



**House of Lords Select Committee on Economic  
Affairs  
Inquiry on the Economic Impact and  
Effectiveness of Development Aid**

**Submission by Transparency International UK (TI-UK)  
December 2011**

## **Introduction**

1. A description of Transparency International UK (TI-UK) is provided in the Annex.
2. TI-UK welcomes this inquiry by the House of Lords. As an anti-corruption organisation, TI-UK is primarily concerned about the need for greater transparency and accountability in the provision and use of development aid. TI defines corruption as the abuse of entrusted power for private gain. Corruption has a hugely damaging impact on economic growth and sustainable development because it diverts scarce resources from development programmes, undermines the rule of law and weakens public and private institutions that are essential for growth and stability. This is an especially acute problem where corruption leads to the depletion of capital resources and capital flight.
3. TI-UK welcomes the UK Government's commitment to increasing development aid to poorer countries in order to help them to attain broad-based economic growth as well as specific targets such as the UN Millennium Development Goals. However, weak governance and corruption can undermine the effectiveness of the UK's development aid. Measures to reduce overseas corruption should therefore be integrated into the Government's overseas aid strategy.
4. At the same time, the UK should be ensuring it reduces its 'corruption footprint' abroad. When UK nationals and companies pay bribes in the developing world to win business unfairly, and when UK institutions provide a safe haven for the illicit wealth of corrupt foreign leaders, the UK becomes complicit in perpetuating corruption in these countries, many of whom are recipients of UK development aid. The effective enforcement of the new Bribery Act and a strengthening of the UK's anti-money laundering regime should therefore be given a high priority.
5. This submission by TI-UK responds chiefly to question 12 of the House of Lords Inquiry: "In what ways, if any, can the British government improve the effectiveness of its development aid?"

## **Tackling corruption is essential in order to improve the effectiveness of UK aid**

6. Over the 5 years from 2005 to 2009, 84% of the UK's bilateral ODA was allocated to countries scoring 3 or less on TI's Corruption Perceptions Index (10 is highest attainable score on the Index). It is therefore understandable that the Government's decision to increase rapidly both the aid budget to an amount equivalent to 0.7% of Gross National Income and the proportion going to fragile and conflict-affected states has raised fears that, because of weak governance and corruption, the increased aid will not have the desired impact on poverty reduction and may actually create greater opportunities for graft.
7. Over the years, the UK and other bilateral and multilateral donors have, as part of their overseas development intervention strategies, invested considerable resources in encouraging recipient governments to introduce governance and anti-corruption reforms. These included the establishment of independent anti-corruption agencies that were supposed to spearhead investigative and law enforcement efforts. However, the record has been patchy, particularly when there has been insufficient support from domestic constituencies for reforms and deeply entrenched corrupt networks have been able to frustrate reforms.
8. In several countries, anti-corruption agencies have been starved of resources and subverted by political pressure. It is therefore doubtful whether anti-corruption reforms can be successful when they are promoted by donors without sufficient

support from domestic constituencies. There is no easy solution to this problem. However, if the UK and other donors were to withdraw aid from countries where corruption is endemic and deeply entrenched, they would have no leverage to encourage reforms and this would hurt the poorest and most vulnerable groups in these countries - they are disproportionately affected by corruption and their situation is likely to worsen if aid were to be withdrawn.

### ***Wider context***

9. In spite of the widespread phenomenon of corruption, TI-UK agrees with the earlier observation made to this Committee by Roger Ridell that aid has had a broadly beneficial impact at the level of the macro-economy, particularly in capital-scarce poorer countries. However, the issue in question is whether these countries' growth rates could be further improved by a serious attack on corruption, and, in particular, whether a broader based form of growth, embracing the lowest income groups, is achievable. The question has become more complex in the recent past as the range of financial flows into many developing countries has increased (e.g. high levels of remittances, a sharp increase in FDI, major investments in resource extraction by China) in ways which increase the difficulty of isolating the impact of aid.

10. The increase in the value and complexity of aggregate flows means that in practice the leverage of donors in relation to 'soft' governance reform issues is much reduced. For example in April 2011, Uganda purchased Su30 fighter planes from Russia for \$750 million, or nearly 75% of expected aid flows this year. Yet Uganda has been a prime target of governance reforms by DFID and other donors.

11. Often, the real obstacle to the leverage which donors have sought in order to support anti-corruption efforts are the corrupt networks which control the political finance which keeps governments in power. This may take the form of political funding (as in the Anglo Leasing scandal in Kenya) or of measures to secure votes for constitutional change (as in the bids for third and fourth presidential terms by Presidents Obasanjo and Museveni, respectively). There is no evidence to suggest that the strength of the process of financial accumulation through various forms of corruption for political purposes has yet abated.

12. There are additional structural problems in a majority of aid recipient countries which underpin the sinews of corruption and are particularly difficult problems to address through donor strategies. These are, in particular, the size of the informal economy, the extent of organised crime, and government complicity in very light tax regimes for multinational and other companies. The informal economy in nearly all low-income countries accounts for at least 30% of GDP – flows into and out of this part of the economy are not recorded, elude the tax net, and are regularly used to bribe local and national officials. Organised crime, primarily but not only connected to the drugs trade, is a force which exerts corrupt influence on governments, and thus reinforces corruption at the national level. UNODC's World Drugs Report for 2009 highlighted this issue in relation to West Africa. Separately, light or zero-tax regimes are now widely recognised as an issue in many natural resource exporting countries. The Dodd Frank legislation in the US, if it is emulated with comparable legislation in the EU, will help to exert pressure on governments in this area, because of the requirement for mandatory reporting of all extractive company payments to governments on a country-by-country and project-by- project basis.

13. These structural problems reinforce corruption but donor policies presently do not pay sufficient attention to them.

### ***Dilemmas***

14. There are some key dilemmas which need to be recognised in shaping policies which seek to address the complexities of corruption. First, in relation to

leveraging 'soft reforms', the role of an outside agency will always be constrained since it cannot by definition have democratic legitimacy. As noted earlier, this has been reflected in the patchy record of donor support for good governance through interventions ranging from support to anti-corruption bodies and parliamentary accounts committees. Although in some countries there is discernible progress at the level of national integrity systems, and at the level of support to civil society, it is very modest in relation to the total sums expended on these programmes.

15. Second, donors face a conflict between their 'development' aims and the commercial, export-oriented aims of their leading companies. TI's 'Bribe Payers' Index' has consistently shown that construction and defence are among the most corrupt sectors worldwide. Many donor countries, including the UK, have in the past provided active support to their companies trading in these sectors and turned a blind eye to corruption, a fact which is recognised by many aid recipient countries. Although several international initiatives, and national anti-bribery laws, have changed the regulatory environment, there continues to be a tension between export promotion and promoting good governance. It also remains to be seen whether India, China and Russia - who are major players in global export markets and, increasingly, are also sources of development aid - will enforce effectively the new foreign bribery laws they passed/introduced in 2011.

16. Third, the design of many large scale aid programmes has become more complex over time as donors have sought to promote, for example, competitiveness or improve the construction of wells in thousands of villages. This 'disaggregation' of the level of the end client creates many opportunities for corruption at the local level, as confirmed by many surveys by national chapters of TI and other organizations reviewing the delivery of services such as water and education.

### ***Broad Recommendations***

17. Given these arguments TI-UK considers that the following broad considerations should be observed in relation to UK aid policy:

- 1) The specific target of increasing aid to 0.7 per cent of Gross National Income should not in itself be a goal of the aid programme: such a target can easily lead to an evasion of the issue of the impact of corruption on development.
- 2) Aid can have some influence on 'governance' issues but can never be decisive.  
Moreover, in this area in particular its impact can only be measured over several years; the complexity of financial flows to low-income developing countries has lent further weight to this limitation.
- 3) All donors, including DFID and the international financial institutions (IFIs) which it supports, should be prepared to have their programmes subject to parliamentary debate in recipient countries, as part of the normal process of democratic accountability.
- 4) A key part of donor strategy should be to see a reduction in the size of the informal economy, as a means to both reducing a critical source of corruption and to increasing the tax take; mandatory reporting by companies of payments to governments on a country-by-country and project-by-project basis could be expanded beyond extractive industries to cover all sectors. This would help to reduce the connivance between governments and companies in tax evasion.
- 5) The UK, in line with other donors, should continue to build consistency between its aid and export promotion policies, taking into account the need to enforce effectively the UK Bribery Act.

### ***Specific Recommendations***

18. TI-UK believes that the UK and the recipients of its development aid will be more effective in responding to the challenges of weak governance and corruption through an approach based on mutual accountability between the recipient

government and all donors. In high corruption-risk countries, there should be agreement on a clearly defined programme of specific reform measures that can be monitored both by Parliament and by a donor consortium. Since public financial resources are inherently fungible, the steps needed to ensure that aid is not corruptly diverted are the same as those needed to ensure effective overall public financial accountability. TI-UK makes the following specific recommendations, some of which build on recommendations made by the Independent Commission for Aid Impact (ICAI) to strengthen DFID's approach to anti-corruption (see ICAI's Report 2, November 2011):

- 1) In any country assessed as having a high risk of corruption, DFID working with other donors, including the IFIs in which it is a major shareholder, should develop an explicit anti-corruption strategy.
- 2) DFID should be proactive in assessing and mitigating corruption risks. It should review the structure and nature of its counter-fraud and anti-corruption resources and develop a more co-ordinated approach to risk assessment, risk management, anti-corruption programming and fraud response taking into account the UK institutions which can collaborate with aid recipient governments in tracking funds and freezing assets where appropriate.
- 3) The Government's current Anti-Corruption Champion, the Secretary of State for Justice, and the Secretary of State for Development should work more closely to ensure that a coherent, co-ordinated approach to tackling overseas corruption is integrated fully into the UK's overseas aid strategy.
- 4) Building on its Fiduciary Risk Assessments, DFID, with its partners, should undertake country financial accountability and procurement assessments and develop credible, time-bound action plans for reform of budgeting, accounting, audit and procurement systems. This would build on the existing Public Expenditure and Financial Accountability programme that DFID, the World Bank and other donors support.
- 5) All civil society organisations (CSOs) through whom development assistance is disbursed, should be required to adhere to a common verifiable standard for monitoring and auditing their use of aid monies. CSOs should also have robust internal systems for countering bribery and corruption. TI-UK and other partners in BOND have developed NGO Principles and Guidance for Countering Bribery<sup>1</sup>, which can assist CSOs in developing such systems.
- 6) All aid funds should be recorded in recipient governments' budgets and subject to legislative and other oversight mechanisms. The transparency of public income and expenditure management, all aid transactions and the related monitoring systems should be increased.
- 7) In accordance with the International Aid Transparency standard, UK and other donor aid budgets should be presented in a transparent way so that the public in both the donors' and recipients' countries know the precise nature of commitments and disbursements.

19. In making these recommendations TI-UK is conscious of the fact that there are many challenges to be overcome in rolling back corruption, so that aid will be more effective. In countries where corruption is endemic the injection of very large sums of capital will never be corruption-free. This is equally true of the funds designed to mitigate or adapt to climate change, such as the Reducing Emissions from Deforestation and Forest Degradation programme and the proposed Green Climate Fund. Corruption undermines broad-based development and all donors, including DFID, need to adopt a more robust approach in addressing the problem, which recognises the underlying forces which drive corruption as well as its more public manifestations.

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<sup>1</sup> <http://www.transparency.org.uk/publications>

Transparency International UK ([www.transparency.org.uk](http://www.transparency.org.uk)), the UK national chapter of TI, fights corruption by promoting change in values and attitudes at home and abroad, through programmes that draw on the UK's unique position as a world political and business centre with close links to developing countries.

TI-UK:

- Raises awareness about corruption;
- Advocates legal and regulatory reform at national and international levels;
- Designs practical tools for institutions, individuals and companies wishing to combat corruption; and
- Acts as a leading centre of anti-corruption expertise in the UK.

TI-UK's vision is for a world in which corruption is greatly reduced and the UK has zero tolerance for corruption both at home and abroad.