

Center for International Private Enterprise

# ECONOMIC REFORM

## Issue Paper

---

No. 0405 January 22, 2004

## **Democratic Governance: The Key to Political and Economic Reform**

Lack of democratic governance seriously threatens democracy-building and market-based reforms worldwide. In some countries, the absence of democratic governance has engendered populism, socialism, and even terrorism. Establishing the necessary governance institutions is essential to the future of democracy and free markets and to the stability of the international system.

The political, economic, and social consequences for countries lacking democratic governance include: widespread corruption; poor infrastructure; high business costs; low investment, growth, employment, and income levels; national, regional, and international instability; and growing citizen disappointment.

This paper presents a series of policy recommendations and strategies that provide members of the private sector and civil society, government officials, and foreign aid donors with essential tools to establish democratic governance. The report also highlights several case studies that reveal the experiences of CIPE and its partners in building better democracies. The report concludes by emphasizing that democratic governance is the linchpin for successful political and economic reform and that countries that have instituted democratic governance have achieved superior development outcomes.



published by the  
**Center for International Private Enterprise**  
an affiliate of the U.S. Chamber of Commerce  
1155 Fifteenth Street NW • Suite 700 • Washington, DC 20005 • USA  
ph: (202) 721-9200 • web: [www.cipe.org](http://www.cipe.org) • e-mail: [cipe@cipe.org](mailto:cipe@cipe.org)

CIPE Authors:

**John D. Sullivan, Ph.D.**, Executive Director

**Aleksandr Shkolnikov**, Global Program Officer

**Catherine Kuchta-Helbling, Ph.D.**, Global Program Officer

**The Center for International Private Enterprise** is a non-profit affiliate of the U.S. Chamber of Commerce and one of the four core institutes of the National Endowment for Democracy. CIPE has supported more than 800 local initiatives in over 90 developing countries, involving the private sector in policy advocacy, institutional reform, improving governance, and building understanding of market-based democratic systems. CIPE programs are also supported through the United States Agency for International Development.

This paper was presented at the The World Movement for Democracy in February 2004 in Durban, South Africa. The World Movement for Democracy is a global network of democrats including activists, practitioners, scholars, policy makers, and funders, who have come together to cooperate in the promotion of democracy. The World Movement seeks to strengthen democracy where it is weak, to reform and invigorate democracy even where it is longstanding, and to bolster pro-democracy groups in countries that have not yet entered into a process of democratic transition.

**For more information, contact:**

Center for International Private Enterprise  
1155 Fifteenth Street NW • Suite 700  
Washington, DC 20005  
USA

ph: (202) 721-9200 • fax (202) 721-9250  
web: [www.cipe.org](http://www.cipe.org) • e-mail: [cipe@cipe.org](mailto:cipe@cipe.org)

## Introduction

Global democratization efforts of the past few decades have often fallen short of the desired outcomes, and while 140 countries are now viewed as electoral (holding multi-party elections) democracies,<sup>1</sup> more than half of them are flawed by disregard for human rights, freedom of speech, full citizen participation in the decision-making process, protection of property rights, and government accountability. Those emerging democracies remain illiberal and unconsolidated and continue to suffer from low growth, corruption, and growing citizen disappointment. As a result, many citizens in emerging democracies are rejecting democratic, market-based reforms and are embracing populism, socialism, and terrorism. Uncovering the roots of this poor performance is vital to the future of democratic, market-based systems across the globe.

For the past several decades, the conventional wisdom has been that the plight of developing countries was due to a lack of resources, technology, education, and infrastructure. Hence, donors focused on providing and improving these aspects in the hopes of promoting development. Although a significant amount of these transfers has helped, the overall results in promoting sustained development have been poor to date – in fact, more than 50 countries experienced a declining per capita GDP in 1990s, and some countries are poorer now than they were 30 years ago.<sup>2</sup>

The reason for the democratic deficit, i.e., lack of democratic institutions, the poor economic performance of many countries, and citizens' discontent with market reforms lies not in the policy recommendations, but rather in the failures of policy implementation. Many governments and international experts are quick to propose reforms; yet, they often fail to take into account the very institutional problems that threaten implementation of the reforms on a day-to-day basis. Countries often fail because policy implementation is undermined by corruption, poor institutional development, opaque legal systems, weak enforcement mechanisms, a lack of transparency in administration, and an inability to provide and effectively manage public services.

Recent financial crises in Asia, Russia, Turkey, and Latin America demonstrate that failure to incorporate democratic governance as part and parcel of economic reforms seriously jeopardizes the entire reform agenda. These crises, as well as growing discontent with democracy and lackluster economic performance in emerging or new democracies, have helped to focus increased attention on the importance of democratic governance across the globe. Diverse civil society groups and private and public sector representatives from emerging democracies highlighted the significance of good governance in commitments such as the Sana'a Declaration, the

Monterrey Consensus, and the New Economic Partnership for Africa's Development, among others. International funding agencies and the U.S. government have made sound governance a funding prerequisite.

One of the reasons for the continuing disappointment with democracy-building in the developing world is that citizens in many democracies (emerging, transitional, or otherwise) remain excluded from policymaking, are forced to comply with laws and regulations that were decided upon in a non-transparent manner, and lack any method to redress grievances and thereby secure their rights and/or improve the system. The "Governance and Democracy Survey" conducted by Gallup International<sup>3</sup> in 1999 revealed that over 60% of the people worldwide believe that their countries are *not* governed by the will of people, even though a majority of them agreed that elections in their country *are* free and fair. Thus, simply holding democratic elections is not enough – governments in many countries are not held accountable, and their exercise of discretionary powers often hampers the development efforts.

Hence, the key to a successful and sustainable transition to a democratic, market-based system hinges on effective democratic governance, i.e., on key institutions of accountability. By relying on those institutions, democratic governance holds government and government officials accountable on a daily basis.<sup>4</sup> These institutions oblige leaders to consult citizens and take their interests into account so that public resources are used to uphold basic political, civil, and economic liberties and to provide the public goods necessary for growth (as opposed to being used to enrich the ruler and his/her cronies).

Despite an increased interest in the benefits of democracy, transparency, accountability, and market mechanisms, distilling concrete policies and regulations that uphold those values in practice requires more than good will. Understanding the fundamentals necessary for true implementation of promises of democratic governance is what marks success or failure in economic and political transition. The difficulty in obtaining this crucial understanding is what dooms many reform efforts, even the most well intentioned. This is because a clear roadmap of what democratic governance is and how it can be achieved remains quite elusive.

This report aims to respond to this need by clearly defining the concept of democratic governance and by specifying effective tools and programs that promote it. The report argues that instituting democratic governance is the key to addressing the democratic deficit, consolidating democratic and market-based reforms, generating sustainable economic growth, and equipping countries to take advantage of globalization.

## Dangerous Myths of Development

Despite the progress made in gaining a better understanding of the complexities of building market-oriented democratic societies, there are three dangerous myths loose in the international development community that can be used to illustrate how much further we still have to go.

The first myth is the belief that once private enterprise constitutes a substantial portion of an economy, it has become a market economy. History abounds with examples of where this has not been the case. The Philippines under Ferdinand Marcos and Indonesia under Suharto are classic examples of economies that were capitalist, based on private enterprise. But they definitely were not open-market systems. Economists call this type of behavior “rent seeking,” and terms like corruption and cronyism are more generally used by others. Simply stated, the greater the degree of systemic corruption in a society, the less its economy functions on market principles, and the greater the danger to democracy.

It should be emphasized that many different types of market economies are possible, and there are real distinctions between the institutional structures in different countries. But *all market economies share a common feature: a competitive system where the rules are the same for all participants*. The key institutions include firm property rights, anti-trust regimes (or competition policy), contract enforcement through rule of law, strong corporate governance systems, and freely flowing information (transparency). Together they create the framework for a competitive market system where freedom of entry and exit are guaranteed. Furthermore, only a fully functioning democratic governance system can sustain such a system over time.

The second myth is grounded in the common misconception that the business community or the private sector in general is a homogeneous monolith that either supports or opposes certain policies or leaders. This is not the case. In fact, most countries have several business communities, each with its own interests and objectives. In the economy of a single country there can be the state sector, the private sector, and the informal sector. Even within the private sector, there might be firms and entrepreneurs who work mostly in international trade, while others are engaged in producing solely for the domestic market. Clearly, these two groups will not always support the same policies. Nor will they always favor market-oriented reform.

Firms created behind protectionist trade barriers—and with strong links to and benefits from government—tend to support the status quo. Often they also are quite anti-democratic. Conversely, firms that have been locked out

### Box 1:

#### Common Definitions of Governance

**World Bank:** The World Bank defines governance as the traditions and institutions by which authority in a country is exercised for the common good. This includes (i) the process by which those in authority are selected, monitored and replaced, (ii) the capacity of the government to effectively manage its resources and implement sound policies, and (iii) the respect of citizens and the state for the institutions that govern economic and social interactions among them.

**United Nations Development Programme:** Governance can be seen as the exercise of economic, political and administrative authority to manage a country’s affairs at all levels. It comprises the mechanisms, processes and institutions through which citizens and groups articulate their interests, exercise their legal rights, meet their obligations and mediate their differences.

#### Definition of Democratic Governance

**CIPE:** Democratic governance comprises the traditions, institutions, and processes that determine how government decisions are made on a daily basis, and addresses the following questions:

- How and to what extent are citizens given a voice in day-to-day policymaking?
- How efficiently are public resources and services managed?
- How are abuses of governmental power prevented?
- How are government officials held accountable for their actions?
- How are grievances redressed?

Sound democratic governance mechanisms help to create *functioning* democracies.

of government favors, including small entrepreneurs and those engaged in international trade, are quite often the leaders behind the demand for change. Because business communities are so diverse, it is wiser to form partnerships with business associations, think tanks, foundations, and other business organizations that have a vested interest in an open economy and a democratic political system.

The third myth is the most dangerous and is often called the market fundamentalists’ view. It is the belief that markets will spontaneously emerge if the government

stops intervening in the economy. This is far from true. The government must underwrite and guarantee consistent, fair rules and laws so that a strong market economy may emerge. Further, government institutions and self-regulating organizations have key roles to play in ensuring that the rules are enforced. Credible, fair bank supervision is but one of the most obvious of these functions.

Without binding rules and structures that govern all players, anarchy follows. Business then becomes nothing but “casino capitalism” where investments are only bets: bets that people will keep their word and that companies will tell the truth; bets that workers will be paid; and bets that debts will be honored. Conversely, recent experience suggests that these myths could be discarded, and the sterile debate between those who espouse neo-liberalism and those who attack it as misguided market fundamentals should be ended. In fact, three general observations about how democracy and markets interact should be the focus of discussion.

### **Democracy and the Market – Mutual Support**

Contemporary history has shown that countries with democratic, market-based systems are best equipped to respond to the challenges of globalization. Specifically, there are four essential aspects of democracy that have proven to be crucial to long-term economic and social development:

- A sound democratic system is the best guarantor of political stability, which is essential for long-term economic growth and private sector investment.
- Democratic values such as transparency and accountability are essential for effective and responsive government and for efficient and prosperous economic activity. (The financial crises Asia and Russia experienced in the late 1990s are cases in point.)
- Sound legal and regulatory codes backed by the rule of law must exist if business is to thrive in a market economy.
- Decision-making procedures that allow for participation and feedback from the private sector, civil society, labor, political parties, and other citizen groups have to be established. Without systems of feedback and accountability, governmental regulatory processes, budgeting, and other aspects of day-to-day governance lose touch with the very people and groups they were established to serve. (Examples include comment and notice periods, public hearings, and pre-publication of proposed regulations.)

While there are many issues and reforms that make up a successful democracy, countries that succeed in addressing these four central challenges also succeed in fulfilling the wishes and aspirations of their people and in creating

economic opportunities essential for human growth and poverty reduction. Conversely, those that fail to establish a democratic system of governance find that progress is halting and that they will not be able to take advantage of the many opportunities that globalization provides.

### **The Democratic Deficit**

Market-oriented reform and democratic development are mutually reinforcing factors that can, in the best circumstances, lead to a virtuous circle of development and stability. But if that is true, why is it not to be found more often? How is it that an entire decade of reforms in Latin America is threatened or that countries throughout Africa and the Middle East can't seem to find a way into the virtuous circle that brings citizen support for more reform?

One answer may be found in how democracy and market reforms are thought of by most Western sources of funds and by their advice to counterparts in emerging markets and developing countries. To begin, there is a long-standing consensus that democracy requires free and fair elections, motivated and informed citizens, well built political party structures, a vibrant and self-disciplined media and civil society, and (most recently) the support of the business community. Yet, there is one absolutely vital missing ingredient: the day-to-day decision-making processes by which a country governs democratically.

With some notable exceptions, such as Hernando de Soto, most theorists and practitioners fail to take apart the black box of governance processes to see how they lack democratic values of transparency, participation, fairness, and equity. Similarly, those advocating for market reforms normally fail to include political considerations or the participation of the citizens within the design of the reform program. The heavy concentration on technical experts as designers of reform fails on several levels.

Most importantly, it ignores the fact that reforms must incorporate what Dani Rodrik calls local knowledge, and ways must be found to mandate public participation in the design of reforms. This is a process which government officials and technocrats rightly fear, because it has the potential to dramatically slow reforms. However, if procedures are developed to channel this interaction at several different stages in developing the reforms, the payoffs of superior adherence to the reforms are well worth it.

The weakness in institutional development, the frequent lack of implementation, and the often poorly designed reforms constitute a democracy deficit that threatens to reverse several decades of progress. This democracy deficit is all the more troubling because it often goes unnoticed amongst the triumphalism that heralds a transition to

democracy and the design of market-oriented reforms. To one degree or another, this democracy deficit is affecting nearly every region of the developing world.

Long thought to be a shining example of reform, Latin America has been jarred by economic crises that have led to a resurgence of populism and a broad-based skepticism about supposed “market reforms” that were, in fact, never truly implemented. Central Europe, having seen an inspiring sea-change in the early 1990s, has been the only region to show real growth in the past year, yet the Balkans and Central Asia continue to beget leaders who would consolidate their power, rally nationalist fervor, and distort ‘markets’ for personal gain. Socialism, religious extremism, economic crises, and entrenched dictators all plague various parts of Asia. Africa faces the aforementioned problems, as well as simmering conflicts, a serious lack of infrastructure, health crises, illiteracy, and an absence of market mechanisms, governance structures, and management experience to address problems effectively. The Middle East, with its own conflicts, wealth disparities, extremists, and repressive regimes, also appears near the bottom of the scale in many aspects of development.

### What is Democratic Governance?

Democracies cannot be built by simply organizing political parties and holding free and fair elections — if citizens have little opportunity to communicate their preferences to their representatives between elections and to hold their representatives accountable for their decisions, they are, in fact, handing these representatives a blank check for the entire term. Rather, the key to a successful building of democracies and economic reforms is democratic governance, which comprises the traditions, institutions, and processes that determine how government decisions are made on a daily basis.

Democratic governance requires vehicles through which citizens can routinely participate in policymaking. Governments often fear that this will make the policymaking process slower, yet, the more inclusive the process, the more responsive the resulting policies, laws, and procedures will be. Democratic governance also requires institutions of accountability to prevent the abuse of power. Constitutional rules that stipulate how power is distributed, checked, and balanced (often referred to as mechanisms of horizontal accountability) tend to be effective at preventing gross power abuses and fostering stability.<sup>5</sup> Yet, additional mechanisms to minimize more subtle, routine, and/or daily abuses of power and office are needed, and this is where governance comes into play.

How do citizens ensure that the government, particularly those agencies not directly beholden to elected

officials, upholds its promises and implements/enforces stated policies swiftly, correctly, and consistently? What if citizens suffer damages from government action or inaction? Solving such issues through an intermittent voting process is clearly inadequate. Similarly, taking the government to court to solve minor or routine issues is likely to be time consuming, expensive, and impractical.<sup>6</sup> Hence, democratic governance also requires mechanisms through which citizens can routinely and inexpensively seek redress for grievances committed by the government and thereby improve governance.

Governments with institutions of accountability are more likely to govern democratically and, thus, to enjoy widespread support among citizens, whereas those that do not are unlikely to be re-elected and are likely to suffer from pervasive illegitimacy, inefficiency, and a whole host of other problems.

### The Effects of Bad Governance

Overlooking democratic governance is an omission with potentially serious individual, national, regional, and international consequences. Many emerging democracies and market-based economies fail to uphold basic liberties and suffer from widespread corruption, poor infrastructure, low economic growth, disease, and, at times, violence because they lack institutions of accountability. The lack of democratic governance may be to blame for the failures of many countries, despite the incredible amount of foreign assistance in the last decade.

Poor performance of countries has eroded the legitimacy of and support for democratic, market-oriented systems. Citizens in many countries lose faith in democratic systems and market reforms simply because too often they don’t gain anything from economic reforms or democratic political systems. Rather, they face a situation where corrupt government officials and a few elites are the only ones who benefit from the reforms. Citizens who have gained little from the transition process and have little voice in the policymaking process become targets for those aiming to reverse key political and economic reforms. Recently, in several emerging democracies and economies, socialism has been rejoined by nationalism, populism, and terrorism – challenging fragile states and leading to backsliding. In some cases, entire transitions are at risk.

Following is the outline of the negative effects of bad governance on political and economic development of countries. Lack of democratic governance:

#### *Leads to unresponsive policies and uneven playing fields*

When citizens have little opportunity to shape laws, policies, and regulations, the resulting framework is unlikely to be responsive to citizens’ needs. Such exclusive decision-

making procedures make aggregating dispersed interests and fostering accountability very difficult.<sup>7</sup> Moreover, a lack of control mechanisms, such as a separation of powers, makes governments vulnerable to power concentrations and state capture. The result is that a handful of elites design laws, policies, and regulations for their own benefit often to the detriment of the general population. Examples of unresponsive regulations include those that limit competition in certain sectors or require huge amounts of resources to set up and run a business. This creates barriers to entry, hinders competition and growth, and forces entrepreneurs into the informal sector.<sup>8</sup>

#### *Erodes legitimacy and support for democracy and key reforms*

Governments that fail to enact responsive policies and provide essential goods and services are, in essence, renege on their commitment and thus are unlikely to be viewed as legitimate. For example, recent statistics indicate that poor governance in Latin America has weakened the legitimacy of and popular support for democracy (Diamond 2002 :41).<sup>9</sup> In turn, citizens will be reluctant to offer an illegitimate government support for tough political and economic reforms, thereby hindering democratization and marketization. In some cases, citizens may engage in coups or revolutions to dispose of illegitimate regimes, as has happened in a number of countries in Latin America.

#### *Creates unstable legal and regulatory frameworks*

Democracies that lack control mechanisms, such as the separation of powers and transparent practices, are prone to power concentrations, frequent legal and regulatory changes<sup>10</sup>, and budget volatility. Unstable and opaque legal and regulatory codes increase the risk of non-compliance and raise the costs of doing business. Similarly, a lack of budgetary transparency and accountability<sup>11</sup> produces volatile budgets for government agencies that provide key goods and services. Volatile budgets, in turn, limit the ability of government agencies to administer and enforce laws, regulations, and policies consistently and swiftly<sup>12</sup>. This uncertainty and inefficiency leads to a bad investment climate, deterring entrepreneurs from setting up businesses and investors from investing.

#### *Results in inconsistent and poor quality goods and services*

Stable and well designed legal and regulatory frameworks and budgets are not enough to guarantee consistent delivery of quality goods and services essential to a democratic, market-based system. Each government agency that administers, implements, or enforces laws, policies, and regulations needs to be well governed. This means that agencies and civil servants need to be

monitored and held accountable for their actions (or inactions). In particular, citizens need to have avenues of recourse when the government fails to deliver or when government officials or private parties violate the law. By way of example, businesses need permits to operate, and if obtaining a permit takes several months or even years instead of several weeks, entrepreneurs need to be able to hold the government accountable for forgone profits. Similarly, citizens need to have a means of redress for unpunished contractual violations because of an ineffective judiciary. In all of these cases, democratic governance has an important role to play.

#### *Squanders and misallocates foreign and domestic resources*

Without institutions of accountability, foreign and domestic resources are squandered and misallocated. First, without participatory decision making, resources are often allocated to projects benefiting a handful of people or groups as opposed to the majority of the population. For example, industrial elites that produce for the domestic market are able to convince the government to provide subsidies or barriers that erode competition. Similarly, powerful contractors often persuade their government to embark on huge public works projects that may not be in the public's best interest or that are provided at exorbitant costs at the taxpayers' expense.

Second, when government agencies lack systems of accountability and transparency, giving them more resources is unlikely to resolve the problem. In some extreme cases, such as Peru, Zaire, and Zambia, foreign assistance and public revenue is merely funneled away into the bank accounts of rulers, friends, and families of rulers and government officials. In short, the lack of democratic governance is one key reason why so many foreign assistance projects and domestic reform initiatives have failed to generate sound democracies and market-based economies and sustainable growth.

#### *Encourages corruption and stunts growth*

Poor democratic governance leads to corruption, and there are a number of studies that have confirmed that poor rule of law and accountability (key governance institutions) are correlated with higher levels of corruption. It is a known fact that corruption hinders political and economic development, causes lower growth rates, increases business costs, and deters investment. In 2002, the Executive Business Survey, asking businesses in emerging economies to rate the top business constraints, revealed that corruption and ineffective government bureaucracy were top concerns after securing finance.

Corruption in the privatization processes in many emerging democracies and economies illustrates these

points. The privatizations that took place without proper institutions resulted in asset stripping, inaccurate asset valuations, and privatized monopolies that offer poor quality goods and services at unreasonable rates. In many cases the new owners and/or managers of privatized companies are closely linked with state officials, and they have used these connections to engage in state capture and to resist important market-oriented reforms that would reduce their power.

Corruption also reduces government revenue for essential goods and services, hinders sound fiscal management, and exacerbates poverty and inequality. Finally, corruption erodes the legitimacy of key political and economic institutions, such as the rule of law, which are essential for economic growth. Without the rule of law, property rights are not secure. Insecure property rights prevent entrepreneurs from obtaining credit at reasonable rates to start or expand businesses and deter investors from investing, even if cheap credit is available.<sup>13</sup>

Conversely, numerous recent studies indicate that in countries characterized by the rule of law, extensive transparency, effective parliamentary oversight, well functioning mechanisms of voice and accountability, and high standards of corporate ethics, there are lower levels of

corruption and higher GDP growth rates than countries lacking these characteristics<sup>14</sup>. In fact, some studies<sup>15</sup> found that countries with exclusive institutions have lower employment levels and growth rates and are much poorer because they failed to create opportunities for wealth and asset creation. Together these findings confirm that good democratic governance, not simply democracy, is linked to higher growth rates<sup>16</sup>.

#### *Lowers income and increases illiteracy and infant mortality levels*

It has been shown that countries with inferior mechanisms of voice and accountability – key pillars of democratic governance – have lower national incomes, higher infant mortality rates, and higher illiteracy rates.<sup>17</sup> In particular, in one of his studies Daniel Kaufmann<sup>18</sup> found that weak rule of law is directly tied to low incomes and high infant mortality and illiteracy levels. Similarly, other studies<sup>19</sup> found that poor mechanisms of voice and accountability can be responsible for suppressing current national income levels by a factor of 2.5, and that poor democratic development and a lack of free speech can exacerbate famine<sup>20</sup>. It has also been shown that undemocratic practices can be related to fewer and worse

#### **Box 2:**

#### **Budgetary transparency**

A key way to hold governments accountable is to monitor how they spend revenues. Doing so requires budgetary transparency that can be attained by adopting and implementing the Organisation for Economic Cooperation and Development's (*OECD Best Practices for Budget Transparency*) issued in September 2000.

The OECD best practice guidelines are in three parts:

Part I lists the principal budget reports that governments should produce and their general content: the budget; a prebudget report; monthly reports on budget implementation; a mid-year report; a year-end report; a preelection report; and a long-term report.

Part II describes specific disclosures to be contained in the reports: economic assumptions; tax expenditure; financial liabilities and assets; nonfinancial assets; employee pension obligations; and contingent liabilities.

Part III highlights practices that ensure the integrity of reports: accounting policies; systems and responsibility; audit; and public and parliamentary scrutiny.

Other useful tools to enhance budgetary transparency include:

- The International Budget Project is compiling an Index of Budgetary Transparency that aims to measure in a comparable form the degree of accessibility and usefulness of information provided by national government with respect to finances, revenue, and expenditures. (Please see [www.internationalbudget.org](http://www.internationalbudget.org) for more information on the index and for a wealth of information on improving budget policy and transparency.)
- The Institute for Public Finance in Zagreb, Croatia has published "A Citizen's Guide to the Budget," which provides tips and strategies for understanding the budget and the budgetary process. The Guide is available at: [www.ijf.hr](http://www.ijf.hr).
- The International Monetary Fund's Manual on Fiscal Transparency available online at: [www.imf.org/external/np/fad/trans/manual/index.htm](http://www.imf.org/external/np/fad/trans/manual/index.htm).

commitments to protect the environment and safeguard resources essential for economic growth.

### *Fuels economic and political crises*

Countries without institutions of accountability are prone to financial crises. Today it is widely recognized that the financial crises in Asia, Russia, and Latin America were due to poor governance. Institutions of accountability are particularly important in the financial sector. They help prevent connected lending and asset stripping, which can seriously damage an economy. In fact, results from the 2002 Executive Opinion Survey confirm that the level of governance is correlated with the health of the financial sector<sup>21</sup>. Moreover, financial and economic crises breed political instability.

### *Jeopardizes national, regional, and international security*

States lacking democratic governance are security threats. States that lack the means to create and enforce well designed laws and regulations and to provide essential services, including security to its citizens, are vulnerable to a whole host of problems. First, they will be ill-equipped to resolve disputes peacefully and expeditiously either between individuals and the government, between individuals or groups, or between governmental branches (including between the military and the civilian-led government departments). Unresolved conflicts could then escalate into violence and even civil war. Poorly governed nations are also unprepared to prevent the spread of disease, organized crime, and narcotics trafficking and to curb fraud, money laundering, terrorism, and human rights abuses.<sup>22</sup> Such activities have debilitating and destabilizing effects nationally, regionally, and internationally.

## **How Can Democratic Governance Be Attained?**

Attaining democratic governance is an ongoing challenge that requires a multitude of initiatives from the private and public sectors and civil society organizations. This section describes some of the key means through which this challenge can be met. These recommendations should be considered as tools which citizens and governments can use and adapt to create their own institutions of accountability that are best suited to their local realities.

### *Increase transparency*

One of the most important steps to improve democratic governance is through the provision of information. Information fosters transparency and accountability and thus good governance in all spheres. Transparency is the flow of timely, comprehensive, and reliable economic, social, and political information. There are several

### **Box 3: Effective Governance**

In 2004, the Asia Foundation, a non-profit organization working in the Asia-Pacific region, distributed a governance survey to evaluate local governments in terms of practices and initiatives related to good democratic governance. The results of the survey will be used to develop a good governance scorecard for local governments. Respondents were asked to rate the level and degree of efforts, initiatives, and practices of city governments on specific issues. The survey asked to rate:

- The degree of professionalism exhibited by city employees and officials in the conduct of their duties and responsibilities.
- Access to information on how city government funds are used and how cost-effectively they are spent.
- Transparency of the city government's system for bidding and procurement.
- Sincerity of the city government to communicate with the public through a Public Information Office.
- The degree to which a system of checks and balances is prevalent and practiced within the city government.
- The level of participation of civil society and private sector representatives in the enforcement and monitoring of the code of ethical conduct and practices within the administration.
- The degree of awareness of the city government's employees of the scope and limitations of their respective department's mandate, functions, authority, and jurisdiction.
- The sincerity of the city government to measure performance against publicly accepted targets and goals.
- The establishment and implementation of a sustained long-term education and information program for city employees and officials that is geared towards instilling a governance culture and values.

To view the complete survey, the survey results, and the scorecard, please visit the Asia Foundation at [www.asiafoundation.org](http://www.asiafoundation.org).

### Case Study: Latin America - Journalists Against Corruption

Corruption continues to be the greatest threat to democracy in Latin America. Corruption hinders the development of democratic institutions and, by discouraging foreign and domestic long-term investment, it retards economic growth, entrepreneurial activity, and the development of open and competitive markets. Corruption also perpetuates poverty, which is accentuated by inequities in the justice system, the absence of rule of law, and impunity. And the lack of public pressure and an ideological or muzzled press make corruption an attractive and safe practice in Latin America.

With few exceptions, media reports of corruption have had the most impact in exposing bureaucratic corruption in Latin America. However, frequently, those reports have been selective, incomplete, colored by ideological slants, and even inaccurate because of the internal censorship of editors and media owners who are tied to or bow to pressures of governing parties and economic elites. This is why Journalists Against Corruption (PFC) was launched in August 2000 as a project that would strengthen Latin America's most promising anti-corruption tool - watchdog journalism.

PFC is an expansive and dynamic anti-corruption online clearinghouse, a network, service provider, and support system for Latin American journalists and media that cover corruption in the region. It provides journalists with a venue to obtain and exchange information, contacts, and investigative assistance, to benefit from a regional network, and to learn how to more effectively combat corruption and support anti-corruption initiatives. In addition, PFC monitors and disseminates information about legislation, court rulings, and actions that facilitate or impede investigations and reports of corruption. PFC also takes action on behalf of journalists and media that suffer reprisals for covering corrupt activities. Through its daily review of 50 major newspapers in all of the Spanish-speaking countries of Latin America and a compilation of articles and editorials about corruption and free press issues, PFC has been able to encourage and contribute to cross border investigations and knowledge of corruption in the region.

PFC is a unique project in its own right. While there are many organizations that deal with issues in democratic reform and press coverage, information access, investigative journalism, and protection of sources, PFC is the only resource that brings together all those regional efforts to build independent, strong, and educated media. Many investigations of corrupt officials are too difficult to be performed by a single journalist; hence this multi-regional network helps in investigative processes by allowing journalists to combine their resources and share contacts and information.

The work of PFC is responsible for increased pressure on government officials in the region. Since the coverage of corruption within government agencies in the region has increased and become more effective, there is an increasing popular awareness of the problem and growing public support for anti-corruption measures. By keeping media reports of corruption alive, PFC assists journalists and the media in pressuring governments to implement transparency reforms and other anti-corruption legislation, and eventually in forcing legislative and judicial bodies to take action against the corrupt by making their activities more public. Increased corruption coverage has also caused a few government officials to resign, which is a rare accomplishment in Latin America. The PFC network presently includes more than 600 Latin American journalists in all Spanish-speaking Latin American countries (minus Cuba and Puerto Rico), along with several correspondents in Canada, the U.S., the Czech Republic, and Israel. For more information, please see [www.cipe.org](http://www.cipe.org).

components of transparent information: access, relevance, and quality and reliability<sup>23</sup>. Access means that information is readily available to all citizens. Relevant information is any information that bears on a particular issue or decision. Quality and reliable information is information that is accurate, up-to-date, and comprehensive.

#### Policy recommendations:

- Adopt and enforce freedom of information laws that mandate that the public has access to committee documents and government laws and regulations (draft and enacted), budgetary information (See Box 2),<sup>24</sup> and legislators' voting records so that

citizens and the media can assess public officials' records and hold them accountable.

In particular, standards should be established that specify:

- what information is to be provided (here standards need to be developed to ensure that the information provided is high quality, accurate, and comprehensive)
- what format the information is presented in (information that is presented in simple and straightforward terms is more accessible)
- which government agency is to publish which type of information, including specification of the

### Case Study: Journalist Training in the Middle East and North Africa

During the last decades several countries in the Middle East and North Africa region have implemented economic liberalization programs. Yet, because political systems in the region are largely centralized and governments are reluctant to surrender control of the economic activities, those programs have often failed to achieve significant results. In order for economic liberalization programs to have a greater impact on the democratization of societies, a constituency that understands the values of political and economic reform to society needs to be nurtured. In such environment, free media is one of the keys to success, but even with the freedom of press, the newspapers and other media sources are influenced by socialist and communist economic theories.

Realizing the importance of understanding even basic economic principles in reporting on economic issues, in 2000 CIPE and the Al Ahram Regional Press Institute in Egypt provided a forum for over 45 economic journalists from more than 10 Middle Eastern and North African countries to update their economic reporting skills and to bring them up to par with reporters in other regions. Journalists from Algeria, Egypt, Jordan, Kuwait, Lebanon, Sudan, Syria, Morocco, Oman, Saudi Arabia, and the United Arab Emirates participated in the training and educational programs.

CIPE and the Al Ahram Press Institute held a number of workshops, all of which covered topics that are of a general economic reform interest as well as region specific. The journalists discussed and learned about globalization, the details of the economic and legislative framework in a market economy, the role of institutions and business associations, transparency and flow of information, the framework of corporate governance, methods of economic reporting, and electronic journalism.

As a follow up, the economic journalists were requested to submit several articles or news spots on economic reform and the market economy. Submitted articles have appeared in many newspapers, magazines, and other media in most of the countries in the region. For more information, see [www.cipe.org](http://www.cipe.org).

content to be provided

- how information is to be disseminated (for example, through government publications, government Internet sites, public announcements, newspaper advertisements, upon request and so forth)
- within what timeframe information is to be released (for example, information about a proposed law needs to be released well in advance of any planned discussion and vote)

Outside agencies and the media can then use these standards to verify the timeliness, accuracy, and completeness of information.

#### *Establish and protect freedom of the media*

In many countries journalists are heavily influenced by political powers. A vibrant and independent media is absolutely crucial to enhance transparency by publishing and broadcasting public notices, articles, and announcements and to promote accountability by exposing corruption, the lack of transparency, violations of laws, and procedures, and government inefficiencies. More importantly, there have to be educational programs that train journalists to examine policies, laws, and regulations. In many countries journalists are often threatened when they expose corrupt government agencies or officials, and there are a number

of instances when reporters have been jailed or lost their lives because of their work. Thus, establishing mechanisms that protect journalists and secure their professional rights is essential.

#### Policy recommendations:

- Adopt and enforce laws that guarantee freedom of the media including those guaranteeing the confidentiality of sources and abolishing censorship.
- Allow private ownership of media outlets by standardizing license and permit requirements so that they are accessible in terms of time and money.
- Promote impartial news coverage within state-owned media by having independent oversight boards.
- Provide the media with regular access to information related to government activities.
- Offer journalism training so that journalists are equipped to detect poor governance, fraud, and corruption.
- Promote press responsibility so that journalists report on key social and political issues including

### Case Study: Romanian Business Associations Pioneer an Open Private-Public Sector Dialogue

The transition from a communist dictatorship to a democratic society and a market economy was painful in Romania. Old mentalities and suspicion persisted in Romanian society long after the revolution. It was hard to forget that the communist regime was fighting a permanent war against the people and, hence, individuals were and still are, to some extent, afraid to trust one another. The lack of trust and communication among key socio-economic groups and the government divided society and complicated, even as recently as 1999, the transition to democracy. Moreover, this was aggravated by the persistence of the old rules of the game and weak or poorly enforced new laws and institutions.

The Romanian business community faced a hostile commercial environment in general and a chaotic fiscal system that was suffocating the emerging private sector. Entrepreneurs quickly realized that if something was not done, democracy and its accompanying freedoms would be jeopardized. Hence, members of the business community swiftly organized into independent business associations. These associations then formed an alliance, the Strategic Alliance of Business Associations (SABA), in order to speak with one voice and have a better chance of participating in policymaking. SABA initiated an open dialogue between the Romanian business community and the president. This resulted in the creation of a non-partisan, public-private Commission for the Improvement of the Business Environment, which drafted and advocated for a modern, Western-style tax code for Romania.

After a slow and frustrating start, confidence between members of the public and private sectors was built. Public hearings to publicize and obtain feedback on the new tax code helped garner support from even the most skeptical. In the end, representatives of the business community and the government agreed on a set of fundamental principles for a modern tax code. The effectiveness and usefulness of this open dialogue for crafting responsive policies was confirmed when, much to the private sector's surprise, government representatives resumed the dialogue after the 2000 elections and used a similar model to resolve conflicts and overcome challenges related to Romania's accession to the European Union. Additionally, the government has shared the first draft of the tax code with Romanian business associations in order to obtain their input.

those relevant to women, ethnic and religious minorities, the poor, and the marginalized.

#### *Increase public participation in decision-making*

Increasing transparency through accessible, relevant, and accurate information is a necessary but not a sufficient condition to establish democratic governance. Having information helps citizens to identify what needs to be changed or improved. Citizens also need mechanisms through which they can effectuate change and hold government and government officials accountable on a regular basis. On the other hand, legislators and policymakers need mechanisms of acquiring and aggregating citizens' interests and preferences. In other words, decision-makers need comprehensive and up-to-date information about what citizens need and want on a regular basis. Without such information, even the best-intentioned law and policymakers may support laws and regulations that do not benefit the majority of citizens. Moreover, as discussed earlier, without routine input from citizens, the judicial system and policymakers are vulnerable to being captured by powerful individuals and groups who often succeed in influencing laws and policies

to suit their needs.<sup>25</sup>

In the early 1990s, the Institute for Liberty and Democracy (ILD) in Peru devised a strategy to democratize rulemaking. The strategy has the following components:

#### Policy recommendations:

- Drafts of all laws and regulations (except those relating to public security and foreign affairs) are to be made public before they are enacted into law along with a statement indicating the law or policy's objectives, an analysis of the cost and benefit for society, and an indication of which government body(ies) or representative(s) drafted it.
- Citizens and the media are then given one month to submit comments and feedback to the appropriate government agency or representative. The government should also provide opportunities for public discussion of draft laws and regulations. This can be done by holding public forums that are well publicized and held in convenient locations, as well as by setting up electronic discussions on the Internet. The media can also encourage informed

### Case Study: Reducing Opportunities for Corruption in Ecuador

In January 1997, Ecuadorians went to the streets to demand the ouster of then-President Abdala Bucaram. The reasons for their discontent with the president were the pervasiveness of corruption and the weakness of democratic institutions, which have plagued Ecuador since its democracy was restored in 1979. More than an uprising against Bucaram, these events were an expression of dissatisfaction with a political system and government that is corrupt and unresponsive to the needs of the public. Bucaram's successors, President Mahuad and President Gustavo Noboa had little success in reversing the economic slide in the country.

In fact, a combination of weak and corrupt leadership has made Ecuador a laggard in the region with respect to economic and political reform. In the late 1990s Ecuador was using over 90% of its GDP to repay debt – the largest proportion in Latin America. This debt burden represented over half of the state's general budget and almost half the country's total exports. GDP fell by 7% in 1999 and many banks collapsed. The economic conditions neared those of Haiti, the poorest country in the hemisphere and one of the poorest in the world. At the turn of the millennium, Ecuador found itself in an extreme state of emergency, with citizens questioning the viability of democracy and taking whatever means necessary to pull themselves out of their current economic freefall. The dismal future of 80% of the population who lived on less than \$1 per day has forced citizens to place all their hopes for recovery with corrupt and turbulent political parties.

The National Association of Entrepreneurs (ANDE), a voluntary private business association in Ecuador, proposed to attack the problems of corruption and legal reform in order to clear a path toward a freer and more democratic framework for their national economy. The objectives of ANDE's work were: to significantly reduce the opportunity for corruption in the legal system by identifying and eliminating commercial laws that were duplicative and conflictive; to seek the consensus of a diverse cross-section of public and private sector groups on how these laws should be revised; and to develop a final executive decree that instituted a new body of law to be presented to the president and the National Congress for approval and implementation.

ANDE's focus was not to blame past corruption on any one particular group, but rather to initiate reforms that would change the direction of business and institute clean practices. To identify the roots of corruption ANDE reviewed the country's commercial laws that concerned production, foreign trade, establishment of official prices in the private sector, technology transfer, and others. ANDE released a comprehensive study on where the laws and regulations were duplicated or how they conflicted and indicated how to eliminate duplication and correct legal inconsistencies. Its studies showed that since the Republic of Ecuador was founded 167 years ago, some 92,250 legal norms have been created of which 52,774 were in force in 1997. The sheer number of overlapping, unclear, and contradictory laws has created an environment of legal chaos and left the application and enforcement of laws to the discretion of bureaucrats.

Next, to obtain consensus from civil society groups, ANDE distributed the 350 pages of proposed legal changes to chambers of commerce, industry, agricultural entities, labor unions, ministries, and other non-governmental organizations. ANDE was able to secure the support of large, respected institutions such as the national Chamber of Commerce and representatives of these organizations. Also, prestigious members of the Ecuadorian legal community have actively and publicly supported the project. By meeting with and presenting the proposed legal changes to diverse members of the public, private sectors, and civil society, ANDE obtained valuable feedback on the draft Executive Decree, which was designed to eliminate duplicative and conflictive laws, and cultivated support for the deregulation project.

Due to lack of political will and the typically gradual pace of widespread changes in Ecuador, only 25% of the changes proposed by ANDE were actually implemented by the government, yet this is an accomplishment in its own right. In its Executive Decree, ANDE also recommended creating a seven-member judicial committee empowered to codify and reconcile Ecuador's laws, and ANDE's advocacy campaign was able to secure inclusion of the committee into Ecuador's new constitution. Currently, the Quito Chamber of Commerce is pursuing the government to implement the remaining 75% of changes proposed by ANDE.

**Box 4:****Legislative Advisory Programs: An Essential Reform Tool**

## Key Features of Successful Legislative Advisory Programs:

- **Credibility.** Each legislative advisory program should be based on sound economic analysis, and background papers should be readily available for technocrats and others to study and critique.
- **Simplicity.** Summaries should be written in clear language and stated in terms of the country's general interests as opposed to the interests of one particular group, such as business or labor.
- **Availability.** Summaries should be printed and disseminated to a broad audience. Where possible, arrangements should be made with the media in order to provide even wider coverage.
- **Policy dialogue with government officials.** In many countries, bureaucracies represent formidable obstacles to reform. In their attempt to affect public policy, business organizations should try to influence government personnel, as well as legislators.

Sources: Wallack (1991) and Sullivan (1999).

discussions by publishing articles including commentaries and hosting talk shows. Think tanks can also enhance the quality of discussions by publishing and widely distributing their own cost/benefit analyses of proposed laws and regulations.

- Citizens should be given the right to participate in public hearings and government advisory committees when laws and policies are being formulated.
- Citizens should have the right to challenge arbitrary or unresponsive laws and regulations quickly through well-defined procedures. Citizens may consider requests to be resolved in their favor if the government fails to respond within the designated timeframe.
- Citizens should have the right to initiate referendums either on proposed laws and regulations or new ones. The requirements for referendums should be fair, simple, transparent, and accessible so that all

citizens can exercise this option.

For more policy recommendations on how to increase citizen participation in policymaking, please see the Sana'a Declaration (Appendix A).

*Reduce the degree of government officials' discretion*

Administration and enforcement systems that allow government officials too much discretionary authority are breeding grounds for corruption and poor governance. In these circumstances, government officials can use their authority to solicit bribes and kick-backs. World Bank expert Daniel Kaufmann (1999:94) has provided an illustrative list of the key areas that involve governmental discretionary powers and should be targets for reform.

- Issuing licenses, permits, quantitative import restrictions (quotas), passports, customs and border-crossing documentation, and banking licenses.
- Implementing price controls.
- Blocking new firms and investors from entry to markets and providing monopoly power.
- Awarding public procurement contracts.
- Granting subsidies, soft credits, tax exemptions, and inflated pensions and allowing tax evasion.
- Imposing foreign-exchange controls resulting in multiple exchange rates, the over-invoicing of imports, and the flight of capital.
- Allocating real estate, grain storage facilities, and telecommunications and power infrastructure.
- Selectively enforcing socially desirable regulations such as those that apply to public health and the environment.
- Maintaining obscure or secret budgetary accounts, or otherwise facilitating "leakages" from the budget to private accounts.

Policy recommendations:

- Laws and regulations should be clarified so that rights are clearly defined, rules are clearly specified, and administrative and enforcement procedures are straightforward so that the possibility of multiple interpretations and applications of laws and regulations is minimized.
- Duplicative, superfluous, complex, and conflicting laws and regulations should be rescinded and steps necessary to comply with the law should be streamlined.
- Clear guidelines should be issued, requiring disclosure and set standards by which government

### Case Study: Institute for Liberty and Democracy: Administrative Simplification in Peru

One of the biggest problems in Peru in the late 1980s was that queues and excessive paperwork and bureaucratic procedures cost most Peruvians a lot of lost time and resulted in unnecessary expenses and other constraints on economic activity. The Institute for Liberty and Democracy (ILD) created a draft of the law and designed an administrative strategy to streamline bureaucratic procedures and facilitate institutional reform. This draft legislation was based on public hearings and debates throughout the country, which featured legal specialists and congressmen. Such events, which went on for two years, not only added substance to ILD's proposal, but also created an enormous wave of support for it.

In June 1989, ILD's draft was unanimously approved in Congress by all political parties and, with no major modifications, became the Law for Administrative Simplification. Government now had the mandate and means needed to decrease or eliminate unnecessary red tape, streamline public administration, and substantially reduce transaction costs. The new law rested on four pillars: 1) substituting most *ex ante* requirements that create legal bottlenecks with *ex post* controls; 2) keeping the costs of operating legally below those of operating illegally; 3) decentralizing decision-making procedures; 4) promoting participation to control the application of all decisions.

Shortly after the law was enacted, President Alan García Pérez called upon ILD to manage the implementation of the simplification process. ILD proceeded to design a unique mechanism called "The Administrative Simplification Tribunal" to gather and evaluate proposals from citizens for deregulation and to check up on how various bureaucracies were responding to the dictates of the law. To facilitate public participation, bright yellow boxes were placed in ILD's headquarters and in several government offices as well as at all radio, television, and newspaper outlets to make it as convenient as possible for people to voice their grievances. The media was encouraged to review the grievances it received, and when media agents saw an astonishing or outrageous story, they covered it, creating the kind of public pressure that was impossible for politicians to ignore. The complaints were dealt with in a publicly televised tribunal managed by ILD and presided over by the President of the Republic every second Saturday morning and the televised proceedings quickly racked up high ratings.

Over the year the Tribunal was in operation – with the president, by law, in attendance – more than 200 bureaucratic knots were untied. The time previously required to fulfill hundreds of different kinds of official procedures, including obtaining a passport, applying to university, and getting a marriage license, was cut across the board by at least 75 percent. To get a marriage license, which used to take 720 hours of bureaucratic hassles, was reduced to 120 hours – thus helping women secure their rights as marriage partners. The number of documents required to apply to university was reduced from nine to two. At the end of President García's term in July 1990, 79 percent of the population (and 84 percent of the poorest among them) rated the Law of Administrative Simplification as the best law enacted during the 1985-1990 legislative period.

After the change of government in July 1990, ILD presented President Fujimori with a package containing 39 draft laws for legal reform derived from ILD's analysis of the grievances received by the Tribunal and based on the principles of administrative simplification. The executive branch eventually enacted 15 of these, including the Unified Business Registry for incorporating small businesses, the liberalization of the land real estate markets, and a pardon for prisoners whose cases had never come to trial.

The Fujimori Government used the instruments contained in the Law of Administrative Simplification to carry out most of the structural adjustment reforms that were required for Peru to become a player in the global economy.

agencies may award subsidies, quotas, and exemptions from fines.

#### *Reduce legal and regulatory burdens*

Unresponsive laws and regulations exist in the form of legal, regulatory, and administrative requirements that are expensive and time consuming. Examples include the number of steps and costs it takes to establish a new firm. A recent study of 85 countries revealed that on average this involves 10.17 steps and 63.05 business days and at worst up to 20

procedures and 82 business days in Bolivia.<sup>26</sup> In such cases the result is government failing to provide services and permits in a timely and cost-effective manner. Thus, obtaining licenses and permits becomes a breeding ground for corruption and misused funds. The World Bank study, "Doing Business in 2004", reinforces the direct link between number of regulations and corruption – the report highlights the fact that less corrupt OECD countries have less entry regulations than the developing countries. Entry costs in Africa, for example, are almost 20 times those in OECD countries, and to register a business in Latin America and Caribbean on average takes

2.5 times longer than in high-income OECD countries.

ILD in Peru devised a strategy to eliminate excessive bureaucratic procedures and paperwork and long queues and waiting periods. Throughout the country they held public hearings and debates, which featured legal specialists and congressional representatives on administrative bottlenecks. ILD used the results to draft a law to eliminate unnecessary red tape, streamline public administration, and substantially reduce transaction costs.

#### Policy recommendations:

- Substitute most *ex ante* requirements that create legal bottlenecks with *ex post* controls keeping the costs of operating legally below those of operating illegally.
- Decentralize decision-making procedures.
- Promote user participation to control the application of all decisions.

#### *Reform Government Agencies*

Government agencies that are bureaucratic and complex become a breeding ground for corruption. Lack of internal control and audit allows government officials to use their powers to provide preferential treatment, accept bribes, and deny or delay services. Complex operating procedures only encourage the public to participate in corruption and go around the laws. If establishing a business and collecting all the necessary paperwork takes years because of the number of procedures, many would rather provide a payment to a government official to receive a permit or a license, if such opportunity exists. This gives an unfair advantage to those who are engaging in corrupt behavior. Thus, government agencies that are excessively bureaucratic and inefficient need to be reformed.<sup>27</sup> This can be accomplished best by implementing a series of internal and external controls.<sup>28</sup>

#### Policy recommendations:

- Streamline and simplify agencies' internal operating procedures.
- Establish and enforce codes of conduct.
- Regularly evaluate agencies' performance according to clear, well-defined standards.
- Regularly conduct independent audits of budgets (in this regard, establishing independent auditing agencies similar to the U.S. General Accounting Office can be very useful).
- Regularly audit public officials' assets and financial interests.
- Establish clear and transparent rules on conflict of interest for the public sector. In many countries,

it is still possible for government officials (or their children, spouses, or lawyers) to hold additional paying positions in private or state firms, or to accept consulting fees from private firms. At a minimum, such relationships should be disclosed and the officials should be barred from making decisions affecting those firms. As a corollary, efforts should be made to limit officials' ability to leave office and move into high-paying positions in firms doing business with the ministries or agencies that they served (Sullivan 2000).

- Provide routine opportunities for citizens and employees to voice their concerns. Using diagnostic surveys or scorecards is extremely helpful in this regard.
- Include citizens and nongovernmental organizations on agency oversight committees.
- Implement measures to improve poorly performing agencies promptly and comprehensively. Again, establishing timeframes and evaluative standards to gauge remedial action is important.

#### *Strengthen Administrative and Enforcement Capacity of Government Agencies*

Reforming government agencies and introducing new guidelines and technology is often a challenge when civil servants lack sufficient education and when they remain in the agencies due to their personal relationships rather than professional qualifications. Also, bureaucrats are sometimes not able to provide proper services because they themselves are not up-to-date with the changes in regulations or they lack sufficient financial or other resources to do so.

#### Policy recommendations:

- Cultivate a staff of well-qualified civil servants by hiring and promoting staff based on verifiable professional standards (through standardized tests),<sup>29</sup> offering civil servants vocational training based on the latest technology, paying adequate salaries to attract well-qualified professionals and to deter bribe taking,<sup>30</sup> and offering tenure based on performance not on the election cycle.
- Provide sufficient financial and technical resources to administer laws expeditiously.<sup>31</sup>
- Experiment with new ways to reduce the costs and improve the effectiveness of administering and enforcing laws and regulations and to encourage market efficiency (North 1992).

#### *Strengthen legislative oversight of the executive branch*

Besides representing citizens' interests and making

### Case Study: Reforming Government Agencies: Serbia: Corruption in Customs

2001 marked a new step in the political and economic development of Serbia and Montenegro – President Slobodan Milosevic was ousted on March 31, 2001, and at the same time some other key collaborators of his were arrested. These political changes in Serbia-Montenegro brought about a new political agenda on which corruption in the government agencies was highlighted as a critical item for reform.

At the time of Milosevic's ousting, institutional corruption was widespread throughout Serbia and Montenegro. According to the surveys, one of the most corrupted civil services in the country was the Customs Administration, where, according to some estimates, over 50% of the employees were in some way involved in corrupt activities. Effective customs administration is one of the keys to a country's successful development since it directly deals with the issues of foreign trade, smuggling of goods, tax payments, and others. And while the new administration was willing to reform the agency, it faced a number of challenges trying to weed out corruption.

The Belgrade Center for Liberal Democratic Studies (CLDS), an independent think tank founded to promote democracy, individual liberty, economic development, and the rule of law in Yugoslavia, initiated research on the root causes of institutional corruption within the Customs Administration and suggested anti-corruption measures. Its first step was to make the existence and magnitude of corruption in the Customs public, which CLDS did through the surveys distributed to the private sector. It was an important accomplishment in its own right, since people started to publicly discuss not only the problem itself, but also the negative effects of the corrupt Customs Administration on economic development and what could and should be done.

By carefully examining the structure of the Customs Administration and its operations, CLDS came up with a list of the major root causes of corrupt behavior within the customs. Those causes included:

- Low wages of customs officials
- Corrupt organization (newcomers in the administration become corrupt because the culture of corruption is already established in the organization)
- Weak or lack of regulations and/or enforcement mechanisms that punish and hold government officials accountable for corrupt behavior
- Insufficient resources (when the number of customs officials is limited, the services can no longer be provided in a timely manner, therefore some will tend to bribe officials to receive a service)
- National protectionist policies or otherwise restrictive foreign trade policy
- Complex customs procedures
- High and diverse customs duties and numerous exemptions

CLDS not only studied the negative effects of the corrupt behavior on the economic and political development in the country, but it also proposed policy recommendations and worked closely with government officials to implement them. CLDS's action plan focused on:

- Reform of the existing Customs Administration rules, regulations, and procedures
- Reform of the wage structure and incentives scale for the Customs Administration officials
- Introduction of a new monitoring system for transparency of all the Customs Administration procedures
- Introduction of a Code of Ethical Standards for Customs Administration officials
- Introduction of severe punishments for corrupt staff within the Customs Administration and recommendations for legislative reform that will enable the punishment scheme to be effectively enforced
- Formulating and providing guidelines for a public relations campaign against corruption in the Customs Administration and providing incentives to all the Customs Administration "customers" to increase anti-corruption pressure on the Administration.

At the conclusion of all of the research and analysis, CLDS drafted a full report based on the data. CLDS used the opportunity to highlight the difficulty of curing the problem of corruption in the Customs Administration and offered recommendations based on the surveys, interviews, and research analysis, which can be used to lessen the incidents of corruption, bribery, and favoritism. The report was produced in both Serbian and English and was distributed to the public, government officials, media, and libraries throughout Serbia and internationally, as well as on the organization's website ([www.clds.org.yu](http://www.clds.org.yu)) free of charge. The report secured the commitment of Vladan Begovic, the head of the Customs Administration, to spearhead reforms on national television.

For the first time in the history of Serbia, the evaluation of corrupt practices within the Customs Administration was addressed. This initiative by CLDS examined the problem of corruption in a very specific subset of the Serbian government and came away with information that was at the same time obvious, yet incredibly revealing. As a result of CLDS' efforts, both the Customs Administration and the public in general gained an understanding of not only the causes, but also the consequences of corruption.

**Box 5:**  
**How Businesses Can Affect Public Policy by Developing a National Business Agenda**

A national business agenda is vital tool for the business community to encourage investment and stimulate business activity and economic growth. Building an agenda mobilizes the business community to use their skills to affect public policy by setting legislative and regulatory priorities and communicating them to policymakers.

National business agendas identify laws and regulations that hinder business activity and offer concrete recommendations and reforms to remove these barriers and improve the business climate. Developing a national business agenda also educates the private sector on public policies that affect them and allows it to present the concerns of the business community to government officials in a unified voice, increasing the likelihood that their agenda will be adopted. National business agendas have proven to be an effective tool for removing barriers to entrepreneurship in countries across the globe. CIPE has sponsored national business agendas initiatives in Argentina, Egypt, Haiti, Malawi, Nigeria, and Ukraine.

For more information, please see: [www.cipe.org](http://www.cipe.org)

laws and policies, the legislature plays an important role in governance by overseeing policy implementation by the executive branch. This is accomplished by questioning senior government officials, reviewing or confirming executive appointments, impeaching or dismissing officials, forming specialized committees that monitor policy implementation in specific areas, and holding public committee hearings.

Policy recommendations:

- Legislative oversight committees should be formed to monitor policy implementation by the executive branch in as many policy arenas as necessary and feasible, but particularly in the financial and budgetary arenas.
- Provide committees with sufficient human, financial, and technical resources. The capacity

to conduct thorough research is especially important. When resources are scarce, the oversight committee should enlist the help of civil society organizations to provide research and expertise about the likely effects of public policies and policy alternatives.

*Reform the judiciary*

The judiciary should be reformed and strengthened so that it enforces laws consistently, efficiently, and fairly, thereby maintaining the rule of law and providing citizens with a means of redressing grievances.<sup>32</sup> An extremely useful tool in designing a judicial reform initiative is the Judicial Reform Index (JRI) developed by the American Bar Association. The JRI uses thirty factors in the categories of quality, education, and diversity; judicial powers; financial resources; structural safeguards; accountability and transparency; and efficiency to assess a country's judicial system and to provide a road map for reform efforts. The JRI is available at: [www.abanet.org/ceeli](http://www.abanet.org/ceeli).

*Provide alternative dispute resolution mechanisms*

In addition to reforming the judiciary, alternative means to resolve disputes out of court through arbitration is one way to lighten the courts' load and expeditiously redress grievances. In countries where commerce is regulated by civil codes not bound by precedent (including many in Latin America), laws and regulations can be overturned by decree, greatly weakening stability.<sup>33</sup> Often, greater horizontal accountability or checks and balances have to be instituted to minimize frequent, radical changes to the legal and regulatory framework and general abuses of governmental power (Schedler, Diamond, and Plattner 1999).

*Establish ombudsmen*

A useful means of obtaining regular feedback from citizens is to establish an ombudsman. An ombudsman is a public official who investigates activities of government agencies that may infringe on the rights of individuals. He/she is available to record citizens' grievances and to take action by proposing remedial action, including legal and regulatory changes. A key advantage of an ombudsman is that the service, unlike most legal advice, is free of charge and, hence, accessible to citizens of modest means.

Policy recommendation:

### Case Study: Romania: Open Doors Campaign

The Open Doors Campaign is an initiative led by Romanian business associations and Chambers of Commerce that promotes the passage of specific laws to ensure public input in the process of government, freedom of information, fiscal accountability, and transparency. These laws include but are not limited to the establishment of public hearings and testimony, access to public information, establishment of fiscal impact statements to assess the fiscal and social impacts of legislation on the business community, and the limiting of the government's ability to pass laws by emergency ordinance versus Parliamentary procedure.

The Open Doors Campaign provides the foundation on which other business initiatives are built. As part of the Open Doors Campaign, several business coalitions have been formed, which call on the Romanian government to address issues within some sectors of the economy. The Tourism for Today and Tomorrow (T-3) Coalition has developed a legislative agenda to promote the interests of the tourism sector and to offer solutions as a partner with the Romanian government to the challenges facing the sector. The Tech 21 Coalition, which consists of business associations that serve the information technology sector, has developed a legislative agenda to work as a partner with the Romanian government to increase the pace of investment in information technology and the creation of good jobs for the Romanian people. And finally, ProGlobe, a coalition of the Romanian manufacturers' associations, was formed to promote competitive Products and Processes for the Global Economy – an initiative to address the main issues hindering increased competitiveness of the sector: legal instability, bureaucracy, financial blockage, and slow privatization.

As a result of the Open Doors Campaign, over 200 representatives of business associations, government, and NGOs received technical assistance training in the design and implementation of advocacy campaigns. Many of the associations involved in this training have since launched their own advocacy campaigns. Also, a database of over 800 grassroots supporters was created, and this network is utilized by the coalitions to communicate their messages to government in a fast, efficient, and consistent manner.

Through the Open Doors Campaign, five business associations in western Romania created the Advocacy Academy Association (AAA). The AAA serves as an information source for business associations and promotes a dialogue between the private sector and government on key issues. The AAA planned and conducted the first ever public hearing held in Romania and has conducted two additional public hearings on specific issues. It has been integral in serving as a liaison between the government and the private sector on issues such as the Labor Code and the Regulation of Direct Advocacy Activities. In addition, twenty business association leaders graduated from the Academy's Advocacy Training Program. These leaders now serve as experts to assist business associations in planning and conducting advocacy campaigns. (For more on the open doors campaign please visit [www.opendoorscampaign.org](http://www.opendoorscampaign.org))

- Establish ombudsman's offices throughout the country so that all citizens can take advantage of their services.

### *Combat Corruption*

#### Policy recommendations:

- Specify and streamline legal and regulatory codes.
- Clarify laws on conflicts of interest.
- Adopt and implement Transparency International's Government Procurement Code.
- Adopt and adhere to the OECD's Anti-Bribery Convention (Sullivan 2000).<sup>34</sup>
- Establish independent anti-corruption commissions.
- Institute sound corporate governance systems.

### *Promote well-designed decentralization of government functions*

The decentralization of government functions is often implemented in order to improve governance by bringing government closer to the people. Because people tend to be more involved in local politics, follow local news, and vote in local elections, decentralization can harness these tendencies and create participatory and responsive local government. However, the mere process of decentralization does not automatically translate into better governance. In fact, ill-designed decentralization strategies can increase levels of corruption as local government officials and elites may easily establish cozy, rent-seeking relationships. This may partly explain why cross-country regressions on the link between decentralization and corruption fail to produce consistent results (Azfar 2002:12). In order for decentralization to enhance democratic governance, key institutions of accountability at the local level need to be

**Case Study: Democratic Governance and Institutional Reform in Georgia**

On July 23, 1999 the Parliament of Georgia adopted the General Administrative Code, the aim of which was “to ensure respect by administrative bodies for human rights and freedoms, public interests, and rule of law.” This Code included extensive provisions dealing with freedom of information and the transparency of public agency meetings, and its purpose was to enforce accountability throughout government institutions.

The Partnership for Social Initiative (PSI), CIPE’s local partner, has taken a leading role in monitoring the proper enforcement of the Code. PSI began by conducting a nationwide analysis of public perceptions and understanding of the provisions of the Code. It was discovered that the government had done little to make the public aware of the Code and its provisions and 24 percent of business owners had no knowledge of the Code at all. PSI’s analysis also made clear that government agencies were not applying a number of the Code’s provisions in the way the law stipulated. This was partly due to lack of financing of administrative bodies, insufficient internal management, and the perception of public officials that they would never be held responsible for ignoring the legislation. Also, PSI discovered that while the executive branch was more or less aware of its responsibilities under the Code, this was not the case with the regulatory agencies, which are by law independent of the political process and thus less inclined to abide by the rule of law.

PSI also surveyed businesses and civil society groups to identify concrete experiences and to outline specific issues when attempting to use the Code. In addition to distributing their questionnaire within the business community, PSI advertised their survey in newspapers, association newsletters, and on state television, soliciting responses from civil society at large.

The most blatant and widespread violations of the Code were identified based on the number of organizations affected and the importance to the country’s economy and the development of a free market. The goal was to determine the extent to which government agencies complied with the Code and any follow-up court actions or actions by oversight agencies. In 20 percent of cases, government agencies failed to respond to information requests and only responded when PSI sent them an “administrative warning.” In one case, PSI filed a lawsuit against one agency, the Ministry of Finance, for its refusal to respond, demonstrating that the Code is enforceable and requests for public information can be satisfied.

PSI has shown that appropriate implementation of the Administrative Code is possible through the efforts of interested citizens and informed courts. PSI built a coalition of 70 stakeholders and members of businesses and non-governmental organizations that expressed interest in the Administrative Code and were in a position to contribute their efforts to monitoring and advocacy activities.

Through evaluation of the enforcement of the Administrative Code PSI uncovered a larger problem – in Georgia, civil society groups and business associations are failing to take advantage of advocacy opportunities with policymakers. Public officials, on the other hand, do not feel a need to include the public in the decision-making and legislative process. In this specific case, they argued that the Administrative Code did not provide for such an obligation. The reasons for such attitudes on the part of the public officials are simple: some agencies believe that allowing civil society organizations to participate in decision-making will interfere with state interests, and others lack awareness of the organizations that share their area interests.

To address the advocacy gap, PSI developed a model for accrediting business associations. The goal of this activity was to provide a list of associations and other civil society organizations with specific issue interests or expertise that agencies can contact for input on proposed policy changes and reforms. PSI has established a pilot program with the Georgia National Center of Intellectual Property in which this agency has agreed to consult with the private organizations on its list. This pilot program served as a model for developing similar accreditation processes at other government agencies.

As a result of PSI activities, the participation of civil society and business associations in the development of public policy reforms has dramatically increased. These fundamental cultural changes in the relationship between the public and private sector were only possible because of the Administrative Code and PSI’s continued advocacy for better implementation. Transparency and decision-making provisions of the Code played a key role in convincing and forcing government agencies to give civil society groups a role in policy-making.

in place.

Policy recommendations:

- Clearly stipulate the responsibilities of local government.
- Vest local governments with sufficient power and authority to execute their mandate autonomously and effectively from the central government (i.e., decentralization should entail a true devolution of power rather than merely a deconcentration of centralized power).
- Provide local governments with adequate financial, human and technical resources (see the sections on reforming government agencies and strengthening the administrative and enforcement capacities of government agencies above for more detailed recommendations).
- Develop and implement sound accounting systems based on budgetary transparency.
- Cultivate an independent, investigative local media.
- Encourage the development of civil society organizations that monitor local government activity.
- Establish feedback mechanisms through which citizens can regularly comment on government performance. (e.g., the holding of regular town hall meetings and the use of local government scorecards or surveys).

*Promote democratic governance within public sector companies*

Another significant challenge facing developing, emerging, and transitional economies is instituting sound governance within public enterprises. In many of these economies, public sector companies contribute more to the nation's gross national product, employment, income, and capital use than private sector firms. Moreover, public sector companies often shape public policies. As a result, instituting sound corporate governance within public sector companies is essential to economic development, growth, and reform.

This is true even for countries intent on or in the midst of privatization. To begin with, public companies need to be corporatized before they can be privatized. The corporatization process can, at times, be lengthy. Even after corporatization, it takes time before the new company benefits from active owners and skilled managers. In the meantime, good management of the company will ensure that the company's resources are managed efficiently and fairly, thereby increasing the company's productivity and

value.

There are other scenarios calling for governance practices within the public sector. Public companies, for example, may gain control of previously privately-owned firms through joint ventures. In addition, some public economic entities may never be privatized because they are considered vital to national security or politically sensitive. Obviously, these companies would benefit from sound corporate governance.<sup>36</sup>

Policy recommendations:

- Adopt and implement the recommendations in the First Principles of Corporate Governance for Public Enterprises in India available online at: <http://www.corpgov.net/forums/commentary/reddy.html>.
- The Private Sector Corporate Governance Trust in Kenya has also been active in promoting corporate governance within state-owned companies. For more information, please see: [www.corporategovernance.co.ke](http://www.corporategovernance.co.ke).

*Encourage the establishment of civil society organizations*

Civil society organizations have an important intermediating role between citizens and the government. They help aggregate and represent citizens' interests, monitor government practices, and hold government accountable by providing the public and legislators with information and expertise about the effects of specific public policies and policy alternatives.

Policy recommendations:

- Remove legal barriers that prevent the establishment of civil society organizations and make the procedures simple, straightforward, and inexpensive.
- Offer civil society organizations tax-exempt status.

*Involve Business Associations and Civil Society Organizations*

Involving think tanks, business associations, and other nongovernmental organizations (NGOs) in the governance process is essential to building public understanding of the costs of undemocratic governance and the demand for change.

Policy recommendation:

- Develop programs that involve business associations and civil society organizations in the reform process. Those programs should contain an explicit public education program aimed at creating national norms or values that emphasize that the lack of democratic governance is unacceptable and informing people what services they are entitled to as tax payers and citizens (Sullivan 2000). NGOs can then mount efforts to promote reform and hold government accountable.
- Strengthen advocacy skills of business associations and civil society organizations so that they can become effective reform advocates.<sup>37</sup>

## Conclusion

The lackluster performance of many emerging democracies and economies and the anti-reform backlash occurring in many countries and regions have exposed the serious consequences of omitting democratic governance from the reform agenda. While reform efforts of the past several decades - notably the policies of the Washington Consensus and initiatives to promote free and fair elections - have succeeded in increasing political participation and in attaining macro-economic stabilization, they have failed to promote widespread political and economic freedom and empowerment. As a result, many citizens continue to suffer from corruption, unemployment, poverty, low economic growth rates, and a lack of essential government goods and services such as justice.

The message is clear. The reform efforts to date are the necessary beginning – not the end – of the reform agenda. If citizens are to enjoy the fruits of democracy and market-based economies on a daily basis, then they need to be given the appropriate mechanisms through which they can participate in decision making and hold government accountable on a daily basis. In other words, reform initiatives need to focus on fostering democratic governance. Evidence from the past several decades has indicated that transitions that are not crafted and sustained by the will of the people are doomed either to fail or to languish in a political gray zone rife with democratic deficits<sup>38</sup> and poor economic performance.<sup>39</sup> Either outcome blackens the reputation of democratic, market-based systems and jeopardizes current and future transitions.

Yet it is equally important to recognize that instituting democratic governance is a long-term process and involves measures that could slow reforms. Creating institutions of accountability and allowing them to function is time-consuming. On the bright side, they allow for creative, tailor-made, and sustainable solutions. The policy recommendations presented in this report should be

considered as tools that citizens and governments can use and adapt to create their own institutions of accountability that foster the type of democratic governance best suited to their needs.

Recent cross-country studies have confirmed that countries that have taken on the challenge of establishing democratic governance have been rewarded in terms of superior developmental outcomes. This includes better respect for civil and political liberties, human rights and property rights, higher growth and employment rates, better quality public goods and services, and more political stability. Hence, it is in everyone's interest to ensure that future reform efforts open the black box of governance.

## (Footnotes)

<sup>1</sup> United Nations Human Development Report (UNDP) 2002

<sup>2</sup> Ibid.

<sup>3</sup> This survey was conducted in over 60 different countries, where 57,000 adults were interviewed.

<sup>4</sup> In other words, democratic governance helps to overcome the principal-agent problem between voters and government officials/civil servants.

<sup>5</sup> This is particularly true, for example, when constitutions are difficult to change and high court judges enjoy lifetime appointments. For a comprehensive discussion on horizontal accountability, see Schedler, Diamond and Plattner (1999).

<sup>6</sup> In countries where the judiciary is partial and inefficient, using the court system to obtain redress is virtually useless.

<sup>7</sup> A widespread finding from a study of 16 developing countries indicates legislators are often not held accountable thereby weakening their incentive to enact responsive laws and regulations (Court and Hyden 2003:310).

<sup>8</sup> See Kuchta-Helbling (2000) for a more detailed discussion of the impacts of barriers to participation on the informal sector and political and economic development.

<sup>9</sup> Moreover, a recent survey indicates that citizens' support for democracy is more robust, and democracy is more stable where justice and accountability, civil liberties and restraint of power are greater (see Diamond 1999).

<sup>10</sup> See Schedler, Diamond and Plattner (1999).

<sup>11</sup> A recent study revealed that in many countries budgetary transparency was weakened by a lack of citizen participation in determining and overseeing expenditures (see Guerrero and Hofbauer 2003: 275)

<sup>12</sup> see Knack, Kugler and Manning 2003: 307

<sup>13</sup> Country-level studies show that the less secure property rights are correlated with lower aggregate investment levels and slower economic growth rates. In fact, entrepreneurs with the least secure property rights invested almost 40% less of their profits than those with more secure property rights (see Johnson, McMillan and Woodruff, 2002).

<sup>14</sup> Kaufmann 2003:18. Other studies that have found a positive correlation between sound governance and growth and development

include La Porta et al. (1999); Acemoglu, Johnson and Robinson (2001); Engleman and Sokoloff (2002); Mauro (1995); Easterly and Levine (2002); and Rodrick et al. (2002).

<sup>15</sup> See Acemoglu, Johnson, and Robinson (2001)

<sup>16</sup> See Rivera-Batiz 2002:244

<sup>17</sup> For more information, please see the World Development Report 2002, chapter 7.

<sup>18</sup> Kaufmann (2003:16)

<sup>19</sup> Kaufmann, Kraay, and Zoido-Lobaton (1999)

<sup>20</sup> Besley and Burgess (2001)

<sup>21</sup> see Kaufmann 2003:24

<sup>22</sup> Countries which suffer from an extreme lack of democratic governance and control over their territory are often referred to as failed states. See Rice (2003) for a discussion of failed states.

<sup>23</sup> Vishwanath and Kaufmann, 1999:3

<sup>24</sup> The International Monetary Fund's "Code of Good Practices on Transparency in Monetary and Financial Policies" is also a useful tool in promoting good governance in the financial arena. The Code is available online at: [www.imf.org](http://www.imf.org).

<sup>25</sup> Kaufmann (2003) found that when a state is captured by elites or special interests, that mechanisms of voice and feedback are crucial to foster accountability.

<sup>26</sup> See Djankov et al. (2000). Please note that this study considers only the official time required to set up a business and does not include bureaucratic delays that may lengthen the process.

<sup>27</sup> Cross country surveys have found that civil servants are perceived to be widely corrupt. In some countries, this encourages citizens to be corrupt as well. Please see Lagos (2003) and Dimov (2003).

<sup>28</sup> Kaufmann, Mehrez and Gurgur (2002) found that external, voice-related mechanisms of accountability improved the quality of public services and lowered corruption levels in Bolivia more than traditional, internal, public sector, management reforms.

<sup>29</sup> Rauch and Evans (2000) found that when recruitment and promotions are not merit-based, the level of corruption increases and the quality of bureaucracy decreases.

<sup>30</sup> It is important to note that merely increasing wages is often not sufficient to improve the performance of civil servants or to reduce corruption. A recent study by Di Tella and Schargrodsky (2003) found that higher wages only reduce corruption levels when they are coupled with audit controls.

<sup>31</sup> Using cutting-edge technology can greatly reduce operating costs in the long-term.

<sup>32</sup> For a comprehensive overview of the challenges involved in creating an impartial and independent judiciary, see Domingo (1999).

<sup>33</sup> Moreover, governments in civil law countries exhibit a greater tendency to intervene in the economy and to erect high barriers to entry for new firms (see Djankov et al. 2000).

<sup>34</sup> For a whole host of articles and links about reducing corruption, please see CIPE's Web site: [www.cipe.org](http://www.cipe.org). See also the Final Report on the Washington Conference on Corruption, "Fighting Corruption in Developing Countries and Emerging Economies: the role of the private sector," sponsored by USAID, PriceWaterhouseCoopers, and CIPE,

February 1999.

<sup>35</sup> Many of these points are taken from Azfar (2002:12-13). For more detailed information about the conditions for effective decentralized governance, please see Azfar, Kähkönen and Meagher (2001).

<sup>36</sup> For more information about the importance of corporate governance in public enterprises and for a copy of "The First Principles of Corporate Governance for Public Enterprises in India: Yaga Principles for PEs," October 2001, email: [yaga@hd1.vsnl.net.in](mailto:yaga@hd1.vsnl.net.in). See also the Private Sector Corporate Governance Trust Web site: [www.corporategovernance.co.ke](http://www.corporategovernance.co.ke).

<sup>37</sup> For a useful advocacy guidebook, please see *How to Advocate Effectively: A Guidebook for Business Associations*, CIPE, 2003.

<sup>38</sup> See Carothers (2002).

<sup>39</sup> See Kaufmann (2003).

## REFERENCES

- Acemoglu, D., S. Johnson and J.A. Robinson 2001: "The Colonial Origins of Comparative Development: An Empirical Investigation," *American Economic Review* 91 (5): 1369-1401.
- Alvarez, M., J.A. Cheibub, F. Limongi, and A. Przeworski 1996: Classifying Political Systems. *Studies in Comparative International Development*, 31, 2, 3-36.
- American Bar Association: Judicial Reform Index (JRI) available at: [www.abanet.org/ceeli](http://www.abanet.org/ceeli).
- Azfar, Omar 2002: The NIE Approach to Economic Development: An Analytic Primer. Prepared for a Forum Series on the Role of Institutions in Promoting Economic Growth sponsored by the U.S. Agency for International Development, February.
- Azfar, Omar, Satu Kähkönen, and Patrick Meagher 2001: "Conditions for Effective Decentralized Governance: A Synthesis of Research Findings," *Center for Institutional Reform and the Informal Sector (IRIS) Working Paper No. 256*, March.
- Besley Timothy and Robin Burgess 2001: "Political Agency, Government Responsiveness and the Role of the Media." *European Economic Review* 45(4-6):629-40.
- Bradhan Pranab and Dilip Mookherjee 1998: "Expenditure decentralization in developing countries." *The American Economic Review*.
- Carothers, Thomas 2002: "The End of the Transition Paradigm," *The Journal of Democracy*, January, Volume 13, 1.
- The Center for International Private Enterprise 2002: *How to Advocate Effectively: A Guidebook for Business Associations*. Washington, D.C.: The Center for International Private Enterprise.
- Collier, David 1997: Democracy and Dichotomies: is concept formation inherently based on qualitatively reasoning? Paper presented for the annual meeting of the American Political Science Association, Washington, D.C.
- Collier, David and Steven Levitsky 1997: Democracy with Adjectives: Conceptual Innovation in Comparative Research. *World Politics*, 49, 430-451.
- Court, Julius and Goran Hyden 2003: "World Governance Survey: a new approach to assessing governance." In Robin Hodess with Tania Inowlocki and Toby Wolfe (eds.), *Global Corruption Report 2003*. London: Profile Books and Transparency International.
- Dahl, Robert A. 1956: *A Preface to Democratic Theory*. University of Chicago Press.
- \_\_\_\_\_ 1969: The Concept of Power. In Bell, R., Edwards, D.V., and Wagner, R.H., eds, *Political Power: A Reader in Theory and Research*. New York: The Free Press.
- \_\_\_\_\_ 1971: *Polyarchy: participation and opposition*. New Haven: Yale University Press.
- De Soto, Hernando 1989: *The Other Path: the invisible revolution in the third world*. New York: Harper and Row (edition of August 2002.)
- \_\_\_\_\_ 2000: *The Mystery of Capital*, Basic Books.
- Diamond, Larry 1999: *Developing Democracy: Towards Consolidation*. Baltimore: The Johns Hopkins University Press.
- \_\_\_\_\_ 2002: "Promoting Democratic Governance." In *Foreign Aid in the National Interest: Promoting Freedom, Security, and Opportunity*. Washington, D.C.: the U.S. Agency for International Development, pp. 33-53.
- Dimov, Martin 2003: "Corruption in Balkan Countries." In Robin Hodess with Tania Inowlocki and Toby Wolfe (eds.), *Global Corruption Report 2003*. London: Profile Books and Transparency International.
- Di Tella, Rafael and Ernesto Schargrotsky 2003: "Controlling Corruption through High Wages." In Robin Hodess with Tania Inowlocki and Toby Wolfe (eds.), *Global Corruption Report 2003*. London: Profile Books and Transparency International.
- Djankov, Simeon, Rafael La Porta, Florencio Lopez-de-Silanes, and Andrei Shleifer 2000: "The Regulation of Entry." *Harvard Institute of Economic Research, Discussion Paper Number 1904*, September. Cambridge, MA: Harvard University.
- Domingo, Pilar 1999: "Judicial Independence and Judicial Reform in Latin America." In Andreas Schedler et al., eds., *The Self-Restraining State: Power and Accountability in New Democracies*. Boulder, Co.: Lynne Rienner, 151-175.
- Easterly, W and R. Levine 2002: "Tropics, Germs and Crops: How Endowments Influence Economic Development," *NBER Working Paper No. 9106*. Cambridge, MA: National Bureau of Economic Research.
- Engleman, S. and K. Sokoloff 2002: "Factor Endowments, Inequality, and the Paths of Development among New World Economies," *Economia* 3(1): 41-109.
- Guerrero, Juan Pablo and Helena Hofbauer 2003: "Budgetary transparency in Latin America," In Robin Hodess with Tania Inowlocki and Toby Wolfe (eds.), *Global Corruption Report 2003*. London: Profile Books and Transparency International.
- Huntington, Samuel 1991: *The Third Wave: Democratization in the Late*

- Twentieth Century*. Norman: University of Oklahoma Press.
- Johnson, Simon, Daniel Kaufmann and Pablo Zoido-Lobaton. 1999: "Corruption, Public Finances and the Unofficial Economy." *The World Bank Policy Research Working Paper Series*, 2169.
- Johnson, Simon, John McMillan and Christopher Woodruff 2002: "Property Rights and Finance," *National Bureau for Economic Research Working Paper 8852*.
- Kaufmann, D. 2003: "Rethinking Governance: Empirical Lessons Challenge Orthodoxy." Paper prepared for the Workshop on Assessing European Judicial Systems, Madrid, Spain, March 7.
- \_\_\_\_\_. 1999: "Anticorruption Strategies: Starting Afresh? Unconventional Lessons from Comparative Analysis," in Rick Stapenhurst and Sahr J. Kpundeh (ed.), *Curbing Corruption*. Washington D.C.: The World Bank.
- Kaufmann, Daniel and Aart Kraay 2002: "Growth without Governance," *Economia*, 3(1): 169:229.
- \_\_\_\_\_. 2003: "Governance and Growth in the Very Long Run: Updated Indicators, New Results." In Robin Hodess with Tania Inowlocki and Toby Wolfe (eds.), *Global Corruption Report 2003*. London: Profile Books and Transparency International.
- Kaufmann, Daniel, Aart Kraay, and Pablo Zoido-Lobaton 1999: "Governance Matters." *World Bank Policy Research Working Paper 2196*. Washington, D.C.
- Kaufmann, Daniel, Gil Mehrez and Tugrul Gurgur 2002: "Voice or Public Sector Management? An Empirical Investigation of Determinants of Public Sector Performance based on a Survey of Public Officials," Draft.
- Knack, Stephen, Mark Kugler and Nick Manning 2003: "'Second Generation' Governance Indicators." In Robin Hodess with Tania Inowlocki and Toby Wolfe (eds.), *Global Corruption Report 2003*. London: Profile Books and Transparency International.
- Kuchta-Helbling 2000: "Barriers to Participation: The Informal Sector in Emerging Democracies," Washington, D.C.: The Center for International Private Enterprise.
- Kuchta-Helbling, Catherine L. and Geurts, Geoffrey 2001: *The National Business Agenda Guidebook: A Formula for Success*. Washington, D.C.: The Center for International Private Enterprise.
- Lagos, Marta 2003: "Public Opinion of Corruption in Latin America." In Robin Hodess with Tania Inowlocki and Toby Wolfe (eds.), *Global Corruption Report 2003*. London: Profile Books and Transparency International.
- La Porta, R. et al. 1999: "The Quality of Government," *The Journal of Law, Economics and Organization*, 15(1):222-279.
- Lipset, Seymour Martin 1959: Some Social Requisites of Democracy: Economic Development and Political Legitimacy. *American Political Science Review*, 53, 69-105.
- Mauro, Paulo 1995: "Corruption and Growth," *Quarterly Journal of Economics*, 110 (3), 681-713.
- May, John D. 1978: Defining Democracy: Bid for Coherence and Consensus. *Political Studies*, XXVI, 1, 1-14.
- Naim, Moisés 2003: "Hugo Chávez and the Limits of Democracy," *The New York Times*, March 5.
- North, Douglass. 1992: "Transaction Costs, Institutions, and Economic Performance." *International Center for Economic Growth, Occasional Paper*, 30. San Francisco: Institute for Contemporary Studies Press.
- O'Donnell, Guillermo 1993: On the State, Democratization and Some Conceptual Problems: A Latin American View with Glances at Some Postcommunist Countries. *World Development*, 21, 8, 1355- 1369.
- \_\_\_\_\_. 1994: Delegative Democracy. *Journal of Democracy*, 5, 1, 55-69.
- O'Donnell, Guillermo, Philippe Schmitter and Lawrence Whitehead 1986: *Transitions from Authoritarian Rule: Tentative Conclusions about Uncertain Transitions*. Baltimore: Johns Hopkins University Press.
- Organization of Economic Cooperation and Development -- The Development Center, in cooperation with CIPE, PriceWaterhouseCoopers, and USAID. 1999: Final Report on the Washington Conference on Corruption: Fighting Corruption in Developing Countries and Emerging Economies: The role of the private sector. February 22-23.
- Ott, Katarina (ed.) 2000: *A Citizen's Guide to the Budget*. Zagreb, Croatia: The Institute for Public Finance.
- Polanyi, Karl. 1944 (1957): *The Great Transformation*. New York: Rinehart.
- Quintos de Jesus, Melinda 2003: "Effective Communication for Effective Governance: The Press and the Public," *CIPE Economic Reform Feature Service*, March 31 (available online at:www.cipe.org).
- Rauch, J. and P. Evans 2000: "Bureaucratic Structure and Bureaucratic Performance in Less Developed Countries," *Journal of Public Economics*, no. 75/1.
- Rice, Susan E. 2003: "The New National Security Strategy: Focus on Failed States," *The Brookings Institution Policy Briefs*, No. 116, February.

- Rivera-Batiz, Francisco L. 2002: "Democracy, Governance, and Economic Growth: Theory and Evidence," *Review of Development Economics*, 6(2), 225-247.
- Rodrik, D. and A. Subramanian, and F. Trebbi 2002: "Institutions Rule: The Primacy of Institutions over Geography and Integration in Economic Development," CID Working Paper No. 97. Cambridge, MA: Center for International Development at Harvard University.
- Schedler, Andreas, Larry Diamond and Marc F. Plattner (eds.) 1999: *The Self-Restraining State: Power and Accountability in New Democracies*. Boulder: Lynne Rienner.
- Schmitter, Philippe C. and Terry Lynn Karl 1991: "What Democracy Is...and Is Not," *Journal of Democracy*.
- Schumpeter, Joseph A. 1952: *Capitalism, Socialism, and Democracy*. London: G. Allen and Unwin.
- Sen, Amartya 1999: "Democracy as a Universal Value," keynote address at the Global Conference on Democracy, New Dehli, February 14-17 available at [www.ned.org](http://www.ned.org).
- Shleifer, Andrei, and Robert W. Vishny. 1993: "Corruption." *Quarterly Journal of Economics*, 108, 599-617.
- Stigler, George J. 1971: "The Theory of Economic Regulation." *Bell Journal of Economics and Management Science II*, 3-21.
- Sullivan, John D. 1999: "How Business Can Affect Public Policy." CIPE, *Economic Reform Today*, 1.
- \_\_\_\_\_ 2000: "Anti-Corruption Initiatives from a Business View Point." Speech given at the Sixth Annual Harvard International Development Conference, April 8.
- Tocqueville, Alexis de 1945: *Democracy in America*. New York: Vintage Books.
- Vishwanath .T and D. Kaufmann 1999: "Towards Transparency in Finance and Governance. The World Bank (draft of September 6).
- Wallack, Howard A. 1991: "Legislative Advisory Services Improve Decision-Making." CIPE, *Economic Reform Today*, 1.
- The World Bank 2003: *World Development Report: Sustainable Development in a Dynamic World -- Transforming Institutions, Growth and Quality of Life*. Washington, D.C.: The World Bank.
- \_\_\_\_\_ 2002: *World Development Report: Building Institutions for Markets*. Washington, D.C.: The World Bank.
- \_\_\_\_\_ 2002: "Strengthening Oversight by Legislatures," *Poverty Reduction and Economic Management Notes, Public Sector*, Number 74, October.
- World Economic Forum and Harvard University 2002: "Executive Opinion Survey," prepared for *The Global Competitiveness Report*. New York: Oxford University Press.
- Zakaria, Fareed 1997: "The Rise of Illiberal Democracy," *Foreign Affairs*, November/December, 22-43.