspections in most cases. Remember that inspection visits are mostly preventive measures, not police interventions.
Most offenders commit violations by cutting corners to maximize profits.	The vast majority of businesses want to work in a safe and lawful way but either do not know the regulations, do not understand them, or do not see the point of some requirements. Sometimes complying with the regulations simply appears too costly.	Explaining the rules effectively is essential to good regulation. Businesses and the public need to understand the rules and their justifications and maintaining good relations with the vast majority of honest businesses helps regulators focus attention on the minority that are serious offenders.
Reforming inspections means helping businesses but harming the public.	Many inspections reform programs were initiated because of effectiveness issues (i.e., precisely to increase protection of the public. Data shows that countries that have made inspections more risk-focused and transparent have seen public outcomes remain at least stable and often improve.	Inspections reform should be designed so that inspections become both more effective and more efficient – i.e. use fewer private resources (and if possible fewer state resources) but also deliver better outcomes. Better information, more transparency, improved enforcement and greater focus on serious risks are the ways to achieve these goals.

1.2 Why Inspections Reform is Needed

Inspections reform may be triggered by one factor or, more frequently, by several factors, including:

- The negative impact of excessive or arbitrary inspections on business – increasing costs, discouraging investment, reducing competitiveness.
- The ineffectiveness of inspections in protecting public health, safety, and the environment and in generating revenue for the state.
- The inefficiency of the inspections system and the need to cut public spending to address public deficits or stay within limited state budgets without compromising regulatory effectiveness.[3]

In general, the more factors trigger a push for inspection reform, the stronger the momentum for change and the larger the scope of reform. This pattern has been evident in most countries where extensive inspections reforms have been implemented, notably in Bosnia and Herzegovina, Mexico, and the Netherlands.

1.2.1 Lack of Effectiveness of Inspections

The ineffectiveness of inspections in protecting public health and safety is one of the primary factors that may prompt inspections reform. Tragic losses resulting from industrial accidents (e.g. the Enschede disaster in 2000 in the Netherlands which caused 22 deaths, close to 1,000 injuries and EUR300 million in damages) or the collapse of buildings during earthquakes (e.g., in Mexico), and subsequent public demands for better protection against risks, pushed the Dutch and Mexican governments, for example, to reform inspections. Public perceptions that inspections systems were ineffective also helped push reforms forward in Bosnia and Herzegovina and in Tajikistan.

Since health, safety, and environmental problems are also issues inspectorates can use to justify tighter inspections coverage and more intrusive inspections (and thus to resist reforms that streamline inspections), it is critical in such contexts for reformers to develop an approach to reform, and a communications strategy, that builds public trust that inspections reform will improve outcomes. In such circumstances it is important for reformers to stress that available research does not indicate a correlation between a high rate of inspections and improved regulatory effectiveness. In the Kyrgyz Republic, for example, despite high inspections coverage by the Sanitary and Epidemiological Service,[4] mortality rates from diarrheal diseases are

[3] In Canada, for example, cutting the costs of inspectorates was one of the main factors driving inspections reform. Cost-cutting is also now an important motivation for the Dutch reform program.

[4] Thirty-three percent of the Kyrgyz Republic's individual entrepreneurs and 25 percent of its small and medium companies were inspected by the Sanitary and Epidemiological Service between January 2008 and March 2009. IFC (2010). "Investment Climate in the Kyrgyz Republic as seen by SMEs."

much higher than the rates in other countries that have a much lower rate of inspections. The risk of dying from diarrheal diseases is 27.7 times lower in Latvia than in the Kyrgyz Republic. A high rate of inspections does not lead to higher tax revenues either; indeed, while the annual number of inspections decreased in Latvia between 2003 and 2005, the tax yields resulting from these audits increased, thanks to risk-based planning of inspections.[5] Evidence from Ukraine also shows that, within the same country, regions with higher rates of inspections do not appear to have better regulatory results.[6]

1.2.2 Excessive Administrative Burden for Businesses

The excessive cost of inspections for business is another major motivation for inspections reform and for the WBG's strong involvement in this work. Inspections create administrative burdens in several ways: for the cost of the staff involved, the fines imposed, and, in many countries, for the unofficial payments that are also part of the inspections process. Revenue is also lost during inspections or consecutive to business closures caused by inspections. This burden can be measured by surveys, standard cost model exercises, and other tools.

In countries where business associations are strong, these associations often respond to such costs by lobbying for inspections reform. Such pressure from the business sector has been an important force for reform in Mexico, the United Kingdom and also in Mongolia. In countries where businesses' ability to lobby for their own interests is limited (e.g., in Central Asia), the donor community (including the WBG) may raise the issue and advocate for inspections reform (e.g., Tajikistan). In some cases, governments themselves may push for inspections reform to improve their investment climate in the hope that this will boost foreign direct investment, business profit and tax revenues and perhaps improve their leaders' image as economic reformers (e.g., the Kyrgyz Republic). One of the barriers to reform, however, is that it is often difficult to find the data to establish the extent of the burden inspections impose. Enterprise surveys and reports can play an important role in helping to document the case for reform – if they cover inspections issues adequately.

Excessively frequent and arbitrary inspections not only impose direct costs on the private sector but can have a deeper adverse effect on the trust and competitive climate necessary for investment and growth. In many countries that lack clear regulations, criteria for the selection of businesses to be inspected and procedures for inspections, sanctions, and appeals, businesses frequently complain about the discretionary powers of inspectors. Officials with excessive discretion often select businesses to be inspected based on personal interest or connections, demand compliance with unknown or meaningless regulations, and interpret

[5] Olegs Sejans (2009). "Case Study on Tax Control Reform and Implementation of a Risk Analysis System in the State Revenue Service of Latvia," IFC.

[6] The results of the 2007 "Business Environment in Ukraine" survey showed that regions with a higher frequency of tax inspections did not have higher tax revenues than regions where the frequency of tax inspections was lower. Rather, the greater the number of active businesses, the higher the tax revenue.

requirements inconsistently – with one inspector sometimes requiring a change in practices and the next one calling that very change a violation of the rules. Businesses also complain about inspectors harassing them and threatening to close their operations instead of advising them about how to comply with regulations.

The lack of transparency of an inspections system and the excessive discretionary power of its inspectors can make entrepreneurial activity more uncertain in ways that deter investments and may have a negative impact on business growth. Before inspections reform in Colombia, for example, initial inspections from all key municipal departments were *de facto* required for any new business, and a negative inspection could close down the business. This practice jeopardized investments and deterred the creation of new businesses. In Jordan, the IFC's team found during its initial assessment in 2007 that potential entrepreneurs saw the risk of different reviews by different inspectors – in which one inspector could validate a construction project or an initiative and the next one could shut it down – as one of the main problems affecting investment decisions.

At the same time, excessive discretion and the arbitrary use of inspections distort competition by putting businesses that do not have the right contacts with inspectorates at an unfair disadvantage. Arbitrary inspections may harm one company but leave another one unscathed. This pattern is quite common in many countries, and it is often used by incumbent businesses with extensive political ties or deep "links" to regulators to harm potential competitors. In Ukraine, for instance, a new, high-quality corporate catering business we studied was cowed into avoiding bids for new contracts by repeated food safety inspections made "upon request" of the main incumbent business in that market.

An ineffective inspections system can also seriously harm export businesses. Not only will some potential private buyers in other countries refrain from purchasing goods from a nation with an inspections system that is not perceived to be reliable but, still worse for exporters, entire classes of that country's products may be banned by other countries' regulators. This problem is particularly acute in the case of food products because large food markets such as the European Union conduct regular audits of the regulatory systems of would-be exporters, with a particular on inspections, especially of high-risk products such as meat, fish, and dairy products. Such audits are very strict and frequently result in bans on entire classes of products. The EU has thus refused imports of fish from Cambodia, of meat and many other animal products from Ukraine, and of other products. Maintaining high safety standards that ensure exports win access to other markets is particularly important today because other markets that were once accessible to many producers have also imposed quality barriers. Food products from the Kyrgyz Republic, for instance, are not well-accepted by the country's main trading partners (Russia and Kazakhstan) and must be re-tested in importing countries, a practice that hurts Kyrgyz exporters.

1.2.3 Systemic Problems in the Inspections Regime

1.2.3.1 Lack of risk focus: inspections do not target the right objects

Failing to use risk-based planning principles and inspections tools is one of the major problems that makes many inspections systems ineffective. Many inspectorates still do not target inspections based on an analysis of which businesses pose the greatest risk – which we define as a combination of the *probability* and the *magnitude* of a potential dangerous incident. Regulators often are reluctant to use risk-based targeting because they favor an antiquated approach that treats blanket inspections coverage as their goal. In reality, however, trying to achieve blanket coverage works poorly for two reasons:

- Trying to inspect all businesses, all the time means regulators spend too little time in each business and spread their resources and attention too thin over too many objects (See Box 3).
- Focusing on high-risk targets gives regulators time to inspect more risky enterprises in depth and to have deeper interactions with those businesses that can include sharing information and recommendations.

BOX 3 Trying to Inspect all Businesses Means Inspectors Do Not Have Enough Time to Examine Each Business

France puts a high priority on labor legislation and regulation and consequently has a well-staffed inspectorate. Yet even in France, and even assuming that French labor inspectors spend 50 percent of their work time actually inspecting businesses (and that is a high assumption given transportation time and the other administrative tasks inspectors must perform), inspectors would only be able to spend only 1.5 hours a year on each business each year if they inspected all businesses with at least one employee. French inspectors could spend an average of nine hours a year on each business they examined, however, if they only inspected all businesses with more than 10 employees.

Source: IFC staff calculation.

Even when inspectorates try to change their approach and implement risk-based targeting, they often have no information systems in place that allow them to select businesses for inspections based on pre-determined risk criteria such as a business' type of activity, size, location, or previous record. As a result, inspectorates often revert to trying to inspect all businesses or to selecting inspection targets based on inspectors' subjective views or on sheer convenience (e.g., closeness to the inspectorate's office).

Indeed, in many countries inspectorates not only ignore risk-based analysis but practice a kind of "reverse selection" in which inspectors target smaller, weaker businesses. Given their small size and limited operations, such businesses often pose negligible risks to the public. Yet these businesses are also often the most likely to pay bribes to inspectors, because they

have little knowledge of their rights or of what the regulations actually mandate and few high-level contacts. Such inadequately targeted inspections are costly for the state and for businesses, ineffective for the public, and breed corruption.

"I know, my inspectors do nothing serious, they just go around and inspect small businesses in order to get bribes from them, and neglect the really important objects."

—The head of a Tajik inspectorate in 2005, prior to inspections reform.

1.2.3.2 Lack of focus on key issues during inspections

Insufficient focus on serious risks is often also evident in the inspection process itself. Many inspectors do not focus on key issues and essential safety requirements but on petty matters and paperwork (e.g., on making sure the business has all its required licenses and displays them properly, has filled all its logbooks, and has posted the appropriate documents on the wall, etc.) Such practices were common in Mexico before its inspections reform. In Mongolia, inspections still routinely focus on trivial issues that have no impact on public safety and inspectors regularly make apparently random recommendations that do nothing to promote safety (e.g., one inspector we know of required a businessman to write down the personal history of his employees for the last three generations).

What is at stake in the way inspections are carried out is not just the troubling tendency of inspectors and inspectorates to focus on the letter of the law rather than its spirit but the broader goals and attitudes of inspectors. They often seem to consider businesses "guilty until proven innocent" and to look for infractions, however petty, to use to pressure that business, sometimes threatening entrepreneurs with heavy sanctions for irrelevant or imaginary violations in the process. In Kenya, for instance, it is common practice for municipal hygiene inspectors to conduct inspections while trade businesses are loading or unloading, note that some (sealed and airtight) milk packages are on the floor and that the floor is dirty, and then threaten the entrepreneur with arrest (or with impounding his or her goods) to try to force him or her to offer a bribe. This process frequently ends with an arrest and an entrepreneur spending a weekend in jail awaiting a court hearing.

The larger issue here is not individual corruption and rent-seeking behavior by some inspectors but the tendency of many inspectorates to rely on threats and sanctions instead of focusing on promoting compliance with critical public safety rules by sharing information and educating the public. As such a confrontational approach is often deeply rooted in an inspectorate's culture, changing that attitude, and moving toward a more cooperative approach, can be one of the most difficult tasks of an inspections reform.

"Inspectors often threaten to close down our businesses. I am afraid of inspectors because they have so much power. Just hearing the word 'inspector' makes me tremble."

—Focus group participant, Mongolia.

1.2.3.3 Poor communication makes business compliance difficult

Since improving compliance with key public safety rules is the primary mission of regulators, informing the public and businesses about those rules ought to be one of their most important roles. Yet inspectorates in both developing and developed countries often fail to communicate their requirements simply and effectively to businesses. Before the recent inspections reform in the United Kingdom, for example, a 2003 study suggested that 62 percent of small food business proprietors did not understand which food safety regulations were relevant to them.[7] The situation is even worse in several of the successor states to the Soviet Union, where information on the many technical requirements businesses must comply with is often not even available to the public. Businesses sometimes have to purchase this information or simply cannot find any access to it, which makes compliance wellnigh impossible (See Box 4).

BOX 4 In the Kyrgyz Republic, Many Technical Requirements are Not Available Publicly

In the Kyrgyz Republic, information on the 220 health and sanitary regulations the nation's businesses must comply with is not available from the Ministry of Justice. Although these regulations are listed on the Web site of the Sanitary and Epidemiological Service,[8] their content is not displayed. In addition, only 57 of these 220 regulations are available on the "Toktom/Adviser" database, an electronic archive that contains most of the country's legislation. Although some regulations are available in hard copy, these print versions are not always available for consultation or sale. Thus many businesses have no way to get access to, or even to purchase, full information on the full range of legislation and regulations they must obey.

As a result of their lack of knowledge about the rules, businesses (a) often fail to comply with safety rules, which harms the public, (b) are more frequently subject to sanctions, and (c) are more vulnerable to abusive practices by inspectors.

Source: IFC (2010). "Investment Climate in the Kyrgyz Republic as Seen by Small and Medium Enterprises."

One of the aims of inspections reforms should be to push regulators to put more emphasis on ensuring compliance with health and safety regulations through improved communication of requirements. As the "Hampton Review" noted, "regulators should provide authoritative, accessible advice easily and cheaply."[9]

[7] Cited in Philip Hampton (2005). "Reducing administrative burdens: effective inspection and enforcement," HM Treasury.

[8] See http://www.dgsen.kg/.

[9] Philip Hampton. (2005).

Although the focus on finding fault by any means necessary is generally driven by individual purposes or by the institutional culture of inspectorates, it usually must rely on actual rules violations because, at least in most countries, it is difficult for inspectors simply to create violations.[10] Thus the fact that inspectors are finding a large number of violations or imposing frequent sanctions (or threatened sanctions that lead to bribes) usually points to the presence of an extensive body of rules and detailed prescriptions that businesses often do not respect. Such a profusion of rules often can also point to a broader regulatory problem: that the rules businesses have to comply with are obsolete or excessively detailed.

As we noted earlier, Mongolia is a good example of a country that maintains numerous obsolete and over-prescriptive requirements (See Box 1). Many other countries have over-prescriptive rather than performance-based rules and norms – and impose compulsory standards (which were often adopted several decades ago) on a very wide range of goods and services. A good example of such standards can be found in Ukraine (See Box 5), where Soviet-era standards applying to food are not just safety norms but recipes that prescribe the exact composition and preparation of many food products. Similarly, norms for food-processing hygiene in Ukraine and other countries of the former Soviet Union tend not to be "performance-based" (e.g. "it must be possible to clean food-preparation surfaces easily and ensure that bacteriological parameters can be met after cleanings") but "inputs-based" (e.g., "there should be white tiles up to 1.80 m of height on the walls").

The advantage of performance-based requirements is that they allow for innovation, as entrepreneurs can develop or adopt new materials and approaches as long as they meet the safety targets the regulations establish. Prescriptive requirements hamper innovation and often block the adoption of new technologies because they require entrepreneurs to follow the "recipe" described in the regulations. Excessively prescriptive norms also lead to intrusive and burdensome inspections, particularly when the rules are outdated, and often make efforts to enforce regulations ineffective. When standards are over-prescriptive, inspectors will find many violations because the rules are so detailed and sometimes so obsolete that they punish businesses for using new materials, equipment, or methods that businesses must try to use even if they violate the rules because they are now essential to production. The resources spent pursuing such violations do not contribute to protecting health and safety.

[10] There are, of course, a number of countries where the abuses of the executive are so great, and the balance of power so detrimental to business, that inspectors may simply make up violations. There are also intermediate cases such as Kenya where, if inspectors make up violations, the courts will generally rule in favor of businesses but only after such unpleasantness and costs (including arrest) that most businesses will prefer to pay fines or bribes.

BOX 5 In Ukraine, Inspectorates Monitor Compliance with Obsolete and Over-prescriptive Standards

Many of the standards Ukraine's regulatory agencies monitor compliance with are out of step with present-day business practices. For example, the nation's health regulations for airline meals were adopted in 1973 and have not been reviewed in the more than 30 years since they were established. In that time, many new food products with longer shelf-life and improved packaging and storage technologies have been developed. Nevertheless, the shelf-life and storage conditions of products offered to passengers remain the same. One obsolete requirement mandates that airlines may only use ice to maintain proper food storage temperatures aboard an aircraft. Today, there are modern cooling agents that are much more convenient to use than ice and the vast majority of international carriers use these techniques. Using them in Ukraine requires a specific authorization, however, because regulators resist updating their obsolete standards.

Source: IFC (2007). "Business Environment in Ukraine."

1.2.3.4 Problems with the institutional structure

Ineffective inspectorates often suffer from institutional dysfunctions that range from useless inspections functions to overlapping jurisdictions among inspections agencies and between national and local regulators to outdated staffing policies and counter-productive pay practices.

As we have discussed in the sections above, some inspectorates oversee compliance with rules that simply should not exist because they do not help protect public health, safety, and the environment or help guarantee state revenues. The very existence of these inspectorates – or of the departments within these inspectorates that enforce the useless rules – should be reconsidered.

Many countries also maintain standardization agencies that have excessively broad mandates, powers, and staffing. While in more appropriate regulatory systems such agencies are small and do not regulate businesses directly, some countries still have standardization agencies with thousands of staff members who are empowered to control almost all aspects of business activity; Kenya's bureau of standards and the standardization and consumer protection body in Ukraine are conspicuous examples of bloated regulatory agencies (See Boxes 1, 2, and 5).

Overlapping jurisdictions that put multiple inspectorates (or several departments of a unified inspectorate) in charge of supervising compliance with the rules for the same business activities can create even more widespread and vexing problems. Such duplication is frequent in food safety and labor safety regulation as well as in the enforcement of building safety rules (in which architectural and fire safety inspections may check compliance with the same rules or, and even worse, with different rules). Ukraine's inspections system offers an extreme example of duplication and overlap in regulatory functions (See Box 6).

BOX 6 Duplication and Overlap of Functions in Ukraine's Inspection System

The structure and scope of the responsibilities of Ukraine's regulatory agencies creates so much duplication of function that as many as eight different inspectorates may inspect the same aspects of business activity. Six inspectorates control land use (and four more control the use of minerals), six inspectorates oversee tax-paying and the collection of duties, five inspections agencies control consumer standards, four regulate the generation and use of electric power, and eight different authorities inspect plant cultivation and seed production.

Number of inspectorates overseeing similar issues of business activity:

Communication and radio broadcasting	4
Compliance with labor legislation	6
Environment and sub-surface mineral use	4
Compliance with consumer standards	5
Transportation	5
Education, science, and intellectual property	6

Inspection functions also often overlap, creating gray areas where the same issue can be controlled by several agencies with different perspectives. Enforcement of fire safety rules (controlled by fire safety authorities) often overlaps with enforcement of labor safety requirements (controlled by the labor safety inspectorate) and the enforcement of labor safety and sanitary requirements also regularly overlap. At the same time, the vast responsibilities of the State Committee for Technical Regulation and Consumer Policy (SES) cause its work to duplicate much of the work other agencies do. In practice, the absence of clear and specific boundaries for the inspections functions of different inspectorates means that inspectors from some agencies check issues that officials from other agencies are also authorized to control – and sometimes their findings, recommendations, and orders conflict.

Although this kind of duplication is a common problem in many countries where the inspections system needs to be reformed, it is particularly acute in Ukraine because Ukraine has two to five times more regulatory agencies than many similar countries do. As of 2008, approximately 85 of Ukraine's state agencies had a mandate to inspect businesses. Sixteen agencies have similar authority in Latvia, 30 in Serbia, 26 in Montenegro, 26 in Slovenia, 44 in Uzbekistan, approximately 40 in Belarus, 31 in Tajikistan, 31 in Albania, 22 in the Kyrgyz Republic, 19 in Armenia, and 20 in Georgia.

Source: IFC (2009). "Investment climate in Ukraine as seen by Private Businesses."

The problems such overlapping mandates cause are even more serious when different agencies check compliance on the same issue, sometimes under different rules. Before inspections reform in Mexico, for example, three national institutions regulated the location and position of fire extinguishers under different rules. As a result, most businesses were violating at least one rule.

Duplication in inspections between central and local levels of a single inspectorate and between national institutions and local governments can also pose serious problems. In the Mexican case cited above, for instance, in addition to the three national institutions

regulating the location and position of fire extinguishers, local environmental authorities were authorized to regulate this issue, adding to the regulatory burden for businesses.

Local governments indeed often impose a heavy inspections burden on businesses, both in developed and developing countries, and many problems related to inspections are caused or exacerbated by the numerous local inspectorates. In Kenya, the majority of inspections are conducted by local authorities, even when the regulations are national (as most of Kenya's national regulators delegate the bulk of inspections to municipal authorities). In the Kyrgyz Republic, local governments are responsible for 40 percent of inspections of farmers.[11] Before the recent reforms in the United Kingdom, local authorities carried out four times as many inspections as national regulators.[12] Before reforms were carried out in Colombia, businesses in Bogota identified the initial inspections performed by the municipality's various inspectorates (fire, sanitary, environment, and police) as a key constraint to business development. The Netherlands maintains only 14 national inspectorates but conducts 56 inspecting functions at the local level,[13] and ACTAL, the Dutch Advisory Board on Administrative Burden estimates that these local inspections account for at least one-third of the nation's total administrative burden from inspections.

Local inspections are a major problem for businesses not only because they are so numerous but because some of their functions overlap with those of national regulatory institutions. At the same time, local inspectorates are more difficult to reform than national inspectorates because they are inherently decentralized, and each city or municipality may need to be the target of a separate reform effort. Even in centralized countries where national institutions can adopt general guidelines for reform, successfully implementing reforms will also require extensive work at the local level; in federal or highly decentralized states, it may prove very difficult to push reform effectively from the capital.

These institutional dysfunctions are costly for both governments and businesses: governments waste resources inspecting the same issue in the same business several times while multiple inspections multiply the burden on businesses. These burdens are often compounded by the absence of coordination and information-sharing among inspectorates, a failing that adds to their tendency to duplicate one another's work and undermines the effectiveness of inspections.

Staffing problems and unwise pay practices often also add to the institutional dysfunctions of inspections systems. The regulatory agencies in developing and emerging economies often carry excess staff, in part because governments regularly use such public service jobs to appease social tensions by adding to employment, to reward supporters, and to accomplish other political goals. In the case of the nations of the former Soviet

[11] IFC (2010). "Investment Climate in the Kyrgyz Republic."

[12] Philip Hampton (2005).

[13] Ferry de Rijcke (2010). "Risk Focused Inspections in the Netherlands."

Union, vast public agencies are simply a feature inherited from the previous system. When inspectorates are overstaffed, more inspectors naturally leads to more inspections and more burden on businesses. Overstaffing such public service jobs also makes it difficult or impossible for the state to pay adequate salaries and large numbers of underpaid staff clearly create a serious risk of increased corruption. Conversely, some inspectorates have too few personnel, leaving them unable to inspect even high-risk targets adequately. Based on an informal review by WBG staff, however, we believe that understaffing is uncommon and is only a problem for a minority of nations.

Even when regulators have many inspectors, those inspectors are often under-qualified, and their limited technical capacities can hamper the quality of inspections – especially inspections of business that use advanced technologies. The low general skill-level of inspectors appears to be a result of a combination of factors, including the lack of specialized and on-the-job training by inspectorates, low salaries, biased selection procedures, and the limited prestige of the inspections profession. These issues often discourage the best-qualified candidates from even applying to join inspections agencies, and this clearly has negative consequences for the effectiveness of inspections.

Inadequate compensation and a lack of incentives to reward more professional and effective inspectors may also negatively impact the quality of inspectors' work. Bad pay practices include both the lack of financial incentives (e.g., bonuses) for good performance and the use of improper indicators to measure inspectors' performance and to allocate bonuses when bonuses are available. Establishing target levels for fines for individual inspectors or for units of inspectors or, more generally, taking the number of sanctions or the amount of fines inspectors give out as a positive performance indicator is a very bad practice, for example, as it encourages inspectors to impose sanctions on businesses for any small reason they can find – and of course it also gives them an incentive *not to* inform businesses about requirements so that they can find more violations.

Many inspectorates could achieve better results with a smaller staff of better-skilled, more professionally trained and better-rewarded inspectors.

1.2.3.5 Lack of a clear regulatory framework for the inspections process

One basic problem common to most countries in need of inspections reform is that the ways inspections are planned, carried out, and followed-up are often haphazard or left to the discretion of individual inspectors or their supervisors. In these circumstances, the legal norms defining the rights and obligations of businesses and inspectors and detailing the inspections procedures tend to be under-developed and the excessive discretion of inspectors leaves businesses open to widespread abuse.

Such a haphazard approach to inspections is reflected in the widespread bad practice of allowing inspections without a formal order from the inspectorate's management or at the will of an individual inspector, regardless of any pre-determined selection criteria. Left to

their own discretion, inspectors may choose to inspect the businesses that are most likely to offer unofficial payments or those that are simply near their office instead of examining the firms that represent the greatest safety risk. In some cases, inspectors are not even formally required to present an ID or other proof of their status when they inspect a business.

The lack of clearly defined procedures for the inspections themselves often means that inspectors do not check compliance according to a standard checklist that reflects the most important rules businesses must obey. Inspectors may choose instead to check compliance with obsolete or secondary requirements that are not essential to public safety – and they clearly often have very broad discretion in the "interpretation" of these requirements, especially in countries where some or all of those regulations are not available to the public. Many countries also lack formal procedures regulating the conclusion of inspections or requiring inspectors to write a report that must be signed by the inspector and a representative of the business inspected. When no such record of earlier inspection results is available, the findings and demands of consecutive inspections may well be contradictory.

Inspection follow-up procedures often appear haphazard as well, as many countries lack a transparent sanctions grid for violations or an efficient appeal procedure or a systematic way to plan follow-up or control inspections for businesses that have committed violations. Inspectors are often responsible both for recording violations and determining sanctions; this dual responsibility fosters collusion between inspectors and businesses, especially when sanctions grids are vague and contain important gaps between minimum and maximum sanctions and fine amounts. Appeal systems often appear complicated, costly, and biased in favor of inspectors. In many countries, businesses fear retaliation if they appeal and therefore rarely report or appeal abuses.[14] The lack of proper planning for follow-up inspections may be equally problematic, both for businesses and for public safety, because this practice causes some businesses that have committed major violations to escape a control visit – especially if they have the right connections or have paid the right people – while other business that have committed minor infractions suffer repeated inspections.

When procedural guarantees for the rights of businesses are so weak, inspectors have excessive discretionary power that can enable them to abuse inspected businesses or arbitrarily handle similar cases in very different ways. In the absence of clear norms for the inspections procedure, inspectors can decide which businesses will be inspected, how inspections will be conducted, and what the consequences of rules violations will be. Before inspections reform in Mexico, for instance, inspectors had the legal authority to close a business without due process. (They even carried special ribbons to seal doors and windows.) Such abuse of

[14] Such facts are usually difficult to capture, except through focus groups, but anecdotal examples from focus groups abound. In the Kyrgyz Republic, for instance, leaders of one large business reported giving presents worth US$10,000 per year to officials from of regulatory bodies, at the regulators' request, but did not want to use the appeals system because they felt it was biased in favor of the inspectors. In Uzbekistan, one business representative who appealed successfully in court against the tax authorities noted that his victory was not worth the time and money he had to spend to achieve it.

power is particularly striking in Kenya, where many inspectors have the power to arrest and detain entrepreneurs and corrupt inspectors regularly arrest businesspeople on Friday afternoons, and threaten to hold them in jail all weekend before a judge can hear their *habeas corpus* case, in order to maximize unofficial payments.

Relying primarily on sanctions, or on the threat of sanctions, to achieve compliance with regulations has generally proved ineffective. If businesses are not properly informed about the rules or those regulations are obsolete or unworkable, they often will not comply with the regulations even in the face of possible sanctions. Unfortunately, many inspectorates (and their staff members) still see their role as that of a policeman: to find violations and punish them. In 2009 in Mongolia, for example, 22 percent of businesses went through a follow-up inspection for a violation while 21 percent of businesses had to pay a fine as a result of non-compliance.[15] The fact that these percentages were virtually identical suggests that Mongolia's inspections system focuses on the imposition of sanctions at least as much as on fostering compliance with the rules. In countries where the inspections system has been reformed, however, the identification of violations typically results in follow-up inspections rather than in the imposition of fines (except in the case of particularly severe or repeated violations). Efficient enforcement systems should reward the quick correction of problems – and use sanctions only on a graduated basis and as a complement to improved information and education about how to comply with the rules.

Even as many inspectorates focus, perhaps unwisely, on finding violations and applying sanctions, the way those sanctions are structured often further undermines the efficacy of this approach. In many cases, the fines that punish violations are too small to be an effective deterrent, and unscrupulous businesses prefer to pay the fines than to incur the costs and inconvenience of complying with the rules. Britain's Hampton Review, reported numerous cases in which the value of the possible fine was lower than the commercial value of the regulatory breach itself, citing in particular one company that was fined only £840 for dumping thousands of tons of illegal waste over a 10-year period.[16] Outdated legislation that fixes the value of fines in absolute terms, without indexing them to inflation, has helped make such situations commonplace in many parts of the world.

The accountability of inspectorates for their work is also often rather haphazard, in part because in many countries – and not just in transitional or developing economies but also in many OECD nations – the measurement of regulators' performance is nearly non-existent or, and even worse, is based on the wrong principles. Instead of measuring hazard mitigation or the reduction in adverse outcomes, many inspectorates evaluate their performance based on the number of inspections they conduct or the amount of fines they collect. It would be more logical to see a high number of violations as evidence of poor performance by regulators, as it suggests that they are failing to promote compliance with the rules, but many

[15] IFC (2010). "Business Inspections in Mongolia."

[16] Philip Hampton (2005), p. 39.

agencies take the opposite view. Statistics measuring the desired outcomes of inspections work (e.g., safer food, safer workplaces) also are often hard to find or of poor quality – and, even when they are available, they are rarely correlated to regulators' work. Many countries also lack systems that hold their inspectorates accountable by requiring regular reports to the national legislature or the public.

1.3 Summary of Results: Ineffective Systems and Corruption

Deeply flawed inspections systems undermine compliance with public safety rules and limit the effectiveness of inspections in guaranteeing public health and safety. Such systems seem to work well only to benefit some individual inspectors.

The prevalence of corruption in these systems also undermines the prestige of inspectorates among the business community and the society at large. Under such circumstances, inspectors often come to be seen as enemies to hide from rather than protectors of public safety. Compliance with regulations falls even further as businesses come to believe that the rules exist to punish them rather than to protect the public interest.

Chapter 2. Reforming Inspections: Challenges and Solutions

2.1 The Challenges

2.1.1 Many Opponents, Few Supporters

The first challenge facing an inspections reform program is to gather the support needed to create momentum for reform.

This challenge can be daunting because inspections reform is rarely welcomed by inspectors or by higher officials within inspectorates, who often fear that they will lose their job, their power, and their opportunities to collect bribes.

Potential reformers themselves may be hesitant to work for reform for fear of being blamed in case of a serious accident: If the number of inspections decreases and a dramatic accident happens, reformers indeed may well be the first to be blamed.

Although in developed countries such as the United Kingdom businesses and business associations have been strong advocates for inspections reform, businesses in emerging markets are often weaker, more divided and either lack powerful business associations that can speak effectively for their interests or are simply afraid to speak up. As a result, they usually are unable to lobby successfully for their own interests on issues such as inspections reform. This kind of reform also faces an uphill battle because many businesses that have the right contacts within key inspectorates (and these are usually the most influential firms) may lobby against reform because they benefit from the existing inspections system and use it to fight off competition or to deter new businesses from entering the market.

Since inspections reform often has more opponents than supporters, at least at first, it is important for the reform effort to win early, high-level political support. Thus it was critical that reform won the backing of the president's office in Uzbekistan and Tajikistan and of influential parliamentarians and ministers in Ukraine and Mongolia and that, in the United Kingdom, the Hampton Review was commissioned by the national treasury when the powerful Gordon Brown was chancellor of the exchequer. Successful reform programs are usually

coordinated from the center of the government, while reforms led from lower levels or by a single, not-very-powerful ministry or agency often falter because reformers lack authority over the various ministries and agencies that control inspections functions.

Since the inspections problem is, by virtue of its multi-faceted nature (it is not about changing one procedure and is not concentrated in one location or agency), often underestimated, conducting a study to assess and publicize the problem can also be a very useful way to advocate for reform at the highest level. Britain's Hampton Review is a leading example of how such an assessment of the inspections system can be used effectively to initiate and promote reform. The WBG has also used enterprise surveys to create and sustain support for transforming inspections regimes in many nations.

2.1.2 Reform is Complex

The complexity of inspections reform poses many challenges for reformers. As we noted in the previous chapter, simply cutting most inspections functions is not an option because those inspections are necessary to protect health, safety, and the environment. The problem for reformers, therefore, is not to abolish inspections but to develop mechanisms that will make them work better. This is not easy, however, for the following reasons:

- Effective reform involves changing the practices of a large number of institutions including inspectorates, several ministries, and even the parliament.
- Although it is relatively easy to modify inspections legislation or to introduce new legislation on this issue if there is political support for reform, it is more difficult to ensure that inspectorates will actually implement this legislation. Thus reformers need to work hard to see that reforms such as risk-based selection of businesses to be inspected are actually put in place, even after reform laws have passed.
- The reasons inspections system become dysfunctional are always numerous and some of them often go beyond the scope of inspections reform. It is usually beyond the scope of reform, for example, to review the entire set of safety requirements businesses must meet. Yet even fully risk-focused inspections can become unduly cumbersome and ineffective if the regulations they are meant to enforce are themselves obsolete or over-prescriptive. One way to deal with this problem is to develop enforcement checklists that leave intact the underlying body of regulations but define the issues that inspectors will address in ways that ensure that inspections will focus on the essential rules.
- Issues involving the staffing and compensation practices of inspectorates tend also to be beyond the reach of inspections reform because they raise broader civil service reform questions. Yet international experience and best practices suggest that reforming human resources management in inspectorates is important to successful reform and to efforts to reduce corruption and rent-seeking practices.

- The institutional changes reform often requires (e.g., merging and closing some inspectorates) are complex processes and sub-optimal implementation of these changes may lead to disappointing results. In Mongolia, for example, problems involving overlapping inspections persist seven years after the General Agency for Specialized Inspections (GASI) was created by merging 13 inspectorates into a single inspections agency.
- Inspections reform is an extended process that will need to maintain momentum for change over a long period of time. That makes it important for reformers to involve as many stakeholders as possible to ensure that reform continues even as governments change.

2.2 Overcoming Challenges: Some Approaches

2.2.1 Top-down Reform: Rarely Fully Possible

In a handful of countries, the inspections reform process has been (or still is) able to succeed mostly on the strength of top-down pressure from one or several champions of reform at the highest levels of government, in part because that reform has been part of a broader plan to overcome an economic or a political crisis[17] or to achieve a "quantum leap" in economic performance. This is a rare feature for successful reforms programs, however; most effective inspections reform efforts have been supported not only by high-level government leadership but by a broad range of stakeholders within inspectorates, ministries, and the business community.[18]

Although sustained, high-level political support is necessary for the success of inspections reform (e.g., the support of the president was essential in initiating reform in Tajikistan and support from the prime minister was essential in Latvia), in most cases it is not sufficient and high-level backing must be complemented by a participatory process that involves as many stakeholders as possible, both from state agencies and the business community, throughout the reform. It is especially important for reformers to win the support of mid-level government officials, since they are the ones who must implement reforms and who can maintain the continuity of a reform program as governments change.[19]

[17] In Uzbekistan, the reform program relied primarily on top-down pressure from the president's office. In Tajikistan, however, although the president's office was the leading advocate for reform, the involvement of other stakeholders was critical to the success and sustainability of reform.

[18] In Latvia, the reform program was initially led by a leadership champion (the prime minister), but it also came to be widely supported by the management of the inspectorates (the chief of the labor inspectorate was among the most active reform advocates), by civil servants, and by the business community.

[19] In Latvia, pro-reform senior- and middle-level civil servants provided critical continuity for inspections reform while governments changed. Similarly, in Jordan, the replacement of much of the top- and middle-level management of the Ministry of Labor (its minister, secretary-general, and inspections director were all replaced during a very short period) did not jeopardize the implementation of labor inspections reform, largely because support for reform from all levels of the ministry's staff, including field inspectors, had been established from the start of the project. Indeed, in some countries (e.g., Belarus), such mid-level officials have even been effective in persuading high-level decision makers to support regulatory reforms.

2.2.2 Fostering Participation, Building Consensus

At the onset of the reform process, it is very helpful to conduct a stakeholder mapping exercise (See Box 7) and to develop a communication strategy that ensures that key regulatory agencies either support reform or that their opposition is, at least, relatively muted and can be neutralized. This means engaging the management of the inspectorates by demonstrating the potential benefits of reform from their perspective. Those advantages include:

- Increasing their effectiveness in managing inspectors.
- Winning the satisfaction of high-level policymakers, which can boost the career prospects of inspectorate managers.
- Building an improved image for the inspectorate in the media and the society at large by improving its effectiveness.

Another way reformers can show top officials that change may be in their own interest is by stressing that improved effectiveness by the inspectorates can safeguard top officials against the risk of being sacked as a result of a dramatic failure by their agency – a process that happens regularly in countries where inspectorates are very ineffective and, as a result, avoidable disasters happen frequently.[20]

In Tajikistan, reform won the support of some inspectorates because they understood that it had the support of the president, and therefore was going to happen with or without their support, and that it was in the interest of the inspectorates to participate in reform instead of being left out. Obtaining the initial support of one or two inspectorates can also be a useful way to engage more skeptical inspectorates in reform. The labor inspectorate in Latvia, for example, played an important role in piloting the reform program and in convincing other inspectorates of the benefits of reform.

In addition to winning the support of inspectorates, reformers need to win over representatives of key ministries and other state agencies that may benefit from reform (by increasing their influence, their public visibility, etc.). Key ministries likely to back reform include the ministry of justice (since reform should improve compliance with legal and constitutional requirements by inspectorates and may increase the power of the justice ministry to register and assess the actions of other ministries), the ministry of finance (since reform should help control public spending), and the ministry of economy (since reform should promote growth). Winning support for reform from as many government agencies as possible is important because it may make the reform program less vulnerable to backtracking by key agencies.

[20] In Tajikistan, for example, the management of the fire safety inspection agency has been replaced several times but its leadership has continued to engage in reform precisely because some managers have regularly been sacked as a result of major incidents that should have been avoided.

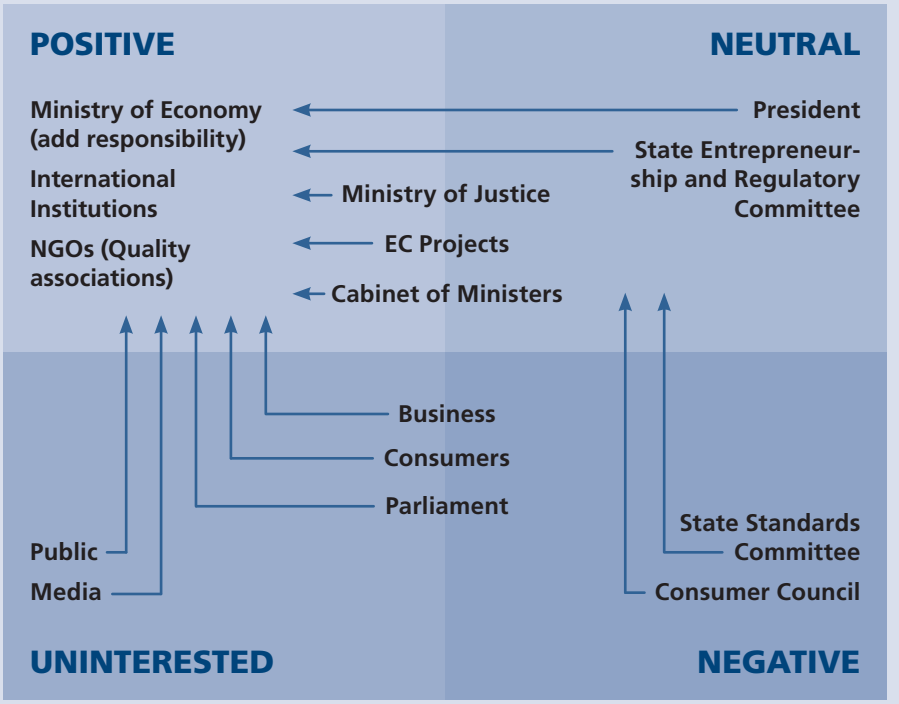
BOX 7 Mapping the Stakeholders

"Stakeholders are individuals or groups of individuals who have an impact or are affected by the activities, products or services of a company (or other organization)… Mapping stakeholders means identifying the expectations and powers of each right-bearing group. This helps establish political priorities whilst keeping a global vision of possible interactions between groups."[21]

Important stakeholders for inspections reforms typically include various government agencies, non-governmental associations (e.g. business associations), international organizations (e.g. the European Union), businesses, the public, the media, etc.

Once inspection reform promoters have become aware of the range of stakeholders they must work with, it is important that they break down the stakeholders based on their attitudes to reform (for reform, against reform, neutral, and uninterested), as the IFC did in its work in Ukraine (See Chart 1). It is also important to determine how to involve the different stakeholders – by building their capacities, informing them, consulting them, etc. (See Chart 2). Messages targeted to various stakeholders should be developed based on the results of this analysis.

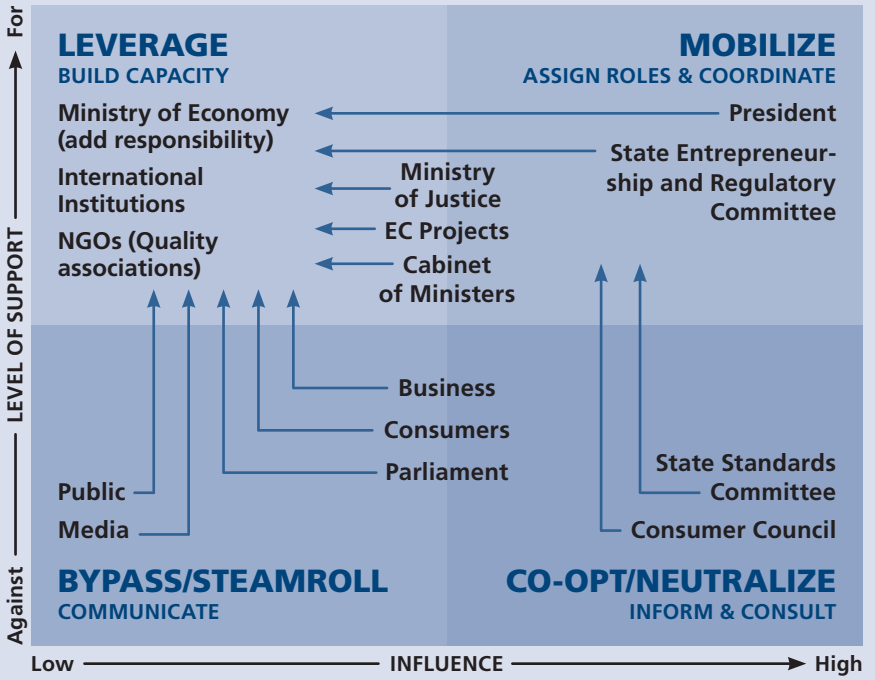
Current/Desired positions of main players



[21] Definition taken from "Proactive stakeholder engagement, Practical Guide for Companies and Stakeholders," December 2008, published by CSR Europe and available at http://www.csreurope.org/data/files/toolbox/Stakeholder_engagement.pdf.

BOX 7. *(Continued)*

Stakeholders May 2007 – Influence, Attitudes, Strategy



Source: Planning Communication Strategy, IFC Ukraine BEE Project (PowerPoint Presentation).

It is particularly important to engage representatives of the business community throughout the reform process, even in countries where the private sector is relatively weak or divided – indeed, it is important to make an extra effort to engage the private sector in places where it has trouble speaking for itself. Those who stand to benefit the most from reform must be involved in the process from the start to ensure that reform meets their needs fully and to help maintain momentum for reform. In countries where the business community is strong and well-organized, business can be a key champion of reform. Indeed in Georgia and Mexico customs inspections reform was made possible largely as a result of the strong support of exporters. Continuous pressure for reform by business associations in Latvia (along with support for reform by civil servants and, critically, the European Union accession process) helped sustain momentum for reform through several changes in government between 1999 and 2002.

To maintain stakeholders' engagement in reform and their support for change, reformers (including WBG teams) should use all the tools at their disposal to demonstrate the need for reform, the feasibility of reform, and the positive results that can be expected. Strategies such as publicizing business survey results on the burden of inspections, organizing

exchange visits with countries that have successfully implemented inspections reforms (e.g., Latvia and the Netherlands) and organizing roundtables for reform stakeholders can all be instrumental in gathering broad support for inspections reform.

Finally, international organizations and donors can play a key role in putting reform on the agenda, especially in countries that rely heavily on external donor support and in countries seeking to join organizations such as the European Union. In Tajikistan and Ukraine, for instance, the WBG strongly pushed national governments to initiate and implement reform. In Latvia, the prospect of joining the European Union (and of failing to join if reforms were not implemented) created momentum to improve the business environment, including the inspections system. The desire to join the NAFTA treaty played much the same role in Mexico. Latvia's government also proposed that inspections reform be included among the conditions for a World Bank structural adjustment loan. This arrangement both created pressure for the inspectorates to meet the loan's conditions in full and provided the government with additional resources (through a World Bank PHRD grant) to help implement reform. Combining that kind of pressure (from the World Bank, the European Union, etc.) with technical assistance has often proved to be a very effective way to promote complex and difficult reforms; it is, therefore, essential for inspections reformers to try to put reform in the context of broader goals such as accession to the EU or the World Trade Organization or the chance to earn multi-lateral credits.

BOX 8 Teaming Up Across the World Bank Group – How to Leverage Strengths to Make Reform Happen

It is crucial for inspections reform supporters both to put reform in a broader perspective (e.g., overall improvement of competitiveness, civil service reform) and to find solid reasons for neutral power holders to break with the status quo and the existing mechanisms (despite the fact that those arrangements often bring direct advantages, through corruption, to those who can tap into corrupt practices). In many countries, the most effective way to achieve such goals has been the joint work of the World Bank's Investment Climate teams, PREM teams and, where relevant, its FP teams. Making achieving inspections reform benchmarks a condition of winning policy credits gave strong leverage to those reform teams but focused and effective advisory work was also essential to making those conditions work. The reform programs in Tajikistan (2005-2006) and in Ukraine (2006-2007) are good examples of this kind of collaborative approach.

2.2.3 Making a Strong Case for Reform

To generate momentum for reform, it is also critical for reformers to demonstrate the problems linked to the inspections system very clearly, including its inability to ensure public safety, the burden it creates for businesses, and, in some cases, its high cost to the state. Since the existing data from inspectorates usually are not a reliable measure of the inspections burden (inspectorates in many countries report only a small number of their visits to businesses, while those in some other countries try to overstate their level of activity), reformers

often must design and implement specific assessment tools (e.g., surveys, focus groups, etc.) that demonstrate the problems of the inspections system and the priorities for reform. In Tajikistan, for instance, publishing the "Business Environment as seen by SMEs" survey in 2003 was instrumental in winning the president's support for reform. The survey showed that small and medium businesses were inspected an average of 16 times a year in Tajikistan and that inspections consumed an average of 17 working days in 2002. Tax authorities alone inspected 95 percent of entrepreneurs an average of seven times in 2002.[22]

2.2.4 Reform Design and Tools

Inspections reform can take place at one level or (preferably) at a combination of levels, ranging from the framework for inspections (i.e., changing the general rules and procedures of inspections), to the sectoral level (helping specific inspectorates work better) to the institutional structure (assessing which inspectorates should inspect what). Reform may also target all inspections, most inspections (inspections reform programs frequently targets all "non-revenue" or "technical and safety" inspections), or only a subset of inspections such as hygiene and food safety inspections. The scope and depth of inspections reform (which inspections are reformed and at what level) will be based on a country's unique context, including the political support for reform, the capacities of government agencies, the budget available, the objectives of reform, and other political considerations.

2.2.4.1 Framework reform: general rules and procedures

Reforming the framework for inspections is necessary whenever a lack of clarity in the rules governing the planning, execution and follow-up of inspections leaves excessive power and discretion in the hands of individual inspectors. Experience suggests that successful inspections reform almost always involves a substantial element of framework reform, and that framework reform is an effective way to achieve some rapid improvements, to root out the most obvious abuses, and to lay the foundation for sustainable reform.

BOX 9 Abuses of Power During Inspections in Kenya

Kenya offers some of the most blatant examples of abuse of power during inspections. Inspectors in Kenya can impound property, even for minor or imaginary offenses (such as putting packaged goods on the floor while loading or unloading, a practice some inspectors treat as a violation because the floor is dirty even though the goods are packaged and sealed), and many inspections result in the arrest of the business owner, manager, or another staff member. The main objective of such inspections seems to be to make entrepreneurs pay up. This kind of abuse is a result of the excessive discretion inspectors have to interpret the rules and impose heavy sanctions. Some so-called "city inspectors" actually have full police powers and are really law enforcement officials rather than inspectors.

Source: IFC Staff Report based on focus-group discussions.

[22] IFC (2003). "Business Environment in Tajikistan as seen by Small and Medium Businesses."

When problems related to excessive inspections and abuses of power during and as a result of inspections are very acute (See Box 9), framework reform very often is the easiest and fastest way to achieve improvements. If sufficient political support is available, this can actually be the easiest part of the reform program because good practices are well-known in this area and examples of them are numerous and because most of these changes involve introducing new legal provisions rather than making significant investments in training or in developing new practices. To rein in abusive inspectors, the framework reform legislation must provide businesses with strong procedural guarantees against abuse.

Since framework changes regarding the general principles for inspections can easily be designed to apply to all inspections, reformers should try to include as many inspection functions as possible in such reforms to achieve the largest possible impact. It is not always possible, however, to include all inspections in framework reforms because some inspectorates usually wield enough clout to demand successfully that they be exempted. Tax inspections, for example, are often regulated by the tax code and fall outside the scope of inspections laws – in part because the agencies that collect tax revenue tend to be quite influential. Thus the WBG and the International Monetary Fund often advise that tax inspections be regulated by specific legislation. Similarly, customs inspections are usually exempted from framework reforms because they exert control mainly at the border and under procedures different from those other inspectorates use. Since regulating banks requires more or less continuous oversight of their activities, banking supervision also is usually exempted from inspections laws. At the same time, law enforcement agencies also mostly fall outside inspections reform, although in many countries they conduct *de facto* inspections that can be an important problem. Police agencies often need more discretion in their crime-fighting activities than an inspections law typically will allow – although this concern can be accommodated by specifically exempting criminal investigations from inspections legislation while leaving "inspection-style" activities by law enforcement within its scope.

As a rule, inspections procedures are best defined and regulated through a framework inspections law or by some other high-level policy instrument like a presidential decree. Giving inspections reform this kind of stature helps ensure that it is not vulnerable to amendments from agencies that oppose reform or undermined because reforms conflict with other rules. (See Box 10 for examples of inspections reform laws.) In some countries, however, adopting a framework law or a high-level decree is politically difficult and may take years. Therefore reformers should start work on framework reform early in the reform program, even as they conduct other efforts (e.g., pilot programs with certain inspectorates, work to raise awareness) but bear in mind that framework changes must remain a key objective given their importance to the overall success of reform.

BOX 10 Examples of Framework Inspections Reforms

In Mexico, the 1995 "Federal Administrative Procedure" law regulated, among other issues, the practices for inspection orders, the presentation of ID by inspectors, the records provided at the end of inspection, and the rights of those inspected to contest the findings. By requiring inspectors to present ID before inspections, the law played a major role in eradicating the widespread previous practice of "pirate inspectors" preying on businesses.

In Georgia, the 2001 law "On Control of Entrepreneurial Activity" sought to reduce the discretion of inspectors by:

- Requiring that each inspector present a court order prior to conducting inspections.
- Limiting each inspectorate to inspecting a given business once a year unless it could prove the need for additional inspections.

In Bosnia and Herzegovina (both in the Republika Srpska and in the Federation, under parallel and roughly contemporaneous reform processes) reform laws adopted in 2004:

- Consolidated most inspection agencies into one inspectorate and thus clarified previous overlaps and duplications of jurisdiction and other uncertainties.
- Established clear and detailed process rules for all inspections, preventing abuses and enabling businesses to assert their rights.

As a result, both in the Republika Srpska and in the Bosnian Federation, inspectorates have embraced inspections procedures that focus on preventing and correcting violations rather than on punishing offenders. These procedures also emphasize teamwork and risk-based inspections and have increased the efficiency and effectiveness of inspections.

In Ukraine, the 2007 law "On State Control over Business Activity" sought to streamline business inspections throughout inspectorates and to reduce the inspections burden for businesses by:

- Limiting the duration of inspections.
- Introducing risk analysis as the key principle in inspections planning and setting inspection frequency limits for inspectorates that do not use risk-based planning.
- Defining the rights and responsibilities of control agencies and businesses in the inspections process.

In Tajikistan, the 2006 law "On Inspection of Economic Activity of Business Entities" gave the nation a unified regulatory framework for all inspections for the first time. This law defined the inspections process and mandated advance notice of inspections, the use of checklists during inspections, the registration of inspections in a logbook, and the submission of an inspection report detailing the results of the examination within five days of the inspection as well as the maximum frequency and duration of inspections. The law also stipulates that the amount of any fines assessed must be determined by the line manager of inspectors rather than by the inspectors themselves.

Sources: Jacobs and Associates (2005). "Case Studies of Reform of Government Inspections: Mexico."
IFC (2006). "Business Environment in Georgia."
IFC (2009). "Business Environment in Tajikistan as seen by Small and Medium Enterprises."
IFC (2009). "Investment climate in Ukraine as seen by Private Businesses."

2.2.4.2 Institutional reform: who inspects what

Institutional changes can be particularly difficult to achieve, especially when they involve closing, merging, or re-defining the functions of state or quasi-state agencies. Indeed this kind of reform is where the opposition of vested interests to change is likely to be strongest, and many governments have therefore avoided institutional reform altogether or made only marginal changes to their institutional arrangements.[23] Nevertheless, making reforms at the institutional level may be essential to achieve broader reform or to address one or more of the following problems:

- The sheer number of inspectorates is too high and involves a proliferation of agencies with very small mandates and many overlaps in jurisdiction that costs the state too much to maintain. Before inspections reform in the United Kingdom, for instance, Britain had 674 regulatory bodies at the local and national level[24] that employed 61,000 people. Their combined budgets amounted to close to £4 billion a year.[25]
- Major overlaps and duplications of function among inspectorates (e.g., several inspectorates checking compliance with the same rules). This problem frequently arises in the fields of food safety, occupational health and safety, environmental protection, and building safety.
- A lack of effective collaboration and coordination among inspectorates or of clear definition of their respective roles endangers the effectiveness of the regulatory system. Since information-sharing among inspectorates is usually poor, ill-defined jurisdictional boundaries can cause dangerous gaps in the control system that leave major risks unchecked. This problem is particularly critical in food safety, a field in which many countries have distinct veterinary, hygiene, and market inspectorates that do not exchange data with one another or with the health care system (which would allow quick reaction to food-borne disease outbreaks). Overlapping jurisdictions among these inspectorates can mean that there is no coherent control over the food chain, and therefore that food-borne hazards are not adequately monitored.

The proliferation of inspectorates can actually be worse in developed countries than in emerging economies because the regulatory systems of more established economies contain many legacy features and dated institutions. The United Kingdom maintained a particularly complex regulatory system before its recent inspections reform: regulatory inspection and enforcement was divided among 63 national regulators, 203 trading standards

[23] At the other end of the spectrum, some governments have made the mistake of thinking that institutional reshuffling would be enough to solve all their inspections problem (e.g., in Mongolia where a unified inspectorate was created, but for several years not much else was done), and this assumption has of course proved wrong.

[24] Philip Hampton (2005).

[25] Philip Hampton (2005).

offices, and 408 environmental health offices in 468 local authorities.[26] The multiplication of small regulators at the national level also made it difficult to obtain a comprehensive view of business risks (See Box 11).

BOX 11 The Number of Regulators in the United Kingdom Before Reform Was Excessive

"There are many small regulators at national level – of the 63 regulators covered by the review, 31 have fewer than 100 staff, and twelve have fewer than twenty. Small regulators, although focused, are less able to join up their work, and are less aware of the cumulative burdens on businesses. It is more difficult and more expensive to have a comprehensive risk assessment system if data is split across several regulators with similar areas of responsibility. In such circumstances, a holistic view of business risk becomes difficult, if not impossible. Small regulators are also more expensive. Regulators with fewer than 200 staff are on average more than £8,000 per staff member more expensive than regulators with more than 200 staff members. Smaller regulators which undertake fewer inspections also appear to have higher inspection costs. For example, regulators that inspected between 2,000 and 10,000 businesses per year had an inspection budget of £7,600 per inspection while those that inspected more than 25,000 businesses per year had an inspection budget of £1,000 per inspection."

Source: Philip Hampton (2005). "Reducing administrative burdens: effective inspection and enforcement," HM Treasury.

BOX 12 Good Practices for Institutional Reforms

- Inspections should focus on areas that are appropriate aspects of state authority in a modern market economy: protecting health, safety, and the environment and guaranteeing state income. Any inspections function that does not correspond to these criteria (e.g., examining how energy is used, whether recipes correspond to standards, how menus are written, etc.) should be canceled.
- Overlaps and duplications of functions among several inspectorates should be limited and, if possible, eliminated. When overlaps cannot be eliminated, the rules should be reviewed to ensure that the agencies that share control over an issue employ identical requirements and regulatory approaches and coordinate their communications effectively.
- The choice between more "radical" (merging and restructuring many entities) and more "conservative" (making minor revisions to the responsibilities and competencies of some agencies) institutional reforms should be guided by the conditions on the ground in any given country (e.g., the means to implement restructuring, the political and financial support for reform, etc). It can make sense to experiment with mergers in one area first (e.g., in revenue or food safety inspections) before deciding whether consolidation should be extended to other sectors.

Source: IFC (2008). "Overview of Business Inspections Functions, EU and Eastern Europe experience," note prepared by Florentin Blanc.

[26] Philip Hampton (2005).

Although institutional arrangement are very diverse across countries, and reform options can range from limited mergers and agency closures to setting up a full-scale unified inspectorate, some general good practices about fundamental inspections functions can be identified (See Box 12).

2.2.4.3 Function-specific reform: helping inspectorates work better

Working at the functional or "vertical" level is always a critical aspect of inspections reform because many critical elements of reform cannot be accomplished through changes in the legislative and institutional framework alone but require deeper implementation efforts within individual agencies to change specific regulatory functions.

Implementing function-specific reforms in one or two inspectorates as a pilot project can serve as an effective model for broader reform. Making such an initiative work, however, requires a combination of push from top policy makers and buy-in from the pilot inspectorates' management. However, sectoral reforms that are not backed up by a solid legislative framework are vulnerable to backtracking, especially if there is a change in management. Therefore while such agency-level work can be conducted without framework reform, it is more often done as part of a broader reform effort or following framework reform.

Such "vertical" reforms may be implemented at varying degrees of depth and breadth. The appropriate level will depend on the resources available to support reform (the more resources, the more depth is possible – and the more agencies can be covered) and on the need and capacities of the country itself; in general, the lower the country's capacities, the more work will be needed to ensure that the principles and processes detailed at the framework level are actually implemented at the local level and in all inspectorates. Reform project resources usually are not sufficient to cover training each and every individual inspector or to engage all inspecting agencies. It is therefore important to make sure that the government has a real commitment to reform and to use the demonstration effects from the inspectorates selected as pilots to promote reform.

Many of the most important tools of inspections reform – including developing risk-based inspections planning, providing business with better information about regulations, and implementing inspections checklists – can only really be implemented at the inspection-function level.[28] Yet once a basic framework reform is in place, these function-specific reforms are often the changes that create the greatest impact. Implementing them requires substantial work, however, and it is often difficult to ensure that these tools are used by all inspectorates. Since resources are limited, the most important inspectorates are likely to get most of the support to implement such reforms but developing manuals for risk-based planning, checklists, and other function-specific reforms can help spread those tools to other agencies. (See Box 13).

[27] Data from regulator submission to review questionnaire.

[28] Even when a unified inspectorate is created, most of this work is department-specific inside the unified agency.

BOX 13 In Jordan and in the Kyrgyz Republic, the IFC is Working on In-depth Reform Implementation with Selected Inspectorates

In Jordan, IFC rendered assistance to help the Ministry of Labor and the Ministry of Environment improve their inspections systems. We chose to work with these inspectorates because labor and environmental issues are very important for Jordan's exports (which must comply with certain labor rules to retain specific free-trade agreements with the United States) and for foreign investment (especially in the tourism industry) and because Jordanian businesses ranked these inspectorates among the most cumbersome or most difficult to deal with.[29] These labor and environmental inspections are also critical to public safety. The IFC has supported these inspectorates' work to:

- Develop risk-assessment tools.
- Develop checklists.
- Develop inspections manuals that contain good inspections practices, forms, checklists, and sample legislation.
- Train inspectors to use newly developed manuals.
- Conduct a functional analysis to identify all legislation and regulations related to the environment and to identify areas of overlap and duplication in those rules in order to amend the legislation accordingly.

In the Kyrgyz Republic, IFC is working with the tax, fire safety, and sanitary inspections agencies to protect public safety and streamline inspections. Tax inspections pose the greatest burden for Kyrgyz businesses. Despite the fact that an inspections moratorium was in place from April 25, 2008 to December 31, 2008, 71 percent of individual entrepreneurs and 65 percent of small and medium companies were subject to tax inspections between January 2008 and March 2009. Fire safety and sanitary inspections also represent an important burden for businesses: 33 percent of individual entrepreneurs and 25 percent of small and medium companies were inspected by the sanitary and epidemiological service between January 2008 and March 2009 and 24 percent of individual entrepreneurs and 31 percent of small and medium companies were inspected by the fire safety department during the same period, despite the eight-month inspections moratorium.[30] Sanitary and fire inspections are also among the most critical for public safety. The IFC is helping these inspectorates develop risk-based planning (for all three agencies) and checklists (for sanitary and fire safety inspections.)

Source: IFC Staff reports

[29] Interdisciplinary Research Consultants (2007). "Inspection Benchmark Survey of Jordanian Industries."

[30] IFC (2010). "Investment Climate in the Kyrgyz Republic as seen by SMEs."

Chapter 3. Reform Tools: a Closer Look

This section describes in more detail the tools that may be used to reform inspections. The final menu of reforms implemented in any country must be adapted to the specifics of that country (its problems, political and administrative system, budget for reform, the capacity of its government and inspectorates, etc.). Nevertheless, it is generally easier for reformers to begin by carefully assessing problems and priorities and by implementing a few simple reform tools (e.g., streamlining the inspections process, developing better information materials for businesses) and then move gradually toward implementing more complex reform tools (e.g., risk-based selection of the businesses inspected). The process may move more quickly, however, in higher-capacity countries or regions.

3.1 Framework Laws and Decrees – Clarify How and When an Inspection Can Take Place

International experience suggests that it is most convenient for businesses, and generally most effective, for inspections procedures to be governed by a single framework inspections law rather by many different laws and regulations. As a stopgap measure, however, inspections legislation may be improved in the short-term by decrees while a framework law is developed (and indeed in some countries where the power of the president is strong presidential decrees may be sufficient to reform inspections law and a new law may not be needed).[31]

It is essential for a framework inspections law to provide procedural guarantees to businesses, to strengthen their right to resist abuses of power and to appeal the conclusions of inspections, to require inspectorates to adopt risk-based planning and to use checklists during inspections, to decrease the discretion of inspectors in issuing sanctions, to require public reporting from inspectorates, and to ensure that all the rules and norms inspectorates enforce are available to the public.

[31] Some countries with relatively advanced economies, including Mexico and Latvia, have implemented broader reforms, adopting new laws that reform not just inspections but administrative procedures in general. Many of the provisions of the reform laws in Mexico and Latvia are similar to those in more specific inspections reform laws and both laws are quite far-reaching, if not always very detailed on some technical points. Nevertheless, in most countries a legislative reform that focuses on inspections will be a more practical approach, given how long and complex the process of developing a new general law on administrative procedures is likely to be.

It is also essential for the inspections legislation to allow as few exceptions as possible. Qualifying clauses such as "except if foreseen in other legal norms" can easily become a way for regulators to void the new legislation of any effect and make the law all but impossible for businesses – which are always unsure which other legal norms they would need to check – to use. Such loopholes can vitiate a framework inspections law. Changes in the inspections legislation also need be widely publicized through the media and by business associations, training events, etc. In many countries where new inspections laws have been adopted, the publicity surrounding their adoption and the subsequent debates about the role of inspections, the rights and responsibilities of businesses, the rights and responsibilities of inspectors, and other issues have played an important role in supporting the implementation of the law.

The following sections list some best practices for reform based on the experience of countries that have adopted inspections laws in the past five to ten years.

3.1.1 "Everything That Looks Like an Inspection is Indeed an Inspection"

Framework laws and decrees regulating inspections must apply to everything that is *de facto* an inspection, even when it is called something else (a "check," "review," "examination," "investigation," etc.). Experience has shown that if the law defines "inspections" too narrowly or specifically, regulators may use that definition to claim that their activities fall outside the law.

In Russia, for instance, the original post-Soviet inspections reform law adopted in 2001[32] specifically listed several types of inspections to which it applied but did not make clear that any type of visit by regulators to a business would be understood as an inspection and thus covered by the law. As a result, inspectorates called their visits by other names (e.g., "monitoring," "checks") and widely disregarded the law.[33]

Examples of good practices in inspections reform include the reform laws in Ukraine, Uzbekistan, and Tajikistan. In all of these laws, the definition of inspections includes all visits by an official from an inspectorate, whatever that visit may be called (See Box 14).

3.1.2 No Inspection Without an Order and an ID

Reform legislation should require any inspector conducting a review to produce an ID and an order from the chief of the inspection agency (or at least from the inspector's supervisor or regional chief) that specifically indicates the name and address of the business to be inspected as well as the name(s) and ID numbers of the inspector or inspectors, the topic

[32] This 2001 law was replaced by a revised law in 2009, which was itself further amended in 2010. Yet the effectiveness of the Russian legislation on inspections remains in doubt, in part because of implementation issues but also because of the way the law itself is drafted. See, for instance, a short comment at http://www.russianlawonline.com/content/law-good-intentions

[33] Ukraine's 2005 Permits Law suffered from a similar problem: because its definition of "permits" was too narrow, many regulators simply ignored its provisions, claiming to be issuing only "expertises" or some other advisory document.

BOX 14 Definition of "Inspections" from Ukraine's Law "On State Control over Business Activity"

Ukraine's law goes to great length to define its scope as broadly as possible so that no regulatory agency can try to evade its provisions under the pretense that its activities are not "inspections." As a result, the law even shies away from using the word "inspection" in defining its scope, referring instead to a "procedure of state surveillance." This is how the law itself defines the procedures it covers:

"Procedure of state surveillance: planned and *ad-hoc* procedures performed by means of inspections, revisions, reviews, examination and other procedures."

Source: Ukraine's law on the Main Principles of State Surveillance over Business.

of the inspection, and the date when it will take place and to leave a copy of the inspection order with the inspected business. Failure to produce these documents should give businesses the right to refuse entry to inspectors with no adverse legal consequences. The legislation should also list the information that must be contained in an inspections order.

Making inspectors present identification and orders can be a powerful deterrent to abusive and excessive inspections. In Mexico, for example, the reform law requiring mandatory presentation of ID by inspectors has played an important role in eradicating the "pirate inspectors"[34] who previously plagued businesses. Tajikistan's 2006 inspections law requiring inspectors to present an inspection order and ID contributed to a sharp decrease in the number of inspections: the average Tajik private firm was inspected just twice in 2007, compared to 10 times in 2002, while small and medium companies went through an average of five inspections in 2007, less than half the number they endured in 2005.[35]

Many countries now also require each inspection to be recorded in a logbook maintained by each business. This reform is intended to help keep track of the overall number and duration of inspections, to allow inspectors to see the results of previous inspections, and to enable inspections agencies to monitor inspectors' work more effectively. Logbooks may not be adequate tools for higher-capacity countries, where IT tools are more likely to be used to track inspections, but they can be a useful instrument in other places.

A number of countries (e.g., Armenia and Kenya for tax inspections, Ukraine and Tajikistan for all inspections but with some exceptions for emergencies) have also experimented with requiring inspecting agencies to send businesses notice of their upcoming visit several days in advance. The wisdom of this approach is widely disputed, as it in some ways contradicts accepted good practice concerning the safety and effectiveness of inspections (and it contradicts international norms such as International Labor Organization conventions that

[34] Fake inspectors who were not, in fact, affiliated with any inspectorates but preyed on businesses.

[35] IFC (2009). "Business Environment in Tajikistan as seen by Small and Medium Enterprises."

require labor inspectors to be given entry to enterprises at any time and European Union food safety regulations that emphasize the same kind of access for food safety inspectors). However, advance notice rules have been shown to produce some positive effects: Kenyan businesses, for example, report much higher levels of satisfaction with the work of the tax inspectorate now that they able to prepare the documentation they need in advance of an inspection.

Key arguments against the use of advance notification emphasize the difficulty of catching the most serious offenders and the possibility of businesses faking compliance with the rules (e.g., by borrowing fire extinguishers from each other or renting fire extinguishers for one day to make it look as if they comply with fire safety codes). Notification of tax inspections well in advance could even give businesses the chance to prepare fake accounting documents. Yet there are important counter-argument to such objections, including the fact that not all compliance can be faked: the existence of emergency exits and general compliance with building regulations cannot be temporarily fixed and accounting documents can generally be checked by cross-verification with suppliers and clients. Advance notification can also be an effective way to incite businesses to put their house in order and thus to improve compliance with the rules – and this should be the very goal of the inspections system.

It is clear that, especially in countries where inspections are particularly numerous and burdensome and corruption is widespread, advance notification can be one of the tools that helps protect businesses' rights. Yet given the controversy that surrounds advance notification, we cannot recommend promoting it across the board. Reformers should emphasize instead that it is good practice for inspectorates to advertise their inspections priorities for a given year, a practice that could prompt the worst-offending sectors to improve their practices. If reformers in specific countries decide to push for advance notification rules, project advisers should advise them on how to make that approach work and explain that they will need to include appropriate exceptions for cases of declared emergencies, epidemics, etc. in notification rules (and, of course, that criminal investigations are automatically exempted from inspections rules).

3.1.3 How Often Can One Inspect?

In countries where the frequency of inspections is very high and corruption and harassment are widespread, it can be useful for the framework legislation to limit the maximum frequency of inspections in ways that would not normally be considered good practice in higher-capacity countries. One effective way to design such an inspections cap is to create an overall limit for each type of inspection for a given business[36] but allow more frequent inspections for high-risk businesses – provided that inspectorates develop sound, risk-based criteria to identify high-risk businesses.

[36] Some countries have experimented with different approaches. Poland introduced a cap in the total duration of all inspections for SMEs in 2004 (see below), a policy that also puts de facto a cap on their frequency.

There are two main difficulties with such an approach: the development of risk-based criteria and categories may take a long time or be done inadequately (e.g., by simply declaring all businesses, or the vast majority, to be "high-risk") and the absence of any universal rule as to what the frequency cap should be.

On the first point, the reform legislation should set a deadline for adopting risk-based criteria and make the frequency cap enter into force only after those criteria have been established (six months to one year would be an appropriate period of time). The law should also require these risk criteria to be approved by a higher authority than the regulator itself (e.g., the Cabinet).

On the second point, the frequency cap can be based on international averages and best practices (it is unusual for good-practice inspectorates to inspect more than 5 percent of businesses each year, and this suggests a mean frequency of about one inspection every 20 years) and of political realities (what limits appear to be acceptable to stakeholders). A maximum of one inspection every five years can be taken as an acceptable rule of thumb.

It is also important to allow exceptions to frequency caps to address urgent or high-risk situations. In officially declared emergencies or epidemics (and "officially declared" is important to prevent each and every inspector from declaring his or her own "emergency"), the frequency cap should not apply of course. Exceptions to the cap might also be allowed in cases in which the head of the inspectorate decides that extra inspections are required. Formally allowing such exceptions is not the best practice, however, because in some countries inspection chiefs might well be very forthcoming about granting exemptions from the cap and such decisions would be taken frequently.

Reform laws in several countries demonstrate how frequency caps can be combined with other requirements to introduce a risk-based approach to inspection. As a result of excessively high inspections coverage in Ukraine, for instance, (95 percent of SMEs were inspected in 2006 and each SME was inspected an average of six times[37]), Ukraine's law now stipulates that businesses with a low level of risk should not be inspected more than once in five years and that, if an inspectorate fails to get risk categories developed, and approved by the Cabinet by the deadline the law provides, that agency must automatically treat all businesses as low-risk. In Belarus, planned inspections for high-risk businesses may be held no more than once a year (or once every two years if the previous inspections did not identify any violation). Planned inspections for medium-risk businesses may be conducted once every three years (or once every five years if the previous inspection did not identify any violation). The maximum inspection frequency for low-risk businesses is once every five years.

[37] IFC (2007). "Business Environment in Ukraine."

3.1.4 How Long Can the Inspector Stay?

In many countries where inspections are in dire need of reform, the average duration of inspections is, in an apparent paradox, too short rather than too long. The reason for such short visits is that inspectors are looking for "illicit income maximization" (i.e., to visit as many businesses as possible in search of unofficial payments), not trying to conduct thorough inspections. In Tajikistan, for example, 23 percent of individual entrepreneurs were inspected for less than 15 minutes in 2005.[38]

At the same time, the total duration of inspections over the course of each year can represent a heavy burden for businesses. In 2008 in Ukraine, for example, the average duration of all inspections performed at any one enterprise was 14 working days (or about three work weeks per year).[39] Some corrupt inspectors may also unreasonably extend the duration of an inspection to push businesses to make unofficial payments.

It is therefore useful for framework legislation to include limits on both the duration of an individual inspection and, if possible, the total annual duration of all inspections. The maximum duration of inspections should be based on the size and risk level of the business and the rules should accommodate the longer time needed for tax inspections than for technical and safety reviews (if tax inspections are covered by the legislation).

Reform laws in different countries have adopted different caps on the duration of inspections. In Poland, for example, SMEs can be inspected for a maximum of four weeks a year, in total, except in criminal cases. In Ukraine, planned inspections may not exceed 15 working days for large businesses and five working days for SMEs, and unplanned inspections may not exceed 10 working days for large businesses and two working days for SMEs (for each inspection). In Tajikistan, the maximum duration of inspections is differentiated by the type of inspections: financial audits should be less than 20 calendar days for corporations and less than 10 days for individual entrepreneurs. All other inspections of individual entrepreneurs and firms should last fewer than five business days.

There is no universal rule about what the duration of the caps should be, and these limits are bound to differ based on the level of development of the country in question. In general, more advanced economies, with larger and more complex firms and objects to inspect, will conduct some inspections that last significantly longer than those in poorer countries, where most firms are very small. As a rule of thumb, however, a technical or safety inspection of a small firm should last no more than one or two days.

[38] IFC (2006). "Business Environment in Tajikistan as seen by Small and Medium Enterprises."

[39] IFC (2009). "Investment Climate in Ukraine as Seen by Private Businesses."

3.1.5 What about "Unplanned Inspections"?

In some of the countries of the former Soviet Union, inspectorates have been evading attempts at reform (and at limiting over-inspection) by using so-called "unplanned inspections." Although this semantic distinction ("planned" inspections are the ones included in the inspectorates' yearly plan, "unplanned" ones are decided upon during the year on the basis of changing situations) can be understandable, it should be noted that more advanced inspectorates generally do not use it.

A well-functioning inspections system should base all its planning on risk analysis and update this planning constantly as conditions evolve. Since in many countries this goal is quite remote, however, it remains important to review the issues involved in "planned" vs. "unplanned" inspections. Based on the countries we have reviewed, we believe this distinction exists mostly in countries of the former Soviet Union. These countries have faced particularly acute inspections problems, but they also have been trying to tackle these problems for more than 10 years now – and the planned/unplanned distinction appears to be a response to earlier attempts at reform.

In many of these countries as gradual restrictions were imposed on the use and frequency of "planned" inspections, regulators have multiplied the use of "unplanned" ones. Since it is fair to expect that regulators in other countries would respond to such restrictions in similar ways, it is important for reformers to tackle this issue right from the start. Thus limitations on the frequency of planned inspections should be accompanied by the restrictions limiting the right to conduct unplanned inspections to clearly defined cases of emergency (e.g., cases of immediate danger to the life and health of citizens or the environment). The power to authorize unplanned inspections should be limited to the top management of the inspectorates.[40]

In addition to allowing unplanned inspections in case of emergency (which has to be carefully defined to prevent abuse), the framework legislation of course must also provide for control inspections – repeat inspections of businesses where serious violations have been identified – to verify that those violations have been addressed.

3.1.6 Require Inspectorates to Adopt Risk-based Planning and to Develop Checklists

As we have outlined above, to make the inspections process significantly more effective and more business-friendly, reform legislation needs to (a) require inspectorates to target and plan inspections based on risk analysis and (b) mandate the use of checklists by all technical

[40] It is generally good practice to restrict unplanned inspections to cases of official emergencies declared by competent authorities in ways the law mandates. Some countries also allow unplanned inspections that are based on a court order, and this is also a reasonable practice.

and safety inspectorates. Basing the frequency of inspections on risk levels helps ensure that the resources of the inspectorate are used efficiently and that low-risk businesses are less burdened by the process. Using checklists helps make compliance easier even as it also makes inspections more transparent and consistent. Checklists and risk-based planning are therefore the two primary tools of inspections reform.

This fact makes it particularly important for inspections legislation to establish a definition of risk that combines the likelihood and the scope of potential damage and to impose a deadline by which inspectorates must develop risk categories and checklists. The legislation also needs to establish the principle of public and free access to checklists[41] (perhaps by requiring inspectorates to post them on their Web site). Good examples of such reforms include the 2006 Tajik inspections law and the 2007 Ukrainian inspections law (See Box 15), both of which mandated that all inspectorates use risk principles to plan inspections and develop checklists for inspectors to use to check business compliance with rules and norms.

BOX 15 Extracts from the Sections of the 2007 Ukrainian Inspections Law Related to Risk-based Inspections and Checklists

- **Definition of risk:** "A quantitative measure of danger which envisages probability of negative consequences of business operations and possible amount of losses."
- **Deadline to develop risk categories and checklists:** "During six months upon publication of the law, the Cabinet of Ministers of Ukraine is obliged to approve the criteria for differentiating business entities according to the level of risk of their activities for the human lives and health, environment and determine the periodicity of performance of the state surveillance (control) procedures"; "if the criteria for evaluating the risk level of business entity activity, periodicity of performance of the state surveillance (control) procedures and list of issues for their performance are not approved within the term envisaged by this Law, the business entities are considered business entities with low level of risk and are subject to the state surveillance (control) not more often than once in five years."
- **Development and public availability of checklists:** "Depending on the level of risk, lists of issues for the regular procedures are determined by the state surveillance (control) agency and to be approved by its order. Depending on the objectives of the procedure every state surveillance (control) agency shall determine the issues which will make the basis of the state surveillance (control). Unified act forms containing the list of issues depending on the level of risk are approved by the state surveillance (control) agency and placed in the Internet as per the procedure established by law."

Source: Ukraine's Law on the Main Principles of State Surveillance over Business.

[41] Whether agencies should publicize their risk criteria is a more disputed issue. Although it is generally believed that making those criteria public would make high-risk businesses more likely to comply with the rules (because they know they will be inspected more often), some authorities (particularly in the tax area) contend that it would let low-risk businesses relax too much. Most countries and agencies do make their risk criteria for technical and safety inspections public, however, and this can be accepted as good practice.

3.1.7 Establish Clear Rules on Taking and Testing Samples

In many countries, inspectors' unregulated power to take samples at will, and at entrepreneurs' expense, is a real nuisance for businesses, as is the fact that inspectorates often tests these samples in ways that yield untrustworthy results and open the door to more unofficial payments. Such nuisances can become a major problem in more developed economies, where the value of goods sampled is higher, and in industries that use high-cost inputs (e.g., jewelers). As a result, it is very useful to include provisions on sample-taking in the inspections legislation.

Those rules should establish the following principles:

- As a rule, the cost of samples should be covered by the inspectorates (at market prices) along with the cost of testing. Only in cases in which violations are found should businesses be required to pay those costs.
- The taking and storage of samples should be strictly regulated and fully transparent. Control samples should also be taken and businesses should be able to appeal the test results and get a second opinion. The law should also clearly define which laboratories are authorized to test what substances.

Although these may sound like rather technical points, they can create fierce opposition among inspectorates, as the abuse of sample-taking is a common practice. Forcing inspectorates to pay for these samples is a sure way to curb such abuse.

3.1.8 Strengthen the Rights of the Inspected

Strengthening the rights of those inspected to resist abuses of power is one of the central goals of inspections reform. Inspections legislation must enable businesses to shut their doors, without being obliged to appeal to a higher authority, if inspectors do not present inspection orders and ID, check compliance with issues that are not part of checklists, refuse to fill inspection logbooks when doing so is required, or violate the rules in other ways. Indeed, businesses now have that right in many countries that have recently adopted framework laws or decrees on inspections (e.g., Ukraine, Tajikistan, Belarus, Kazakhstan, etc.). The Ukrainian law on inspections, for example, clearly stipulates that businesses have the right not to allow inspectors to conduct inspections if they fail to respect the rules on the frequency of inspection or to provide businesspeople with copies of inspection orders or if their inspection orders do not meet legal requirements.

Limiting the arbitrary power of inspectors to issue sanctions is also a critical concern for reformers. Framework legislation should forbid inspectors from issuing any sanctions on the spot, except in cases of immediate danger to the life and health of citizens or the environment (and such exceptions must be precisely defined by the legislation). Inspectors should instead be required to prepare a report detailing their findings, to give a copy of that report

to a representative of the business inspected, and to forward that report to their supervisor or manager. That supervisor should have the exclusive power to issue sanctions. Both the Tajik and Ukrainian inspections laws, for example, stipulate that the supervisor or line manager of inspectorates must determine the amount of any fines required, based on written reports from inspectors (See Box 16).

BOX 16 Extract from Article 7 of the Ukrainian Inspections law Related to Violations and Sanctions

6. (…) Official of the state surveillance (control) agency specifies in the Act the status of fulfillment of law requirements, and in case of non-fulfillment thereof- a detailed description of identified violations with reference to the respective requirement of law…
7. Based on the Act, a writ, instruction or other order document on the elimination of identified violations is prepared within 5 working days upon completion of the procedure.
8. A writ is a written requirement of an official of the state surveillance (control) agency which is mandatory for fulfillment by business entity regarding the elimination of violations of law. A writ does not envisage imposing sanctions on a business entity. The writ is issued and signed by an official of the state surveillance (control) agency which performed the inspection.
9. An instruction or other order document of the state surveillance (control) agency is a written resolution on the elimination of identified violations within the established deadline which is mandatory for fulfillment. The instruction is issued and signed by the head or deputy head of the state surveillance (control) agency. The instruction may envisage certain sanctions to be imposed on business entities as envisaged by law.

Source: Ukraine's Law on the Main Principles of State Surveillance over Business.

The law should also encourage inspectorates always to issue warnings first, and to impose sanctions only if a repeat inspection shows that the violation has not been corrected, except in cases of major violations or in which violations pose risks to life. The inspections law of Bosnia and Herzegovina appropriately reflects such an emphasis on using the possibility of sanctions to encourage compliance rather than issuing fines immediately. It holds that: "if the subject of the inspection fails to execute the administrative measure comprised of non-financial obligation and if that measure cannot be executed through a third party but only by the subject of the inspection personally, the inspector shall institute a fine in order to force the execution of the administrative measure and at the same time prescribe a new deadline for execution with a threat of a new higher fine."

It is also important that the law ensures that sanctions are commensurate with offenses. Ukraine's inspections law, for instance, upholds this principle when it stipulates that, "if fines for violations of law are applied… the principle of proportionality of violation and punishment is taken into consideration."

The value of any fines imposed must be sufficiently high to deter would-be violators. Therefore the value of the sanction set out in the regulations must exceed the commercial value of the regulatory breach itself. In other words, regulations should make it cheaper for businesses to comply with the rules than to pay a fine. The appropriateness of sanctions (neither too high nor too low) is a vexing issue for inspections reformers, in part because reforming administrative or penal sanctions is a complicated exercise that involves legislation that goes far beyond inspections and is often politically and legally difficult. As a result, sanctions tend to be an issue where reform lags, except in cases in which sanctions reform can be connected to an overall drive to reform a nation's administrative penalties.

3.1.9 Establish Accessible and Reliable Appeal Procedures

Inspections reform legislation must also establish accessible and reliable appeal procedures if such procedures are not already in force in the country in question. It is particularly important that the legislation (a) requires inspectors to inform businesses about their right to appeal the results of the inspection during the inspection itself, (b) defines a period in which businesses can appeal inspection results, (c) allows appeals to be filed with an authority separate from the inspections and adjudication unit of the inspectorate itself, and (d) establishes a deadline for decisions on appeals filled by businesses. Those businesses should also retain the option of appealing their case to the courts.

Tajikistan's law sustains such principles by requiring inspectorates to include information about the appeal process in the inspections report. Inspections legislation in both Ukraine and Bosnia and Herzegovina also includes good practices on appeal procedures. The law of the Federation of Bosnia and Herzegovina on appeals related to the inspections act stipulates that "the appeal is made immediately upon reception and reading of the minutes, and within three days from the reception of the minutes at the latest." Bosnia's law also gives authorities a deadline of 15 days from the day they receive an appeal to issue a decision.

Article 21 of Ukraine's reform legislation stipulates that "Business entities are entitled to appeal to the central executive power authority or to the court against the resolutions of the state surveillance (control) agencies. The respective central executive power authority is obliged to consider the appeal of the business entity as it is envisaged by law." This law also gives businesses the opportunity to appeal both the inspections report and the results of any testing done as a result of the inspection.

3.1.10 Ensure Sanctions are Commensurate and Set in a Transparent Way

Since introducing sanctions for inspectors who violate the law is another powerful tool to reduce the discretionary power of inspectors, it is important that the inspections legislation also defines the sanctions to be imposed on inspectors when they violate the law. The law of the Federation of Bosnia and Herzegovina is an example of good practices on this question, as it clearly defines the grounds for relieving and suspending inspectors from their duties (See Box 17).

BOX 17 Extract from the Inspections Law of the Federation of Bosnia and Herzegovina

[An] Inspector shall be suspended from his duty:

- if he fails to perform an inspection or undertake other administrative measures when it is obvious that they must be performed, and especially if this failure results in substantial harmful consequences;
- if he oversteps or misuses his authority when performing inspections;
- if he fails to perform his executive decision to undertake particular administrative measures within the prescribed period of time;
- if he causes substantial material damage to the subject of the control or other party by illegal or immediate activity during the performance of an inspection;
- if he fails to inform another inspector about illegal activities by the subject of the control that he becomes aware of during an inspection;
- if, while performing the duties of an inspector, he commits a criminal offense that is an obstacle to the work of the civil service;
- if he fails to return business documentation temporarily taken from the subject of the control within the time period prescribed by law;
- if he violates his obligation to protect business secrets and other secrets he may become aware of during an inspection.

Source: Law of the Federation of Bosnia and Herzegovina "On Inspections in the Federation of Bosnia and Herzegovina."

It is often difficult to make such rules part of part of inspections reform, especially in countries where all administrative sanctions are gathered in one legal code that is beyond the scope of inspections reform. Yet defining the penalties for inspectors' misconduct is a very important point, and one which can give real sting to reform. It is also a good practice for inspectors who have committed serious violations to be fired and barred from any public service or civil service employment for a number of years.

3.1.11 Require Public Reporting From Inspectorates

To increase the transparency of inspectorates' activity and their accountability for their results, it is important that inspectorates be required by law to submit annual reports detailing their activities. Reform legislation should establish an annual deadline for these reports, define the information they should include, and require inspections agencies to make those reports available on the Internet.

The Tajik inspections law, for instance, stipulates that each inspection body must publish an annual report that includes a short summary of its inspections, findings, plans, and priorities for the next year. The Ukrainian inspections law requires inspectorates to publish annual reports (by April 1 of the following year) and to make these reports available on the

BOX 18 Information and Transparency in Bosnia and Herzegovina

The inspectorate of the Republika Srpska holds regular monthly media conferences and has invested into a modern Web site. The inspectorate of the Federation of Bosnia and Herzegovina has promoted transparency and accountability by such strategies as publishing full-page newspaper ads to inform the public about an upcoming inspection campaign in the labor sector.

The two general inspectorates have also adopted official guiding principles for their site inspections that are based on the following principles:

- Transparency
- Efficiency and effectiveness
- Responsibility
- Proportionality
- The introduction of good practices
- Consistency
- Fairness
- Creativity (avoiding routine sanctions)
- Flexibility (not every violation – has to be sanctioned, but firm repression when violations are intentional and dangerous)
- Non-discrimination.

Source: IFC Internal briefing paper.

Internet. The Federation of Bosnia and Herzegovina makes it mandatory for chief inspectors to submit monthly reports to the ministry relevant to their activity. In many OECD countries, inspectorates have to report annually to the parliament, and this is a very good practice as it creates independent oversight of their work.

3.1.12 Ensure all Rules and Requirements are Public

Finally, it is of paramount importance that the framework legislation ensures that all requirements, rules, and norms are made public and are freely and easily available. This publicity condition is a critical part of shifting inspectorates' away from focusing on detecting violations and levying fines and toward educating businesses and promoting compliance with the rules. The law should even spell out how the regulations must be made public – requiring, for instance, that regulations be available on the Web site of relevant inspectorates, that copies must be distributed in inspectorates' offices, that inspectorates must provide written answers to questions about regulations free of charge upon request by businesses, etc.

In Tajikistan, for instance, the reform law stipulates that inspections bodies must make legal regulations accessible to the public. Ukraine's law stipulates that inspectorates must provide written consultation regarding both regulatory requirements and inspections procedures upon request from business entities.

3.2 Institutional Changes and Mergers – Potential and Pitfalls

The institutional changes nations use to address dysfunctions such as overlapping inspections and a lack of coordination between inspectorates are numerous, ranging from minor revisions of the responsibilities and competencies of various agencies to creating a unified inspectorate that gathers most or all inspections functions under one agency. The choice of the right institutional tools for any country must be based on that country's specific situation (institutional legacy, size, political and financial support for reform, etc.).

Many countries have established some sort of coordination council of inspectorates, most often to steer the reform and share good practices (e.g., Latvia, the Netherlands) but in some cases (e.g., Uzbekistan) as an institution that actually supervises and controls the planning and implementation of inspections. These councils have often proved to be a useful tool. Since they are primarily a way to initiate and maintain the impetus for reform rather than a feature of a reformed inspections system, and because research on the different experiences of inspections coordination councils is not yet sufficiently consolidated, we will not detail them further in this section but focus instead on the institutional changes that should be the results of the reform process.

3.2.1 Function-specific Consolidation

Consolidating inspections functions for related topics (e.g. veterinary inspections and sanitary inspections, both of which contribute to food safety) is an effective way to address the duplication of inspections. In addition to enhancing efficiency and decreasing the burden inspections impose on businesses (because they will get a single inspection rather than two, or more, on the same issue), consolidating inspections functions may allow governments to realize significant savings, and those savings can be an important trigger for reform in the context of the general public finance crisis. The consolidation of inspections functions is most frequent in the food safety field (See Box 19).

Reformers must keep in mind, however that, as in the case of any merger, the risks of bungled implementation of such consolidations, the potential costs (political but also financial), and the opposition that the merger will prompt are all quite significant. Thus mergers are a powerful reform tool but not a risk-free one. Although there are many examples of good practice (especially in setting-up unified food safety agencies), it is also important that the design of the merged agency must always be based on the local situation. In designing the new agency, the primary question should be which of the agencies involved seems to have the most capacity and the best-qualified staff, and therefore should become the backbone of the merged inspectorate. The answer will vary widely from country to country.

BOX 19 Creation of the Canadian Food Inspections Agency in 1997

In Canada, food inspection activities were consolidated in the Canadian Food Inspections Agency (CFIA) in 1997 upon the initiative of the Auditor General of Canada. The main objectives in creating this agency were (a) to improve the efficiency and effectiveness of food inspection and quarantine activities by applying an alternative service delivery approach and (b) to realize financial savings by eliminating the duplication of functions among existing inspectorates. Before the creation of the CFIA, food safety along with plant and animal health were under the supervision of five separate departments (Agriculture and Agri-food Canada, Health Canada, the Department of Fisheries and Oceans, Industry Canada, and Revenue Canada-Customs).

The Canadian Food Inspection Act stipulated that the CFIA would be responsible for enforcing all statutes related to food inspections (10 laws in total). CFIA now oversees, among other matters, food safety, trade and consumer education, quarantine services, and the regulation of seeds, animal feed, and fertilizers. The president of the agency reports directly to the Ministry of Agriculture and is responsible for CFIA's management, while the Minister of Health is responsible for assessing the agency's effectiveness in guaranteeing food safety.

It is difficult to assess whether CFIA's performance has fulfilled the agency's initial objectives (improved efficiency of inspections and fiscal savings) because the food safety context has changed rapidly, resulting in an expansion of CFIA's mandate and budget. However, there is a growing consensus worldwide that food safety needs to be dealt with by a single inspectorate.

Source: Jacobs and Associates (2005). "Case studies of reform of government inspections: Canada."

3.2.2 Closing the Smallest or Least Relevant Agencies

Closing the smallest or least relevant agencies can also be a good way to streamline an inspections system. The United Kingdom's Hampton Review indeed suggested that small inspectorates are the least cost-effective. The inspections functions conducted by the small agencies whose operations are shut down may either be canceled or transferred to other agencies with related inspections functions (e.g., instead of maintaining many small, industry-specific or hazard-specific agencies, all agencies inspecting issues related to labor safety can be merged with the labor inspectorate). Latvia, Slovenia, and the Netherlands are good examples of this kind of consolidation, as they each have about 15 national inspectorates while most countries maintain 30 to 40.

Although there is no "one-size-fits-all" approach, and consolidating agencies can create its own problems (e.g., loss of expertise, conflicting cultures, the cost of mergers, etc.), there is general agreement that creating a limited number of agencies with broader approaches to key safety and health issues is a sound approach (and much the same is true for revenue agencies, where the trend has been to consolidate tax and customs functions in one agency so that data can be more effectively shared). At the same time, it is vital to avoid consolidating functions in ways that create a conflict of interest. Such conflicts can take several forms:

- Merging agencies that inspect safety with agencies that have an interest in increasing the number of operators, as happened when the United States created the Minerals Management Service, an agency that has recently been split again as a result of the oil spill disaster in the Gulf of Mexico.[42]
- Merging agencies that inspect compliance with safety norms and other standards, with agencies that issue certificates of compliance for a fee. This can create situations in which the merged agency (a) coerces businesses to buy its services rather than those of other certification providers and (b) does not report cases where certificates have been unduly issued (corruption cases for instance).[43]

Since mergers do carry risks, it is important for inspections reforms projects to study carefully the agencies that could merge and the problems the merger could involve and to advise the client governments against rushed decisions that can create results more problematic than the baseline situation.

3.2.3 Delegating Functions, Sharing Information

Some countries allow certain inspectorates to delegate functions to other inspectorates, conduct inspections on behalf of other agencies or share information in an effort to minimize the need for additional inspections. Such cooperation between inspectorates usually only works well, however, in relatively advanced or, at least, well-governed countries, as its success depends on (a) effective discipline inside the state apparatus and the willingness of agencies to cooperate (something that is, in many countries, even more difficult to achieve than "simply" shutting down or merging some agencies) and (b) the existence of an information system that is accessible to several inspectorates – a form of cooperation that requires that inspectorates not only be computerized but also (at least to some extent) networked.

In Bogota, Colombia, for example, the municipal fire, sanitary, environment, and police inspectorates collaborate closely. These inspectorates have developed a unified checklist that allows each inspectorate to record issues it spots that lie outside its own scope of work so that other inspectorates may, if necessary, schedule an inspection. The information system common to these four agencies allows for an easy exchange of information. On a broader level, in the European Union, all agencies involved in market surveillance have access to the "Rapex" information-sharing system[44] and can report problems through that system. The latest trend in the Netherlands is to build on that practice by defining a certain agency as the

[42] The MMS, created in 1982 in a merger of several agencies, was tasked with (a) issuing licenses for drilling (the more licenses, the more income for its budget, hence issuing more licenses became the agency's main goal) and (b) safeguarding safety and the environment. It is widely believed that this conflict of interest has caused safety and the environmental protection to take a back seat to revenue-maximization at MMS. See for instance the *New York Times* article "Minerals Service Had a Mandate to Produce Results," http://www.nytimes.com/2010/08/08/us/08mms.html?emc=eta1

[43] A case in point is the State Committee for Standardization and Consumer Protection in Ukraine. See, for instance, the IFC report, "Technical Regulations in Ukraine, 2008."

[44] http://ec.europa.eu/consumers/safety/rapex/index_en.htm

"lead" inspectorate for a given industry (e.g., the Mining Inspectorate for offshore platforms) and making this agency conduct inspections and report to others on any potential problems it identifies in their respective spheres of authority. Only if problems have been spotted by this lead inspectorate will other agencies conduct their own inspection.[45]

3.2.4 Joint Inspections

In countries where the number of inspectorates is high or where there are overlapping jurisdictions in a given field, conducting joint inspections on related topics (e.g., fire safety and architectural inspectors jointly examining building safety.) can also be an effective way to reduce the inspections burden for businesses by decreasing the time they spend on separate (and redundant) inspections. In some countries, inspectorates also conduct joint inspections on issues that are not directly related.[46]

In Bogota, Colombia the municipal fire, sanitary, environment, and police inspectorates conduct a joint, multi-purpose inspection when the businesses targeted are considered high-risk for all inspectorates concerned. This joint inspection is planned automatically through common information and planning software. If the target business is considered high-risk only for one of these inspectorates, only that inspectorate will inspect. In Jordan, several agencies with responsibilities linked to food safety also inspect businesses jointly.

3.2.5 Creating a "Single Inspectorate"

A radical way to address the duplication or overlap of inspections functions and the lack of information-sharing among inspectorates is to create one unified inspectorate that oversees all or most[47] inspections. Such an agency usually includes just a handful of separate departments, each of which handles one of the main inspection functions (See Box 20).

Creating a unified inspectorate is a complex and time-consuming initiative and there is no guarantee that it will succeed in meeting its initial objectives (eliminating overlapping inspections, decreasing the burden of inspections for businesses, cutting the cost of inspections for the state, etc.) Indeed, if the roles and missions of the inspectorate's different departments are not properly defined, internal overlaps in jurisdiction can remain a problem. Another concern is that reform may stop with the creation of this single agency; this change would result in only very minor improvements over the status quo in cases where the targeting,

[45] This is generally an excellent practice but it requires not only a high level of coordination but also, obviously, well-qualified staff in the lead inspectorate(s) who have extra training that enables them to spot issues in areas of expertise other than their own.

[46] In Uzbekistan, for example, the Coordination Council plans joint inspections that can gather tax, fire safety, health safety information, etc. in an effort to minimize the number of inspections businesses face.

[47] The existing examples of unified or single inspectorates have generally left the revenue agencies and the inspectorate that focuses on controlling other state agencies out of the unified inspectorate. In Mongolia, however, the inspections agency that oversees other state agencies was included in the single inspectorate, and this decision has created more confusion than positive results. So it would appear to be good practice to leave such oversight agencies out of unified inspectorates.

BOX 20 Unified Inspectorates were Created in Croatia and Bosnia Herzegovina

Croatia's Inspection Reform

In 1999, Croatia took the unusual step of consolidating many of its inspection processes into a single autonomous agency that now conducts most of the nation's inspections: the State Inspectorate. Once a department of the Ministry of Economy, the State Inspectorate is today responsible for 11 inspections functions and three technical inspections, including inspections previously conducted by the Ministries of Economy, Forestry and Agriculture, Tourism, and Work and Social Welfare. This system has not only reduced the number of visits a business is likely to endure but has saved considerable budgetary resources.

The number of units that conduct inspections has been reduced from 110 to 49, and the number of county offices cut from 22 to five.

Another important benefit of Croatia's single inspectorate is that it has prevented the kind of conflicts of interest that arise when the same ministry or agency issues licenses and conducts inspections in the same field (by taking most of the ministries and subordinate agencies that issue licenses out of the business of conducting inspections). This change has helped reduce the frequency of inspections and increase the professionalism of inspection supervision.

The larger goals of establishing this unified state inspectorate were to concentrate key inspections in one place, improve working conditions, raise the expertise level for supervision of inspections, improve cooperation and coordination among various inspections units, and eliminate the costs of performing several inspections of the same target. The greatest advantage of this arrangement is that it has reduced the number of inspections needed, benefitting both the state administration and the business community.

According to former Inspector General Branko Jordanic, the new agency immediately achieved greater efficiency and a 15 percent to 20 percent increase in inspection visits per inspector. He also contends that this reform helped Croatia rationalize inspections services and introduce risk-based inspections.

Sources: OECD, Stability Pact. "Investment Compact, Regulatory Governance in South East Europe. Progress and Challenges." July 2004. http://www.regulatoryreform.com/pdfs/FINAL-RGI%20Report-29-07-04.pdf and United Nations Economic Commission For Europe (UNECE), Committee For Trade, Industry And Enterprise, Development Market Surveillance Activities, August 5, 2005 Trade/Wp.6/2005/10.

Tarik Sahovic. IFC (2010). "Internal Briefing Paper."

frequency, transparency, and procedures for inspections all need to be reformed as well. Unifying inspections under one agency can make the implementation of such reforms easier, but it does not make them happen in and of itself.

The unification of inspectorates nonetheless remains an interesting tool because it creates the opportunity for an organizational "big bang" (that transforms procedures and rules, staffing, organizational culture, etc.), for significant savings (for one headquarters instead of 10) and for increased effectiveness as a result of sharing information and resources. It is a relatively difficult tool to use, however, and it should really only be considered if the idea comes from the client country rather than emerges as an external recommendation. As time passes, and the experience from the few countries that have tried this approach can be more thoroughly evaluated, this approach may (or may not) come to be seen as a primary instrument in good reform practice.

BOX 20 *(continued)*

Bosnia Herzegovina's Inspection Reforms

The Republika Srpska (RS) moved faster than the Federation BiH (FBiH) did to create a unified inspectorate but both entities moved quickly to consolidate most inspections functions within a general inspectorate. FBiH now has 15 inspectorates in total : ten of these agencies are part of its general inspectorate while five are part of other ministries. The RS also has 15 inspectorates, and 11 of them are part of its general inspectorate. The inspections functions that are not part of the general inspectorate cover fiscal inspections (on tax and financial issues) along with culture and administration inspections (which mostly apply to businesses) The original vision for reform called for making tax inspections part of the unified inspectorate as well, but this change proved to be too difficult to implement, both technically and politically. Local governments also conduct some inspections in addition to those performed by the unified inspectorate.

In both the RS and the Federation, the unified inspectorates have proved more effective, more efficient and more professional than the various inspections agencies that preceded them had been. Thus inspections reform in the BiH has managed to reduce the burden on business, and not just by introducing risk-based inspections. Since 2001, the WBG has been financing surveys of businesses in Bosnia and Herzegovina to document the burdens inspections impose. These surveys clearly show that the time businesses lose to inspections has fallen sharply since inspections reform began.

Number of days of inspection per year per business

	2001 pre-reform	**2004** reform starts	**2007** latest	**Target** WB Policy Credit
Federation of BiH	18	26	9.9	12
Rep. Srpska	28	34	7.5	15

Sources: Tarik Sahovic. "Case of Bosnia and Herzegovina – Brief for IFC Mongolia Inspections Reform Project," 2009 and Internal Briefing Paper, 2010.

3.2.6 More Institutional Issues: Public Service Rules, Pay and Compensation

Institutional reform work, and inspections reform work in general, are strongly affected by a country's overall public service and civil service frameworks and by pay and compensation practices.

In a number of countries, it is nearly impossible to sack public servants without a lengthy procedure. Although in some specific cases, reform legislation may allow the state to down-size inspectorates' staff and to get rid of some of the least professional staff, shutting down entire agencies (through mergers or other measures) will usually mean that their staff has to be redeployed and most such situations will allow only very limited staff reductions. This does not mean, however, that merging agencies and eliminating overlaps is impossible. In

many cases, the staff from merged or shut down agencies can be more useful if it is transferred to a new, more rational context – and indeed, it is often important to retain the best specialists from some agencies.

If, and only if, it is clear that inspectorates' staffing levels are too high in terms both of (a) efficiency (the ratio of inspectors to businesses, compared to that of countries with similar income, economic structure, etc.) and (b) available state resources, then a reduction in overall staffing can become an objective of inspections reform. The chances of achieving this goal will then depend on the strength of its political support and on the level of coordination of this reform with other public service reform and deficit reduction drives.

As we have previously noted, pay and compensation practices can both help enable good inspections reform (by rewarding good practices) and, on the contrary, help block reform (by linking compensation to bad practices). A good example of a bad practice is the way some countries (e.g., Tajikistan, Mali, Kenya, etc.) link the bonuses some inspectors receive to the level of fines levied against businesses. This practice clearly creates a strong incentive for inspectors to find faults and violations at any cost, and also to avoid informing businesses of the rules so that inspectors can find as many problems as possible.

To alter such counter-productive incentives, reform should not only decouple all bonuses from the level of fines or other sanctions imposed but require inspectorates to adopt positive performance indicators instead. Increased compliance levels and increased levels of information and awareness about the rules and regulations, not high levels of fines or sanctions, should be treated as signs of success.

3.3 Risk-based Inspections Planning – a Menu of Options

Although it is important and useful for reform legislation to establish the principle of risk-based planning of inspections, there is a long road from the principle to its implementation. There is also a wide range of different ways to do some kind of risk-based planning – from the most basic to the most advanced.

Learning to select business to inspect based on an analysis of risk is indeed one of the most complex tasks an inspectorate faces in the reform process, a task that is far more difficult and costly than "simply" improving inspections procedures. The experience of Tajikistan illustrates how slowly this process can move. Although the 2006 Tajik inspections law stipulates that enterprises should be selected for inspections after an assessment of the risk their economic activity poses to public safety, this provision of the legislation still has not really been implemented (although some inspectorates are working on it).

To help move the process forward, it is usually a good practice for reformers to work in-depth to help at least one inspectorate or, better yet, several inspectorates, set up and implement a risk-based planning system. The selection of the agency or agencies to use as a

pilot should be based on a combination of the agencies' importance for private businesses and the public and their readiness and capacity to implement changes. The goal of this pilot program is not just to move the agencies involved toward risk-based planning but to use that pilot as an example for other agencies to follow, even if they do so more slowly.

It is also worth noting that, in some countries, risk-based selection of businesses to be inspected has been complemented or replaced by random selection – a practice now used, for example, in custom inspections in Mexico and in inspections of low-risk business in in Bogota, Colombia. Random checks are relatively easy and inexpensive to implement, and they are an improvement over biased selection by inspectors, but risk-based targeting remains a better option.

Risk-based targeting and planning of inspections is such a broad concept that it can be used and understood in quite different ways. However, in general, "risk-based planning" can mean any form of inspections planning in which the businesses to be inspected are selected through some analysis of the risk they pose. In this context, risk is understood as a combination of the probability and the scope of the hazard a business activity may create.

Although the most advanced agencies conduct risk-based planning using computerized tools that assign a risk score to each individual business based on an analysis of its profile and history, there are also much simpler ways to do some level of risk-based planning using much simpler tools.

3.3.1 Defining Simple Criteria and Categories

Using risk categories is a relatively simple approach to risk-based planning that can be implemented even by relatively low-capacity countries and institutions. Instead of doing extensive data mining to define a risk score for each business, an inspectorate using this approach will try, with the help of external experts, to define key risk factors and then, based on the combination of these factors, to establish some basic risk categories (from low-risk to high-risk).

The initial steps an inspectorate needs to take to establish basic risk categories include:

- Defining the key risks it is mandated to address.
- Analyzing the main indicators for these risks.
- Identifying the main dimensions of risk that should be used to classify businesses.
- Assessing the availability of data on those issues within the inspectorate and other state agencies.

Based on this analysis, the inspectorate can then review the population of businesses under its supervision and rate the different sectors, locations, and sizes of business on both their probability of risk and the magnitude of the hazards they pose. In practical terms, this means selecting a limited number of criteria (e.g., what the business produces, the

technologies it uses, where is it located, its size, its history of compliance, etc.) and defining a set of ratings for each dimension of risk. If the required information is available, it should be possible to give each business a rough risk score on the basis of this simple system.

The inspectorate should also define a small number of categories (three at a minimum: high-risk, medium-risk, and low-risk) based on those risk scores and a recommended or mandatory frequency for inspections of businesses in each category.

To determine the appropriate frequency of inspections for each risk category, the inspectorate should first establish the standard inspection staff-time and resources required to examine a typical business in each category. It can then define an acceptable average inspection frequency that is consistent with its resources. International experience indicates that only business in the top risk category can be inspected about once a year (or more often in some high-risk areas such as food safety), while other businesses must be inspected significantly less often.

For a risk-based inspections system to yield optimal results, it is important that these risk categories be defined in a sound way. One good way to develop those categories is to assess risks by sector, and then by the type of businesses within that sector. Businesses working in the food production industry, for instance, can easily be identified as creating more serious risks for sanitation authorities to address than businesses in the clothes production industry. Within the food industry, businesses producing large quantities of food also clearly pose greater risks than businesses producing small quantities.

In countries where inspectorates have no computerized database of businesses or objects to be inspected (and this is often the case in less-developed economies), the next step is to help inspectorates develop a basic electronic database. This process involves defining what information should be included, how it should be organized, and how it can be gathered. In developing the database, it is important to strive not to create new reporting requirements (which create new administrative burdens) for businesses but to rely as much as possible on existing mechanisms (e.g., statistical reporting, licensing procedures, etc.) to gather the needed information. Only when some vital information is not being gathered at all in the baseline situation should a new reporting procedure be created.

While a database is being developed, inspectors may also implement risk-based selection of businesses manually as a stop-gap measure. In Latvia, for instance, before the introduction of a computerized system, local offices of the State Revenue Service conducted credibility checks of VAT receipts manually on the basis of defined risk-criteria. Similarly, once some sectors and categories of businesses have been defined as high-risk, local inspection offices can start prioritizing them for inspections based on paper records or on their knowledge of the local enterprise population.

3.3.2 What Kind of IT Tools?

Although an information database can be used for inspection planning in a very simple way (i.e., by using manual filters to select businesses from each category to inspect), it is clearly better to develop and implement a basic planning software that will automatically classify businesses into risk categories and randomly select businesses from each category. For such software to be able to plan inspections fully, however, it needs to have the capacity to handle information on the inspectorate's resources (inspectors and their time), and this problem creates an additional layer of complexity. In many countries, creating a database that can classify businesses, and having staff extract businesses from the database and plan inspections based on the prescribed inspection frequencies for businesses in each risk category, will be a more realistic option.

In lower-capacity countries, it is better for both the database of businesses and the planning software used to be low-tech so that the system is faster to set up, easy to use, and easy to maintain. This approach often means using slightly-tailored, off-the-shelf database software rather than custom-built programs, allowing data to be transferred through removable media rather than just on-line, and generally keeping the system as simple as possible. Low-tech systems are far cheaper than state-of-the-art computerized systems and can deliver considerable improvements in a short time. Instead of aiming for an overly sophisticated system at first, inspectorates should begin by developing low-tech databases and planning software and seek to refine those systems gradually over time.[48]

More cutting-edge computerized systems can integrate the entire inspections function – from the basic data on each business, through risk analysis and inspections planning, to reports, sanctions, feedback, and follow-up. These systems are complex and costly to set up and maintain and require more highly-qualified staff, and therefore should be used only in countries where the infrastructure is well-developed, inspectorates' staff capacities are high, and governments are able and willing to invest in expensive systems.

Such state-of-the-art systems not only plan and assign inspections automatically but allow inspectors to enter the results of inspections and update the risk profile of businesses easily. They can even be made accessible to businesses that want to check their own risk profile and history.

In Bogota, for instance, IFC successfully contracted with the company Gestiontek to develop and set up an MIS software system that handles municipal inspections planning and follow-up for fire, sanitary, environment, and police inspections. Using this system, risk ratings for these four inspections functions are combined to create an overall rating for the business and coordinated inspections are easily planned:

[48] In Latvia, for example, before a state-of-the-art planning system was put in place in 2004 (the "Eskort" system), the State Revenue Service was using simple risk-filtering techniques to select the businesses to be inspected. This approach already represented a considerable improvement on the manual credibility check of returns that preceded this system.

- If risk is high for all inspectorates, a joint, multi-purpose inspection will be scheduled, and this will be done automatically by the software system.
- If risk is high only for one or some of the inspectorate(s), only the high-risk inspectorate(s) will inspect – that agency (or those agencies) will record issues of concern it identifies that are outside its scope of work on a unified checklist so that other agencies may undertake an inspection if needed. If overall risk is moderate or low, an inspection may be scheduled later – or not scheduled at all.
- Inspection reports and results are also uploaded automatically and quickly complement each business' data profile.

The system is easy to use and has helped decrease the inspections burden for businesses: inspections coverage and frequency has decreased for low-risk businesses while combined, multi-purpose inspections have reduced the number of separate inspections for higher-risk businesses.[49]

3.4 Checklists and Technical Requirements Review

3.4.1 Checklists: Define What Inspectors will Look for

An "inspections checklist" is a document developed by an inspecting agency to use in inspections of a given type of business. Checklists typically contain all the questions an inspector is likely to cover to determine an organization's compliance with the regulations in the inspectorate's sphere of competence. They are used routinely in countries as diverse as France, Germany, Great Britain, Latvia, Mexico, Uzbekistan, and Tajikistan.

There are usually many checklists for each inspections function because there are important differences between different types of businesses and other inspection targets. The fire safety department, for example, will usually have different checklists to inspect schools and hotels, gas stations and chemical plants. It is good practice to begin by developing checklists for the highest-risk targets or for those that are most numerous (e.g., markets, hotels, etc.).

Checklists should be developed on the basis of the legal documents (laws, regulations, safety norms, etc.) businesses must obey. At the same time, their purpose is not to include everything in these regulations but to focus on only the most essential and critical rules – the cases in which failure to comply could have serious consequences. Checklists should also provide for non-equivocal responses (yes, no, non-applicable) and avoid vagueness (e.g., the use of "etc.") to make sure that their questions are not interpreted ambiguously.

[49] There are many other examples of good IT systems for inspectorates. WBG IC teams are currently gathering more information on examples from Bosnia and Herzegovina (which has a single inspectorate) and Uzbekistan (an example of an IT system developed entirely by the local Coordination Council, without donor intervention). This information will gradually be consolidated and made available.

Inspectorates should cooperate closely with outside experts and businesses in developing checklists to ensure that the questions are informed by everyone's experience. These checklists should also be extensively tested in the field and adjusted on the basis of these tests. Their questions should be reviewed on a regular basis to adjust to new legislation, changing market conditions, and to new equipment and technologies used by businesses.

Since developing checklists is work-intensive, it is not realistic for any project to try to support all inspectorates of a country in the development of checklists for each type of business. However, a combination of examples in pilot inspectorates and guidelines for developing checklists disseminated to all other inspectorates can allow the use of checklists to spread gradually – especially in countries where there is a legal requirement to use them and the political will to introduce them.[50]

3.4.2 Review of Technical Requirements – How to Reach Results with Limited Means

As we have noted above, the benefits of inspections reform may be limited if a country's technical requirements are unsound: If the underlying regulations are obsolete or inadequate, inspections will, despite reform, still often result in unsatisfactory outcomes and in too many violations because businesses will simply not be able to comply with all the rules (either because the regulations are excessive or because they mandate the use of outdated technologies). Reviewing, streamlining, and updating all of a country's regulations requires considerable time and resources, however, and is beyond the scope of an inspections reform effort. Developing checklists can partially address this problem because, prepared properly, checklists will ensure that enforcement focuses on the essential and needed rules. At the same time, and even if the country in question is not ready to engage in a general review of its technical requirements, there are also a few lost-cost options that should be considered to help improve the underlying set of regulations.

3.4.2.1 Identify and target the worst rules

The requirements that are the most problematic (provisions that are particularly useless, obnoxious, costly, rarely respected, and hence promote corruption) should be identified through discussions with businesspeople, and then targeted for elimination as part of the inspections reform drive. As we have suggested above, Mongolia is a good example of a country where some useless requirements could be canceled to the benefit of businesses and inspectorates alike (without harming the public). Its regulations pertaining to the presentation of menus, for example, (menus have to start with appetizers and finish with drinks) and to the need for tourism inspectors to check the veracity of the information given by tour operators and guides about Mongolia's political and economic situation, traditions, and

[50] Additional details and many examples of checklists are included in the "Checklists manual" developed by the late Bobir Taymetov and others at the IFC (2009-2010).

religion could be canceled with only benefits for all sides (since inspectorates could then focus on more important issues) – except, naturally, for the rent-seekers.

3.4.2.2 Adopt internationally recognized norms where they exist

In areas such as food safely in which well-defined international safety norms exist (e.g., the *Codex Alimentarius* of the World Health Organization and the Food and Agriculture Organization's body of internationally accepted food standards, guidelines, and codes of practice), adopting these international safety norms can be part of the inspections reform effort. In the technical field, adopting, as is, international standards (e.g., from the International Organization for Standards or the European Committee for Electrotechnical Standardization, etc.) is a good approach. To speed up the introduction of international standards, it is can be helpful to use the "cover letter" approach (original standards are adopted simply by attaching a national cover letter to these standards) or the translation approach (international standards are simply translated into the national language and then adopted).

3.4.2.3 Get rid of useless fields of regulation

Finally, compulsory rules regulating areas that should be regulated by the market instead should be canceled. For example, compulsory standards regulating services (which are common in the countries of the former Soviet Union) should generally be canceled as, in good-practice countries, services are not generally subject to mandatory technical standards. Compulsory standards for low-risk goods (shoes, bottles, etc.) should also be canceled.

3.5 Training and Outreach

3.5.1 Training Inspectors

To make legal, institutional, and regulatory changes work effectively, it is important that inspections reform include training for the staff of the inspectorates. Such programs are especially important (a) to ensure that inspectorates' staff understand the reforms and implement the new procedures developed and (b) to change inspectorates' culture and help them develop a more client-oriented approach (Box 17).

3.5.2 Reaching out to Businesses

Reaching out to businesses and making entrepreneurs more aware of reform issues is also an essential component of inspections reforms. If regulatory changes are to translate into changed practices, businesses much understand their rights and know how to vindicate those rights. Publishing information on reform in the local media is an important way to increase the visibility of inspections reform within the business community. That effort must be complemented, however, by training and other outreach activities that ensure that businesses understand the details of inspections reform and know their rights.

BOX 21 Trainings for Leaders of Inspectorates and Inspectors in Latvia and Jordan

"Since inspectorates are legally part of the civil service, the School of Public Administration could be involved in their training. However, what was unique in the case of the Inspectorate Improvement Program was that the School agreed to tailor some of the training courses for inspectors specifically and arrange inspectorate-only courses. The School also accommodated the interests of the inspectorates to conduct training in their own premises. Altogether 492 participants attended the seminars organized within the framework of the Training Program for the Heads of Inspectorates and Inspectors.

Training of inspectors was carried out in the following areas – on how to establish an internal audit system, assess risks, prepare informational materials for the clients and create an information system. Eight inspectorates organized seminars specifically on *Client-oriented communication* delivered by the School of Public Administration as part of the civil servants' training program.

Two inspectorates – the State Labor Inspectorate and the State Fire and Rescue Service hosted a pilot training course on *Strategic Planning* conducted by a Swedish management consultant financed by the WB through a PHRD grant. This training was very well received by these two inspectorates, who carried on with the ideas and actually developed their strategic plans for 4-5 years, which now form the basis for their performance management systems. *Strategic Planning* helped to analyze the role and place of the inspectorate in the public administration, to identify the needs and problems of the clients and to plan activities so as to ensure the most efficient implementation of the legislation. Following the success of the pilot training and using the local trainer trained during the work with the above two inspectorates, seminars on Strategic Planning took place in seven other inspectorates – State Construction Inspectorate, Quality Control Inspection for Medical Care and Working Ability Examination, Consumer Rights Protection Center, State Inspectorate for Monitoring of Precious Metals' Standards, State Sanitary Inspectorate, State Technical Monitoring Inspectorate, Sanitary Border Inspectorate."

Source: Jacqueline Coolidge, Lars Grava, Sanda Putnina (2004). "Case Study: Inspectorate Reform in Latvia 1999-2003." Foreign Investment Advisory Service.

In Jordan, the IFC trained 100 environment and labor inspectors to use the inspections manuals developed for these two partner inspectorates, training inspectors about how to use checklists and forms, on the content of inspections legislation, etc. The IFC also conducted in-depth training in inspections management and planning skills for 22 labor inspections directors and senior inspectors.

Source: IFC(2010). "Advisory Services Project Completion Report, Jordan."

This kind of outreach to the business community works best when it is done in collaboration with partners that have a strong field presence in that community, including business associations, business training programs, and organizations that oversee business development at the grassroots level. It is a better practice to train people to conduct business training than to train businesspeople about inspections reform directly, because training trainers helps reach a higher number of entrepreneurs through a multiplier effect. In Tajikistan, for example, the IFC collaborated with NGOs, micro-finance providers, business

incubators, and business associations to conduct inspections training, and this strategy helped reach businesses even in remote areas of the country.

Trainings must be complemented by the distribution of information material (brochures, posters, leaflets, etc.) that explain the provisions of the inspections legislation. In Ukraine and Uzbekistan,[51] for example, the IFC supported the development and printing of a brochure for businesses that summarized the key provisions of the inspections legislation in a simple way and illustrated the issues visually. In Tajikistan, the IFC supported the development and printing of manuals both on the inspections regulated by the inspections law and on tax inspections. The IFC also supported the development of a poster summarizing the main points of Tajikistan's 2008-2009 inspections moratorium. All these materials were developed and published in close cooperation with the relevant authorities.

Experience demonstrates that it is important to collaborate closely both with relevant government agencies and with business representatives in developing such information materials. This practice helps ensure that the materials are endorsed by all parties concerned and are used by and useful to all stakeholders. Businesses in Uzbekistan reported, for instance, that having the seal of the Ministry of Justice on the cover of an information brochure was especially effective in stopping inappropriate behavior by inspectors.

Conducting surveys before and after issuing information materials can also help to assess the effectiveness of that information. In Uzbekistan, a follow-up question included in the 2004 SME survey showed us that a brochure on inspections had been very effective: The share of SMEs estimating that they had good knowledge of the inspections legislation increased from 30 percent in 2002 to 41 percent in 2004, while 49 percent of SMEs reported using the brochure during inspections and 84 percent declared that they were satisfied with the content of the brochure.

It is also important to publish communications materials in local language(s), to reach out to businesses in remote areas, to make information material available to businesses free of charge and to ensure broad printing and dissemination of communication materials. In Uzbekistan, the BEE project compensated for its limited means by granting printing rights to partner business associations and to regional administrations. Some of these associations and administrations printed additional copies of the promotional brochure with their own budgets, and business associations alone printed 10,000 copies of the brochure.[52]

[51] Several examples of this kind of information material are available on the WBG IC intranet and more will be gradually added. As languages, cultural contexts, levels of development, and, of course, the regulations themselves differ widely in various nations, these examples can only be used as inspiration and, in the end, such information material must be developed separately for each country.

[52] Anvar Meliboev (2005). "Improving Legal Awareness of SMEs through an Inspections Brochure," IFC Smart Lessons.

3.6 Diagnosis and Results Measurement

3.6.1 Key to Proper Design – the Right Diagnosis

Getting detailed data on inspections is essential in order to understand why inspections are a burden for businesses in any given country. Establishing the right diagnosis of the problem will help reformers identify the right priorities and design a reform that will address the causes of the problem and is likely to bring tangible benefits.[53]

As we have explained in the chapters above, there are many reasons an inspections system may become a burden for businesses, including a high frequency of inspections, the excessive discretionary power of inspectors, obsolete or overly prescriptive requirements, lack of access to the regulations businesses must obey, overlapping inspections, a lack of clarity in the inspections process itself, an inappropriate sanctions scale, and an inappropriate incentive system for inspectors. Gathering detailed data on inspections will help identify which problems are most important in any given situation and which reforms should be a priority.

Existing data (mostly official statistics), business surveys, and calculations using the standard cost model are the main quantitative tools available to measure the impact of inspections. These tools all have shortcomings, however, and it is good practice to combine them with information from qualitative tools such as focus groups.

Official statistics are the only way to measure the effectiveness of inspections in protecting health, safety, and the environment and guaranteeing state revenues. (e.g., statistics on fire-related and work-related loss of life, the incidence of food-borne diseases, etc.). Official statistics are also a source of information for statistics on inspections themselves (e.g., the number of businesses inspected, the proportion of inspections identifying violations, proportion of inspections resulting in sanctions, etc.). However, in countries where the WBG works on inspections reform these statistics are often unreliable: statistics on inspections outcomes are typically under-reported, both at the local and at the national level (e.g., businesses tend to under-report work accidents, state agencies tend to under-report "embarrassing" figures such as the number of fatalities, etc.), resulting data that is often meaningless – except in the case of exception of tax revenue data, which is usually more accurate. The number of inspections reported by inspectorates also tends to be unrealistically low, in part because inspectors regularly conduct unofficial, unregistered inspections, often with rent-seeking purposes. Given these shortcomings, official data are not fully reliable and must be complemented by additional data collection tools.

Business surveys are one of the most effective ways to collect data about inspections in any given country. Yet cross-country WBG business surveys such as the "Business Environment

[53] Given the availability of a full-fledged note on "Assessment Tools for Inspections" (IFC, 2009), what follows is just a short outline, and details should be found in that note if needed.

and Enterprise Performance Survey" (BEEPS) do not really capture the burden of inspections (they include only two inspections-related questions and those focus exclusively on tax inspections) while the "Doing Business" report does not cover inspections at all. As a result, additional business surveys covering inspections usually need to be conducted in countries where we work to create reform.

Business surveys can collect detailed information about inspections: their coverage and frequency, average duration, the proportion of non-compliance, the type of sanctions applied as a result of non-compliance, the incidence of unofficial payments, etc. Surveys can also measure the average annual cost of inspections for businesses, including their time, cost, and the cost of official and unofficial payments. The average annual cost of inspections can then be multiplied by the number of businesses a country has to estimate the total cost of inspections for the private sector. Depending on how the sample is constructed, business surveys can also provide results by business size, sector of activity, region, etc. These data allow for more detailed analysis.

Unfortunately, business surveys can be costly (particularly in countries with high labor costs but also in places where there are too few survey firms, etc.), they are lengthy and their quality depends not only on the quality of their design (methodology, questionnaire, etc.) but also on the quality of the contractors' work (including the enumerators).

The standard cost model (SCM) is another quantitative tool to estimate the average administrative burden incurred by a "typical" business to comply with a given "information obligation," including time and other internal costs as well as external costs, if relevant. The estimated yearly cost per business can then be multiplied by the number of businesses in the country to estimate the total burden for the private sector. The SCM was initially designed to capture the cost of procedures such as licensing or reporting, but it can be adapted to capture the cost of inspections. In many cases, SCM calculations are based on the identification of a "typical" business experience for a given procedure. In the case of inspections, this identification can be very difficult, however, as the experience of various businesses subject to inspections varies greatly, often as a result of inspectors' excessive discretionary power. As a result, the SCM approach is usually rather poorly adapted to design proper questions for business surveys.

However important these quantitative tools may be, they are unable to capture some of the qualitative information that allows us to interpret these numbers, and they must therefore be complemented by the use of qualitative tools such as focus groups. Such groups are a critical complement to business surveys during their design stage (to identify what the key inspections issues are and design the questionnaire accordingly) and during the analysis of survey results (to help interpret those results that are not readily understandable). Focus groups can also help bring a survey report to life with concrete examples of problems faced by real businesses and help verify recommendations for reform and ensure that those ideas are really in businesses' best interest. Yet while focus groups are a very useful, and relatively

low-cost, tool to assess the burden of inspections, they must be well-prepared and skillfully moderated to be effective.

All inspections assessment tools have their own strengths and limitations. It is good practice to use as many measurement tools as possible during an inspections assessment and to sequence them appropriately (e.g. to start with existing statistics and focus groups, continue with a business survey, go back to focus groups, etc.). To use these assessment tools effectively, the staff in charge of the assessment must be knowledgeable about the inspections system in the target country. It is also good practice for this staff to seek peer review and advice from experienced staff in other teams at all steps of the assessment process to ensure that the data collected is of appropriate quality, and thus is usable.

Detailed data on inspections and appropriate communication of this data to the government and the press of the country in question are of paramount importance in building the case for reform, winning high-level political support for reform, and overcoming the opposition from vested interests within inspectorates.

3.6.2 Results Measurement – Plan from the Start, Link to Diagnosis

Inspections assessments also provide the baseline data against which changes will be measured that are essential to judge the effectiveness of any inspections reform project. Knowing what the cost of inspections for businesses was before, and is after, reform is an essential tool to evaluate the impact of an inspections reform on the investment climate. The failure to document the impact of the environmental inspections reform in Mexico on the cost of doing business was a major shortcoming of that reform.

Knowing the effectiveness of inspections in protecting health, safety, and the environment and in guaranteeing tax revenue, before and after reform, is also essential to evaluate the effectiveness of reform in improving business compliance with rules and norms. As we have indicated previously, flawed statistics can make the impact of reform difficult to establish. In that context, one of the important roles of WBG advisory services can play is to support inspectorates' work to improve their data collection and reporting mechanisms.

Knowing the preliminary impact of an inspections reform is also an important monitoring tool during an inspections reform, a powerful way to show that reform is moving in the right direction and an effective way to maintain the momentum for additional reforms. For example, the 2009 "Business Environment in Tajikistan as seen by SMEs" report estimated that "the 2006 Inspections Law and its implementation resulted in annual savings to the Tajik SME sector of $9.3 million."[54] This figure clearly indicated that inspections reform was bringing tangible benefits and created momentum within the Tajik government for additional reforms.

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World Bank Group

MIGA
World Bank Group
Multilateral Investment
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