Corrupt Budgeting
Fake Reform and the Consequences
U.S. Treasury, Office of Technical Assistance
Budget and Financial Accountability Team Meeting
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Overview

How does corruption work in budgeting?

What are the consequences?

What can be done about it?
How does corruption work in budgeting?
Auction-Based Budgeting

Corrupt budgeting

- **It’s been going on for ages**: Emperors, kings and queens, lords and ladies, dictators and tyrants have all been doing it

- **Auction-based budgeting**: a form of budgeting where resources are provided on the basis of willingness to pay
  - *Handing out resources to the highest bidder*

- **Opposite of what is generally expected**: Allocating resources on the basis of altruistic means, such as good government policy, institutional performance and/or public good investment criteria
Auction-Based Budgeting

Good Ol' Fashioned Bribery

When, Where and How?

- **During formulation:** informal or formal budget hearings
  - Fees and favours

- **During negotiation:** legislative consideration
  - Fees and favours

- **After the legislature has approved the budget:** Allotments and commitments
  - Fees and favours
    - Power comes from not passing the budget (but...) and other legislation

- **Fees and Favours**
  - **To Officials:** Campaign funds, Rolex watches, cash, gold, drugs, promotions, incentives, rewards, blackmail etc
  - **To Legislators:** Projects and contracts, appointments to powerful positions for friends and family, cash etc
  - **To Businesses:** Contracts for projects, subsidies, grants, concessions, waivers, write-offs, asset transfers etc
What are the Consequences of Corruption in Budgeting?
Fake Reform

- Distraction Reform
- Can you tell the reformers from the non-reformers, and the fake reforms?
- Look for the red flags
A National Accountability Framework

The foundation for democracy and good governance
A National Accountability Framework

Empowering citizens to hold government to account

Being clear with officials of what is expected

The Budget Cycle is a key secondary area where citizens can hold government to account in the space between elections

Foundation Accountability of a Democratic Society

• Elect the Legislature and President
• Lobby representatives through town halls and other mechanisms
• Participate in public forums

Media and Social Media

External Auditor

Ombudsman/Anti-Corruption Body

Attorney General/Prosecutors

Inspector General/Police

Courts

Legislature

President

Administration

Ministers

Agencies

Write to ministers

Lobby the executive

Complain to agencies

Engage the media

Sue the government

Give evidence to the authorities

Complain to Ombudsman/Anti-Corruption bodies

Report to the police

The People
Viewing Corruption through a Public Finance Lens

A Systemic Problem
Follow-the-Money Corruption Cycle

**Promises**
- Accountability Institutions
  - Police, Prosecutors, Courts, ACC ...

**Budget**
- Financial and non-financial “promises”

**Commitment**
- Allotments and POs

**Procurement**
- Tendering & contracting

**Contract management**
- (incl. subcontracting)

**Verification and Payment**
- (invoice certification)

**Results**
- Audit (financial and non-financial “results”)

**Revenue**
- Tax
- Customs
- Extractives
- Fees and Fines
- Grants

**Accounting**
- for it all

**Balance Sheet Management**
- Assets (cash, property, prepayments, receivables etc) and Liabilities (loans, guarantees, arrears)

**Follow-the-Money Corruption Cycle**

- **Pay to clear irregularities**
- **Pay to facilitate**
- **Pay to get positions**
- **Pay to change contracts**
- **Pay to access**
- **Pay to clear referrals and capture**
- **Pay to have assets, bailouts and shift risk**

**Auction – pay for budget**
- Pay to access

**Pay to win contracts**
- Pay to clear referrals and capture

**Learn**
- Pay to facilitate and cover tracks

**Pay to facilitate**
- Pay to win contracts

**Accountability Institutions**
- Police, Prosecutors, Courts, ACC...

**Personnel**
- Establishment, Payroll, HR ...

**Pay to access**
- Pay to clear referrals and capture

**Pay to have assets, bailouts and shift risk**
- Pay to clear referrals and capture

**Balance Sheet Management**
- Assets (cash, property, prepayments, receivables etc) and Liabilities (loans, guarantees, arrears)
Main Points

• The Scale of the Problem
  • Waste of time, money and effort
  • Catastrophic collapse of national accountability

• Reform priorities and consequences
  • Downstream and up stream effects
  • Systemic Effects

• Theory of change
  • Target Budget and Audit Corruption
  • For Better Learning and National Accountability

• Aid Allocation
  • Direct aid to most cost-effective but politically difficult interventions?
  • How can conditionality help?
  • Merging anti-corruption with fiscal reforms
What Can Be Done About Corrupt Budgeting?

Focus Where it Matters Most
Technical Reforms are Easy
Politics Reigns Supreme
Budgeting for National Accountability

- Aggregate expenditure out-turn
- Expenditure composition out-turn
- Revenue out-turn
- Macroeconomic and fiscal forecasting
- Fiscal strategy
- Medium term perspective in expenditure budgeting
- Budget preparation process
- Legislative scrutiny of budgets
- Budget Classification
- Budget Documentation
- Central government operations outside financial reports
- Performance information for service delivery
- Transfers to subnational governments
- Public access to fiscal information
- Fiscal risk reporting
- Public asset management
- Debt management
- Public investment management
- In-year budget reports
- Annual financial reports

Comparability

- Reliable Budgets
- Policy-based budgets

Transparency

BudgetDisclosures & Due Process for Investment

- Budget Negotiation: Policy change / stop the auctions
- Budget Disclosures for National Accountability

Constrain: Realistic estimates / stop the auctions

Budget & EoY Fin Stats for National Accountability

First Look For Evidence
Budget Reforms

- Performance and Policy Based Budgeting
  - Might not be a capacity problem but a corruption problem

- Political and Communications Strategies
  - Mobilising the winners (citizens and civil society)
  - Dealing with the spoilers

- Culture Change and Team-Based Performance Management
  - Targeting the institutional culture problem
From Auction-Based Budgeting to Policy & Performance Based Budgeting

**Policy-Based Budgeting**
- Allows only good evidence-based policy ideas to get funded
- Solves problems with a medium-term/forward-looking perspective
- Reduces opportunity for corruption and incompetence

**Performance-Based Budgeting**
- Gives clarity as to what the government is trying to achieve with the people’s money
- Ensures consequences for good and bad performance
- Keeps government responsible for its promises and results
Key Concepts of Good Budgeting

Generally

The 3 Budgetary Outcomes – What Every Budget is Supposed To Do

• Aggregate fiscal discipline
  • We hit our fiscal aggregate targets: Budget Balance, Revenue, Expenditures, Debt ...

• Strategic allocation of resources
  • We allocate resources in accordance with a fiscal strategy developed in accordance with clear priorities.

• Efficient service delivery
  • We get better at delivering services to the people
Key Concepts of Policy Based Budgeting

- **Fiscal Discipline**
  - Achieved by focusing on policy in the budget process

- **Fiscal Space**
  - The room for new policies. Every year low priority-low impact activities should be replaced with higher priority-higher impact activities.

- **Fiscal Rules and Fiscal Gatekeeping**
  - The Rules of the Game
  - Ensuring the Rules are Followed
Policy-Based Budgets

- Only good evidence-based ideas get funded
- Makes it harder for people to get away with corruption or incompetence
- Efficient revenue raising and Efficient spending

Cabinet (and other key decision-makers)

- Implementers (Agencies)

Good Policy

- Raise revenue
- Deliver services
- Allocate and spend

Bad Policy

- Fiscal Gatekeeping
- Reality Checks
- Fiscal Rules

Only Good
Policy

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Busting Budget Auctions By Focusing On Policy Change
Fiscal Space Creation and Filling: Five Dimensions of Fiscal Space

How much fiscal space is needed for next year’s budget headlines?

Cabinet Decides Early

**TAX and Non-tax**
Create Fiscal Space through
- Shifts in informal to formal collections
- Target arrears
- Clear backlogs
- Broaden Base

**EFFICIENCY and Savings**
Create Fiscal Space through
- Public investment management
- Portfolio/project reviews
- Agency reviews
- Efficiency dividends
- Targeted anti-corruption

**BORROWING and Cash Reserves**
Concessional borrowing comes with costs
Seek to reduce concessional constraints
Seek ways to get a sovereign risk rating
But: Debt management, public investment management and fiscal risk management all need to improve

**GRANTS and 3rd Party Payments**
Create Fiscal Space through
- Reprioritizing grant funds to higher prioritize
- maximize access to untapped grants
- accelerated grant execution

COST OF EXISTING EXPENDITURE POLICY
FORECAST OF EXISTING REVENUE POLICY

Time
Key Concepts of Policy Based Budgeting

- **Medium-term perspectives to identify and resolve difficult problems**
  - Difficult problems take time to solve and can not be addressed with single year horizon.
  - Donor projects are often financed by lapsing multi-year grants.

- **Separation of existing and new policy**
  - The forward estimates (revenue and expense) are based on an agreed assessment of the costs to implement existing policies. New policy is considered every year, which once fiscal impacts [costings] are agreed get added to official estimates.

- **Rolling forward estimates for budget building**
  - The principal rolling estimates is that the first forward year becomes the baseline for the new budget year. Current year new policies become existing policy in next budget year.
**Rolling Forward Estimates**

1. **Key to Breaking the Budget Auctions**

   - **EXISTING POLICY**
   - **NEW POLICY**
   - **NEW**

   - **BUDGET**
   - **FORWARD ESTIMATES**
   - **FORWARD ESTIMATES**
   - **FORWARD ESTIMATES**

   **BUDGET**
   
   **FORWARD ESTIMATES**
   
   **FORWARD ESTIMATES**
   
   **FORWARD ESTIMATES**

   **New Health Policy Proposal:** The government wants to build a new hospital at a capital cost of $35 million. It will take 3 years to build and it has an operating cost of $5 million per year.

   **Mechanisms to ensure good evidence-based policy decisions are brought forward**
   - Independently validated costings of the policy proposals
   - Economic evaluations
   - Performance metrics

   **CAPITAL**
   - 10
   - 20
   - 5

   **OPERATING**
   - 5
   - 5

   **PARAMETER-DRIVEN NEW FORWARD ESTIMATE**
Overview of Performance Based Budgeting

- Transparency of planned and achieved performance
- Consequences for good and poor performance
- Announcing promises and reporting on results
- Informs the continuous improvement cycle
Fiscal Performance Analytics: Bringing Financial and Non-Financial Info Together

Performance-Based Budgeting
Building the Learning Machine
Consequences for good and bad performance

1. Announce promises through the budget

2. Budget to deliver better outcomes for the people...
   - Better education
   - Improved health
   - Safer communities
   - Reliable infrastructure

   $ $ $ $
   schools curriculum training hospitals drugs clinics police courts emergency electricity roads water

   ....by producing the right outputs

   KPIs

   ....by using the right inputs

3. Report on progress on fiscal promises

  Govt. report Annual report

   CITIZENS

   TOWNHALLS CONSULTATIONS MEDIA

PHASE I: BUDGET PREPARATION
PHASE II: BUDGET IMPLEMENTATION
PHASE III: REVIEW PERFORMANCE
Core Performance Analytics

- **Mandatory Reports:** Financial and non-Financial Plans, Financial Statements and Non-Financial Performance Statements
- **Efficiency and Value for Money:** Avg Cost per staff member, Admin costs as %, Shares: Travel, International and Local Consultant Costs, Equipment Costs etc. Benchmarked with other “competing” programs
- **Cost-Effectiveness:** Average and Incremental Cost to Secure improvements in outputs or outcomes
- **Credibility:** Of Planning for Results
- **Consolidation:** Supports the bringing of cash and in-kind assistance on budget
Bringing Performance & Policy Based Budgeting Together

The Budget Cycle is:
- The M&E Cycle
- The Continuous Improvement Cycle
- The Institutionalized Learning Cycle
Be Wary of Fake Reforms and Fake Reformers

Policy Based Budgeting

Red Flags for Fake Budget Reform

1. No medium-term perspective
2. No rolling forward estimates
3. Macro-fiscal models are being used outside the resource allocation process
4. No explanation of the changes in the budget and fiscal strategy from the previous year
5. No high-level debate on fiscal space creation and filing
Performance-Based Budgeting

Red Flags for Fake Budget Reform

6. No reporting by standard functions of government
7. Annual reports are not easily comparable to the budget
8. No reliable reporting of performance information (targets and results)
9. Performance information is not actually used to manage performance or inform decision making.
10. Lack of linkages between agency level performance targets and the data monitored by the central budget office
11. The administrative culture is not one that focuses on performance – in getting the basics right, the very first of the “basics first” principles was to “foster an environment that supports and demands performance”.

12. There is no aggregate fiscal discipline – there are implausible estimates of fiscal aggregates over the medium term.
Political Strategies
For Busting Budget-Based Corruption
Political Strategies for Busting Budget-Based Corruption

1. **Building and Protecting a Reform Alliance** – can’t do it without enough people at the top and in the middle

2. **Legitimise revenue sharing** with the most powerful – Don’t need a culture of corruption to share the wealth (constraints)

3. **Amnesties** for past behaviour (save grand corruption)

4. **Targeted Sting Operations** to increase cost of being corrupt, and lower cost of being clean

5. **Communications Strategies** to Build Demand and Support

6. **Diplomatic, Security and Aid Strategy** Coordination

7. **National Accountability Strategies** that “Come Clean on Corruption”

8. **Technical Solutions:**
   - Policy Based Budgeting: Policy Change, no project tables, etc etc
   - Performance Based Budgeting: Much more transparent disclosures
   - Using Appropriation Authorities: e.g. 1/12th rule, allotments/sequestration powers to withhold resources, administrative authorities etc)
Corrupt Budgeting

Background Papers

- Follow-the-Money Corruption Cycle: Revealing National Accountability Failures
- Performance and Policy-Based Budgeting: How to Spot the Fakes
- The Blight of Auction-Based Budgeting: What Is It and How Can We Deal With It?