

Report of the Expert Advisory Group on Anti-Corruption, Transparency, and Integrity in Latin America and the Caribbean

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Executive Summary

Against the backdrop of scandals of unprecedented scope in the Latin American and Caribbean (LAC) region, it is evident that corruption is threatening to erode the foundations of much of the region's economic well-being and political stability as well as the rule of law. Fed up with corruption and impunity, acting concretely and effectively to curb this cancer is at the top of the agenda of voters and many candidates in the region's many elections in 2018 and beyond. It is time to take a hard look at what has transpired in the region and the world and what we have learned, as well as what this means for upcoming efforts to control corruption and improve the prospects of the region's 650 million residents.

Inter-American Development Bank (IDB) President Luis Alberto Moreno convened an Expert Advisory Group (EAG) of eight governance and anti-corruption scholars and practitioners (see Annex 1) to identify innovative and effective approaches to combat corruption in the LAC region. Drawing on the members' decades of experience, this report analyzes the key features of corruption in the region and proposes an ambitious agenda toward more systemic transformation.

It is impossible to overstate the urgency of this effort. Corruption is rampant at the highest levels of government, society, and the economy. It is linked to the pernicious presence of state capture by the elites in much of the region and, as illustrated in the Lava Jato case, operates across borders. The evidence suggests that on balance, over the past two decades, there have been no significant improvements in the

region in key governance dimensions, or worse—in fact, with some exceptions, the region has performing poorly in the implementation of the rule of law and in control of corruption. The distortive impact of money in politics in the region is associated with policies and practices benefiting the elite few and, with failed reforms, undermining public trust in government and in democratic institutions.

On the one hand, globalization and technology provide unprecedented opportunities to hide the proceeds of criminality and corruption, which in turn can be used to buy access to power. On the other, systemic improvements in governance, collective action, use of new technologies, as well as implementation of regulations based on international standards, offer promising avenues to addressing corruption.

In most LAC countries, corruption and capture are systemic. Networks of interconnected political and economic elites often undermine sound policymaking and the rule of law, entrenching impunity, and diverting public resources and investment away from the public good.

This report recommends a multi-layered approach that requires collective action by governments, the private sector, civil society, and international institutions to tackle the roots of corruption and capture through global, regional, and domestic initiatives. Technology and innovative governance tools and approaches can enable these actors to work together to implement effective governance strategies. Political will from the leadership will also be key.

To address the transnational nature of corruption, regional initiatives need to be strengthened.

These include initiatives in the judiciary, which have lagged in the region and have often been subject to corruption, perpetuating impunity, and undermining the rule of law and trust in institutions. Judicial standards, laws, and practices will need to be aligned with international standards, and the implementation of innovations such as plea bargaining and related negotiated settlements should also be considered across the region. More transparency initiatives should be promoted at the regional level, such as establishing public registers that disclose the ultimate beneficiary owners of companies and financial entities or adopting global standards of transparency in natural resources, such as those embodied in the Extractive Industries Transparency Initiative (EITI).

Domestically, reforms need to be implemented to stem the unregulated flow of money into politics and improve the management and governance of natural resources. Reforms are also needed in procurement and contracts, particularly for large infrastructure investments and in extractive industries. The public must have access to accurate and credible information on political finance and on the use of public resources. Additionally, they must have the appropriate channels to participate in public affairs and access government services. Simplification of government transactions can also aid oversight.

The region is currently at a political and socioeconomic crossroads. Whether and how it addresses

the costly challenge of corruption and capture will be critical for its medium and longer-term prospects. Consequently, the report concludes with a call for audacity by regional and country leaders and actors in promoting and implementing systemic and concrete governance reforms. Real progress in the key areas of focus would help strengthen the rule of law and public institutions, address state capture, and help meet citizens' aspirations for sustainable and inclusive development. These efforts must be spearheaded from within each country. Political will, determination, and perseverance will be required to address a challenging agenda for LAC countries and their public and private institutions.

Promising opportunities exist to work closely with civil society and an increasingly concerned private sector, benefit from technology, collaborate with the global and regional anti-corruption community, and draw on the resources, support, and engagement of the IDB and other international institutions. The ambitious strategy laid out here is a significant departure from a "business as usual" or incremental approach. The latter would not restore confidence and investments, nor have the major impact required. While programs should be tailored to the prevailing conditions in each country, a full-throated commitment to implementing concrete governance reforms throughout the region and across borders will be critical.

Acknowledgements

The Inter-American Development Bank appointed the Innovation in Citizen Services Division of the Institutions for Development Sector (IFD/ICS) as the focal point to help the work of the Expert Advisory Group (EAG) in accomplishing its mission. The experts would like to especially thank Ana Maria Rodriguez-Ortiz, Carlos Santiso, Roberto de Michele, Francesco De Simone, and Isaías Losada

Revol for their excellent support. During the process of drafting this report, the EAG presented its preliminary results to the IDB's Senior Management and Board of Executive Directors and received important inputs and feedback on its findings. The experts also appreciate the valuable research assistance from Jimena Montoya of the Natural Resource Governance Institute (NRGI).

Background: Corruption, Crisis, and Opportunity in Latin America and the Caribbean

1

With advances in technology and international legal standards, and the evolution of the economic and financial sectors in the Latin America and Caribbean (LAC) region in recent years, demands for greater transparency and integrity across all sectors of the economy and society have been growing stronger and more sophisticated. These demands have assumed greater urgency in the harsh light of a number of high-profile corruption scandals that have led to a crisis of confidence affecting citizens and investors in most LAC countries.

While the major corruption cases have highlighted the ability of some anti-corruption institutions—most notably prosecutors and judges in a few countries—to respond effectively, the larger narrative is one of failure to prevent corruption across the region. Clearly, these wins against impunity will strengthen incentives against corruption, but there is no guarantee that they will be the harbingers of a new direction for the region. Rather, they will remain outliers if the underlying systems that facilitate and drive corruption are not addressed. Anti-corruption initiatives have figured prominently in electoral campaigns, as the vast majority of LAC citizens elect presidents in 2018. But democracy is exposed to new threats, as political finance has become a source of exceptional influence over governments, including by criminal networks. At the same time, globalization and new technologies are making funds easier to move and harder to track, outstripping the capabilities of all but the most sophisticated monitoring bodies.

Compounding the challenge is the fact that LAC countries face a very different global environment

today compared to just five years ago. Nationalism, isolationism, and protectionism are risks in some major industrialized nations. The United States, once a leader in the global anti-corruption arena, has retreated from commitments to transparency in extractive industries and has reduced controls on political finance and financial integrity. Britain and continental Europe are preoccupied by Brexit, immigration, and their own regional political and economic challenges, including those associated with Russia's foreign policy. The fall in commodity prices, the closing of civic space, and the resurgence of populist nationalistic and anti-democratic values in many countries around the world also create new challenges for advocates of open and accountable governance. As a result, the LAC region will need to take a leading role and develop its own initiatives rather than expecting to rely on global powers outside of the region or related external factors.

This challenging moment also offers significant opportunities. The public's attention has been captured by headlines about corruption scandals, presidents removed from power, increasing unrest, and other types of corruption in electoral politics. Technology provides citizens with the ability to increasingly scrutinize vast amounts of relevant information and data being disclosed, and, through social media, the means to share their discontent and mobilize their movements toward meaningful change. Technology, when complemented with concrete political support of transparency reforms, also provides tools to enhance the quality, cost-effectiveness, and integrity of public procurement, and shed light

on opaque and distortive political financing, hidden financial identities and beneficiary owners, and secret transactions.

The private sector, though evidently sometimes part of the problem in undermining governance, abetting state capture and collusion,—also includes a vast potential constituency for leveling the playing field, simplifying transactions, and reducing the costs associated with corruption. It is also the repository of significant knowledge on risk management. Equally important, civil society has led innovation in anti-corruption tools and has been on the front lines of advocating for reforms for decades. They are allies of anti-corruption champions and are key actors in the work that lies ahead.

It is in this context of both crisis and opportunity that Inter-American Development Bank (IDB) President Moreno convened an Expert Advisory Group (EAG) to identify innovative and effective

approaches to combat corruption in LAC countries, as well to highlight reforms that are long overdue.

This report suggests some ways forward. Drawing from the lessons of experience, we emphasize that leadership on anti-corruption reforms lies with the countries' leaders and citizens. The IDB and other international actors should stand ready to support such country-led action programs. "Business as usual" is no longer an option if the people's aspirations for an equitable and sustainable future are to be met.

The report begins with a brief overview of the costs of corruption in the LAC region. It then describes a systemic approach to reform and why it is needed. This approach encompasses four pillars ranging from the international level, through domestic policy initiatives focused on transparency and improved management of information, initiatives involving the private sector and civil society, and finally, the contributions of the IDB.

Corruption and its Costs in Latin America and the Caribbean

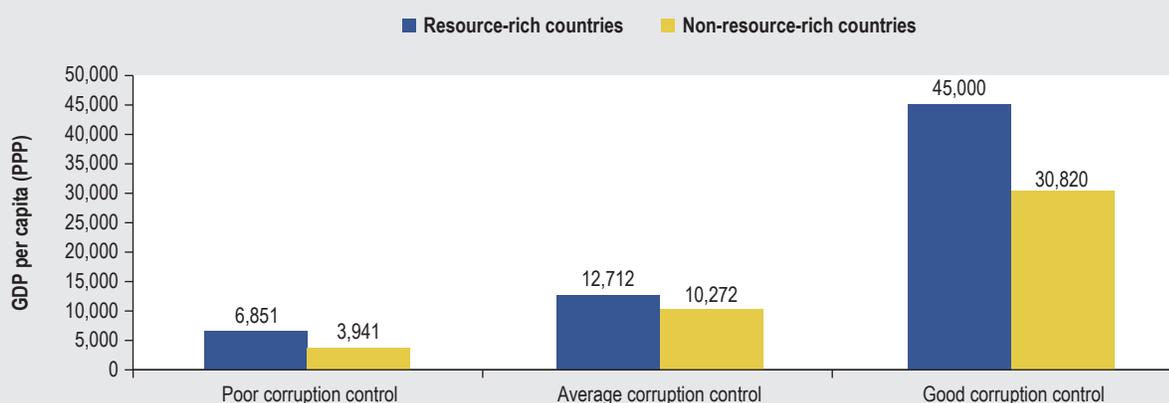
2

Corruption imposes high socioeconomic costs on countries. There is substantial evidence and broad consensus that corruption and lack of transparency adversely impact the normal functioning of the state and the rule of law and undermine public faith in those institutions. Corruption has also been shown to erode the efficient allocation of public spending, encourage tax evasion, raise sovereign borrowing costs and transactional

expenses between private parties, reduce incentives for investment, impede private sector productivity and innovation, and reduce overall economic growth.¹

Globally, improvements in governance and anti-corruption are associated with a three-fold increase over the long run in income per capita (Figure 1). This is an enormous missed opportunity for most LAC countries.

Figure 1: Governance Matters: Development Dividend of Improved Governance in Resource-rich and Other Countries



Sources: GDP per capita (atop each column) from World Bank World Development Indicators, 2012. Corruption Control data from Worldwide Governance Indicators (WGI, 2012). Countries grouped into terciles based on WGI Control of Corruption scores. Resource-rich country classification according to IMF (2010).

¹ For a detailed analysis regarding the negative consequences of corruption in the economy, see IMF, Corruption: Costs and Mitigating Strategies, IMF Discussion Note, International Monetary Fund SDN/16/05 (May 2016), available at <http://www.imf.org/external/pubs/ft/sdn/2016/sdn1605.pdf>.

Corruption in the LAC region touches everyone. The Lava Jato investigation in Brazil and other major cases have exposed the networks of corruption that connect elites at the highest levels of government and business—including transnationally—and the degree to which policy and politics have been merged in a form of state capture. The 2017 Latinobarómetro survey reported that only 30 percent of the Latin American population is satisfied with democracy and 53 percent believe that their governments are performing poorly in their efforts to fight corruption.² Petty bribery is also rampant. In 2016, one in three public service users surveyed in 20 countries reported having paid a bribe to gain access to key public services such as justice, education, or health at least once in the previous year.³

A particular concern in the LAC region is the relationship between corruption and inequality. The region has some of the highest levels of inequality in the world. Inequality in the distribution of wealth, combined with corruption scandals, has generated adverse reactions from the disadvantaged and the middle class, who are increasingly intolerant of a system rigged in favor of the rich and powerful.⁴ In fact, inequality of economic power is strongly linked to inequality of (political and policy) influence, which in its extreme form results in state capture.⁵

In addition, a major immediate cost of corruption has emerged in the region. Recent scandals laid bare the weaknesses of cumbersome legal and fiduciary instruments to fight corruption, slowing down the completion of major infrastructure projects and delaying new investments. Owners and managers of firms directly involved in corrupt schemes are not the only ones paying the consequences of their illegal

actions. Many suppliers to these firms have seen their contracts canceled because the main contract is suspended or declared null and void. Banks have been discouraged from participating in project finance due to the impact of these consequences, which become a new risk that is difficult for financial institutions to mitigate. In several countries, this has created dire economic consequences with massive job losses and many firms filing for bankruptcy.⁶

Finally, sovereign borrowing costs generally tend to increase for those countries in which corruption is perceived to be high. A recent IDB study shows a strong correlation between ratings issued by the three main rating agencies (Standard & Poor's, Moody's, and Fitch) and three commonly used corruption indicators (Figure 2). This correlation is robust to controlling for the fact that corruption is also correlated with level of development, amount of government debt, the current account balance, and an indicator of macroeconomic instability.⁷

Countries are therefore faced with the challenge of striking a balance between bringing to justice powerful firms at the heart of the corruption scandals, deterring future corruption and preserving public investments that are highly valued by citizens. To achieve these goals, it is important to develop new legal tools to face corrupt practices, that facilitate the transfer of project assets to a new firm when corrupt practices by the original firm are detected, to minimize delays and interference with service provision in ongoing projects. Projects tainted by corruption for which the costs of becoming operational exceed their expected benefits to society should not be completed and their funds redirected towards projects that serve the public interest.

² Informe Latinobarómetro 2017, Corporación Latinobarómetro (January 30, 2018), pp. 16 and 36, available at <http://www.latinobarometro.org/latNewsShow.jsp>.

³ Transparency International, *People and Corruption; Latin America and the Caribbean*, Transparency International Global Corruption Barometer (October 9, 2017), p. 5 available at https://www.transparency.org/whatwedo/publication/global_corruption_barometer_people_and_corruption_latin_america_and_the_car.

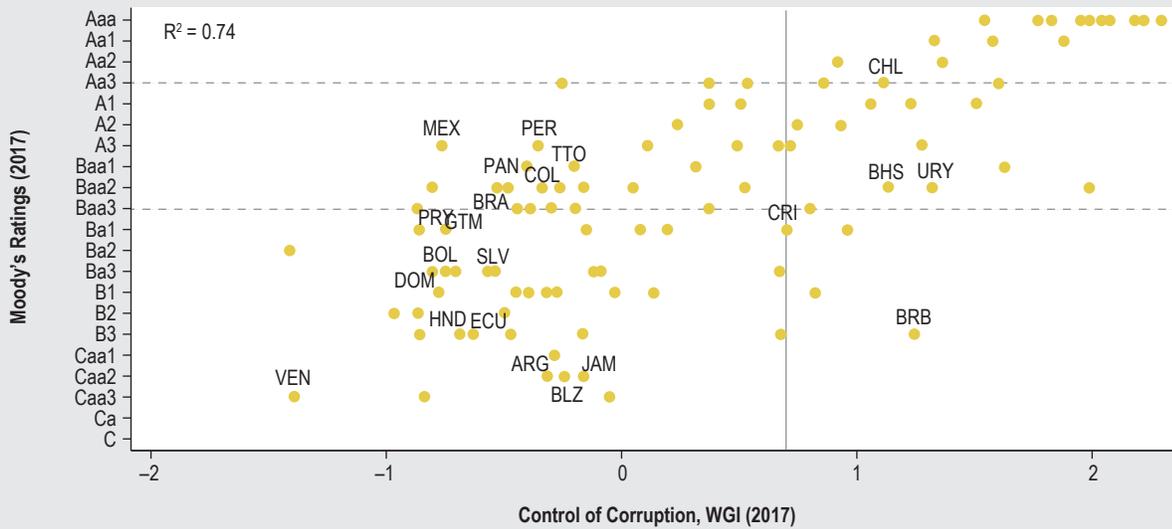
⁴ See generally K. Casas-Zamora and M. Carter, *Beyond the Scandals: The Changing Context of Corruption in Latin America*, Inter-American Dialogue Rule of Law Report (February 2017), pp. 33–34, available at http://www.thedialogue.org/wp-content/uploads/2017/02/Corruption-in-Latin-America_ROL_Report_FINAL_web-PDF.pdf.

⁵ With particular focus on these issues in Latin America, see D. Kaufmann, *Corruption Matters*, 52.3 FINANCE & DEVELOPMENT 20–23, International Monetary Fund (Sept. 2015), available at <http://www.imf.org/external/pubs/ft/fandd/2015/09/pdf/kaufmann.pdf>.

⁶ See, for example, P. Palacios, *Hay 60 mil trabajadores despedidos por causa Odebrecht*, LA REPÚBLICA (March 4, 2018), available at <https://larepublica.pe/politica/1206155-hay-60-mil-trabajadores-despedidos-por-causa-odebrecht>.

⁷ For a detailed analysis, see U. Panizza, *The Use of Corruption Indicators in Sovereign Ratings*, IDB Technical Note IDB-TN-1318 (October 2017), available at <https://publications.iadb.org/handle/11319/8562>.

Figure 2: Relationship between Moody's Sovereign Ratings and the Worldwide Governance Indicators Corruption Control Indicator (2017)



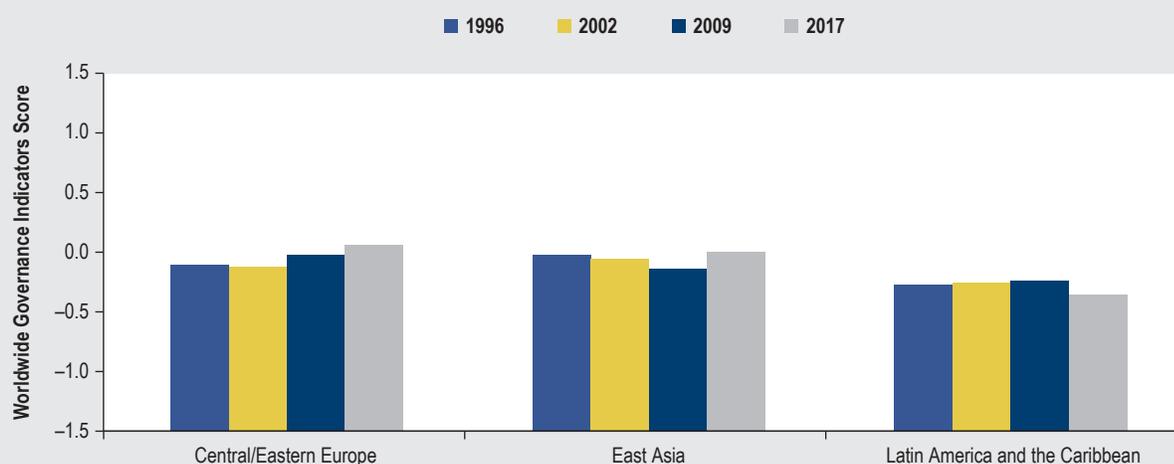
Source: Elaborated by U. Panizza, based on "The Use of Corruption Indicators in Sovereign Ratings"; Worldwide Governance Indicators (www.govindicators.org), 2017 Update.

Are Latin America and the Caribbean Ready for these Challenges?

The data are clear that corruption is not in retreat in the LAC region. Indeed, its modes and mechanisms are getting more complex. The region's governance systems are still not prepared to meet these challenges. Latin America's average score is below the world median in all governance indicators except voice and accountability, which barely tops the median.⁸ It rates particularly

poorly on (implementation of) the rule of law. On personal security and common crime, the region is at the very bottom. Latin America's governance quality trailed that of other predominantly middle-income regions. Unsurprisingly, then, the LAC region also lags behind its income peers in control of corruption, and it appears to be falling further behind over time (Figure 3).

Figure 3: Corruption Control Trends Across Regions

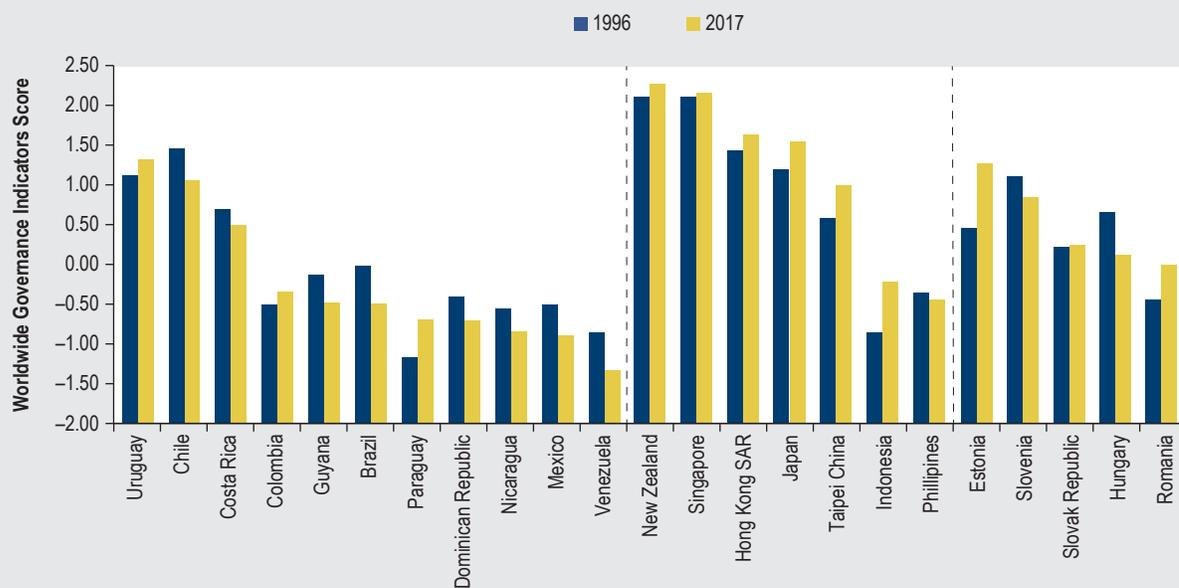


Source: Worldwide Governance Indicators (www.govindicators.org), 2017 Update.

Note: Countries with population over 1m. included in the calculations.

⁸ Data based on the Worldwide Governance Indicators (WGI), available from 1996–2016. See <http://info.worldbank.org/governance/wgi/index.aspx#home>. Calculations shown here include all countries in Latin America and the Caribbean with a population of over 1m. inhabitants. Margins of error apply. For methodological details, see D. Kaufmann, A. Kraay and M. Mastruzzi, The Worldwide Governance Indicators: Methodology and Analytical Issues, World Bank Policy Research Working Paper No. 5430, available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1682130##.

Figure 4: Control of Corruption: Trends: Selected Latin American and Caribbean, East Asian, and Eastern European Countries - WGI 1996, 2017



Source: Worldwide Governance Indicators (WGI) (www.govindicators.org), 2017 Update.

Important variations across countries exist (Figure 4), yet overall, the region accounts for proportionally more underperformers. Nonetheless, countries like Chile, Costa Rica, and Uruguay, which score highly on governance and corruption control, as well as Colombia and Paraguay (and Uruguay), which have improved substantially on that measure, illustrate that

good governance performance is attainable in the region. Further paths forward are suggested by the growing recognition in some countries of the need to improve in key areas such as rule of law, as exemplified by the progress underway in Brazil over the past decade in terms of new tools to address corruption investigations and curb impunity.

Time for Systemic Transformation

4

Recent scandals make it clear that corruption must be countered through political, institutional, and legal reform that enhances deterrence and ends impunity for the politically connected. Though some LAC countries, along with the IDB, have been engaged in selected anti-corruption reforms for the last decade, these have been uneven, partial, and focused more on enacting laws and regulations rather than implementation, more on principles and pronouncements than concrete practices.

A bolder approach to address corruption that engages civil servants, business, civil society, and individuals is warranted to generate the systemic shock needed to overcome the crisis of confidence among citizens and investors and strengthen democratic culture. Governments need to respond to citizen discontent and investor anxiety by making structural reforms in procurement and campaign finance. More transparency about government contracts, budgets, and conflict of interest, as well as innovative IT tools, can be helpful, but they are not sufficient to deal with the cases at hand. In addition

to a proactive approach to disclosure, the criminal justice system needs reform to deal with and deter elite capture of high-level government decision makers and politicians, as well as corporate malfeasance more generally. Countries could explore innovative solutions regarding settlements, including plea bargaining and transnational cooperation, which have the potential to speed up case resolution. Any of these reforms, taken alone, would constitute a step in the right direction. However, without an integrated approach and a systemic shock, they would be insufficient to produce lasting change.

A systemic approach must aim to be comprehensive—not covering every possible measure—but encompassing the key, interrelated pillars likely to make a major difference. Reforms ought to span both the supply and demand sides of corruption and engage the private and public sectors. Any meaningful plan must incorporate both ‘grand’ corruption (including elite capture by powerful vested interests and corruption in politics) and the day-to-day payoffs solicited from ordinary people and small businesses.

Four Pillars of a Systemic Reform Compact

5

Corruption scandals open windows of opportunity for systemic governance reform, as crucial actors temporarily lose their veto power. Seizing this opportunity requires bold and credible leaders with integrity (throughout government and society, not only in the executive). It also requires the support of external actors that can contribute to the credibility of the reform process. The IDB can play a very important role in this capacity.

Programmatic responses to corruption in LAC countries, ranging from the “macro-aggregate” level to the “micro-institutional” level, can be organized under four pillars that integrate the key actors and stakeholders, namely: (1) regional and global initiatives, (2) domestic initiatives, (3) engaging the private sector and civil society, and (4) the support of the IDB and other international organizations. This four-pronged approach is designed not only to be mutually reinforcing but also to attract the commitment and skills of the full range of actors who can and should contribute to this effort. This integrated agenda, if embraced in full, can create mutual commitments and enhance trust, with each set of contributors pledging to do their part.

Pillar 1: Global and Regional Initiatives

Regional and global initiatives coordinate responses and set up collaborative mechanisms to deal with common problems beyond the nation state, such as money laundering, beneficial ownership and shell companies, virtual currencies, extradition, cooperation on law-enforcement (including settlement and

sanctioning mechanisms), regional peer review, and anti-corruption benchmarking.

The LAC region led the world in international cooperation against corruption with the adoption of the Inter-American Convention against Corruption in 1996. Most LAC countries are signatories of the United Nations Convention against Corruption (UNCAC). Several of the largest economies in the region have also signed onto the Organisation for Economic Co-operation and Development (OECD) Convention on Combating Bribery of Foreign Public Officials in International Business Transactions. Through a range of additional agreements and standards that followed, LAC countries now participate in a network of international commitments on the inter-related issues of corruption, money laundering, and harmful tax practices, such as the Financial Action Task Force’s International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation. Most countries have also adopted the OECD Standards related to tax information exchange.

These agreements and standards pave the way for international cooperation to investigate corruption and related offenses in an era of transnational finance and transnational crimes. At the same time, they create incentives for improved performance, as markets and financial actors increasingly pay attention to the reports issued by international standard bearers, such as the Financial Action Task Force (FATF) or the Global Forum on Transparency and Exchange of Information for Tax Purposes (Global Forum). Most of them also propose specific preventive policies, on

such issues as public integrity, public procurement, and access to information.

Although progress has been made to meet the formal requirements of these international agreements, the key challenge now is *implementation*. Capacity constraints, electoral cycles, and political resistance are among the factors that have impeded full operationalization of global and regional commitments. The judicial branch plays a key role in this regard, in terms of both implementation and enforcement. Long processes, lack of sanctions enforcement, and inefficiency of prosecutors in the search for evidence lead to impunity. Some countries have set up a special anti-corruption authority, such as the International Commission against impunity in Guatemala⁹ or the Mission to Support the Fight Against Corruption and Impunity in Honduras. While tailoring the specific measures to country specifics is important, it is essential to strengthen the judiciary and public prosecutors' offices to ensure that they include these core elements: independence, resources (technical, human and economic), and power (legal tools and authority). In addition, procedural rules should be adapted to facilitate investigations and prosecutions, since globalization and technology have modified the nature of corruption cases, which now have a broader geographic outreach and more sophisticated schemes. At the same time as law enforcement becomes more efficient and streamlined, the rights of the accused must be protected to lend credibility to the anti-corruption effort. Defendants may see a "witch hunt"; prosecutors and judges must be able to defend their impartiality and competence.

Compromised domestic law enforcement and judicial authorities weaken the region's ability to respond to the increasingly cross-national challenges of corruption, money laundering, and tax evasion. They also make the job harder for those prosecutors and judges who have demonstrated extraordinary progress in major cases. Domestic law enforcement is frequently hampered by the challenges of

international cooperation: spontaneous cooperation by foreign countries is usually rare.

Typically, LAC countries following up on corrupt officials must resort to cumbersome mutual legal assistance procedures. Financial centers in the Global North (e.g., Luxembourg, Lichtenstein, Switzerland, and the United Kingdom) allow for several layers of appeals, causing slow and complex procedures. Mutual legal assistance is inefficient due to both technical and political challenges. Moreover, ancillary authorities, such as financial intelligence units, are frequently not cooperating in an optimal manner. There are cases where, even after all legal requirements have been met, the recovery of stolen assets has been postponed by financial centers in the North for political reasons. Here the IDB could play a vital role in mediating between international financial centers and LAC countries. This mediation could take place on a case-by-case basis or, better still, in a more general way.

The challenges of international cooperation are exacerbated by those jurisdictions known for their opacity and their near total lack of cooperation. Recent regional and worldwide corruption scandals have shown how offshore hubs and tax haven jurisdictions can facilitate the illicit flow of money and the way in which shell companies can be used for money laundering purposes. Some of these countries are located in the Caribbean area. Typically, though, the actual account management does not happen at the place of incorporation (e.g., the British Virgin Islands or Panama), but rather in the large international financial centers of the North (Luxembourg, Switzerland, or the United Kingdom). The web of opacity that has been termed the "shadow economy"¹⁰ urgently needs to be tackled worldwide. Here the initiative of the United Kingdom to force its overseas territories and Crown dependencies to identify beneficial owners is an urgent step in the right direction. The approach should, however, be made a general requirement on a worldwide basis.

⁹ Recently, President Jimmy Morales announced that the Government of Guatemala will not request the renewal of the mandate of the Commission, an institution that has been working in Guatemala since 2007 achieving important results in prosecuting high-level corruption cases. Morales' decision represents an important step backward against transparency, integrity, and anti-corruption, not only in Guatemala but also across the region. See Transparency International Secretariat, Transparency International Condemns President Morales' Attempt to Stop Anti-Corruption Fight, Transparency International (September 1, 2018), available at https://www.transparency.org/news/pressrelease/transparency_international_condemns_morales_attempt_to_stop_corruption. The official statement <http://www.minex.gob.gt/Noticias/Noticia.aspx?ID=27939>.

¹⁰ J.E. Stiglitz and M. Pieth, *Overcoming the Shadow Economy*, Friedrich Ebert Stiftung (2016), available at <https://www.baselgovernance.org/publications/1819>.

Regional initiatives to complement LAC countries' participation in global frameworks should focus on all these issues. In particular:

- Close remaining gaps in legal alignment with the key agreements, such as corporate criminal liability or equivalent norms in administrative law. States that are lagging behind will face monitoring by international organizations like FATF or the OECD Working Group on Bribery.
- In all resource-relevant LAC countries, implement the transparency and accountability standards for natural resources of the EITI. Further, mainstream such transparency standards into government and industry systems across the region.
- Introduce international procurement standards, set out in the UNCAC (Article 9) and principles articulated by the Construction Sector Transparency (CoST) initiative.¹¹
- Establish registries of ultimate beneficial ownership in every country to facilitate information sharing on tax and money laundering cases. The region's record of compliance with FATF and Global Forum standards is uneven¹² and needs to be addressed.
- Implement local and international information-sharing procedures to detect corruption and money laundering activities, ensuring reciprocity, cooperation, and coordination among relevant agencies and jurisdictions.
- Pass procedural and substantive regulations to facilitate investigations and prosecutions, incorporating laws on whistleblower protection, plea bargaining, settlement rules, forfeiture of illegal profits and proceeds, and extension of statute of limitations provisions for corruption cases.
- Restrict special fora protection, which allows public officials to avoid ordinary procedures.
- Create regional networks and standards for the selection, payment, and ethical and independent behavior of judicial personnel. This effort would require building capacity and reducing political constraints (including addressing internal corruption) across the region.

¹¹ See www.constructiontransparency.org.

¹² See A. Knobel, Regulation of Beneficial Owners in Latin America and the Caribbean, IDB Technical Note IDB-TN-1341, available at <https://publications.iadb.org/handle/11319/8646>.

¹³ Peru and Colombia, for example, have had to introduce new regulations to face the consequences arising from corruption cases on major infrastructure projects.

Pillar 2: Domestic Initiatives

Regional initiatives pave the way for necessary international cooperation, but LAC countries also need to take on a reinvigorated and expanded anti-corruption agenda *at home*. Based on our experience, action is needed in several key areas. These include a multi-faceted expansion of financial and governmental transparency; a reassertion of public-minded management of public resources, procurement, and contracts; a radical transformation of political finance; a step-change in the availability and use of technology to address corruption and improve governance; and finally, a frank recognition of the breadth and depth of both state capture and petty corruption and a renewed effort to address them through all the measures listed here, and more.

Public Procurement: Infrastructure and Contract Renegotiations

As discussed above, several LAC countries are facing a deceleration in the financing of large infrastructure projects from energy to transportation that are critical to the region's economic development.¹³ Countries should redouble their efforts to meet these standards, restore trust, and attract high-quality and high-impact investments. Recent cases reveal that bid rigging, biased scoring rules in contract assignment, and especially ex-post contract renegotiations play a major role in facilitating corrupt deals.

Assigning infrastructure contracts via competitive auctions will contribute little to avoiding cost overruns and corruption if they are later renegotiated to the winner's advantage. To address the most common reasons for contract renegotiations and reduce corruption more generally, infrastructure procurement systems, both regarding public provision and public-private partnerships (concessions) should be realigned to:

- Focus on defining problems to be solved and services to be provided, articulating measurable outcomes for both, rather than infrastructure to be built and inputs to be acquired. This

increases accountability, reduces renegotiations, and increases opportunities for innovation.

- Establish institutional and regulatory frameworks to effectively implement an e-procurement system aimed at ensuring transparency, integrity, competition, and access to information.
- Adopt standardized bidding frameworks and documents that preclude the exclusion of relevant competitors.
- Publish all contract changes in timely fashion and in the same place where the original contracts are published.
- Require competition for significant new investments resulting from contract renegotiations.
- Provide incentives and protection for whistleblowers to come forward with information on corrupt deals in infrastructure.
- Prohibit “financial equilibrium clauses” in public-private partnership legislation and contracts,¹⁴ as these have been a major reason for opportunistic renegotiations, with high efficiency costs and recurrent government bailouts of poorly managed firms.
- Plan and bid complete public-private partnership infrastructure projects following a careful and detailed evaluation process of the social costs and benefits, as well as design, operation, and expected outputs of the project, among others.
- Separate infrastructure planning bodies from the units in charge of contract compliance, to break conflicts of interest between promoting new investment and enforcing existing contracts.
- Use independent technical review panels to mediate conflicts and review any contract renegotiations.
- Treat investments in infrastructure via public provision and public-private partnerships in the same way for fiscal accounting purposes, since their dynamic impact on the budget is the same.¹⁵ Likewise, public-private partnerships should be subject to the same scrutiny in the budgetary process as public infrastructure projects.

As mentioned before, many if not all of the above measures should be part of a major revamping of the

governance of the infrastructure sector, incorporating the many lessons learned from the Lava Jato and related cases.

Management of Public Resources and Governance of Natural Resources

Countries rich in natural resources face a heightened risk of corruption and elite capture. The enormity of the stakes associated with oil (as well as mineral) wealth in particular can easily pervert incentives, public and private institutions, and political leaders. Further, as starkly illustrated by the Lava Jato scandal, in today’s interconnected world, where transnational elites and corporations exert undue regional and global influence, such corruption and capture risks transcend the borders of any single country and involve private and public sector actors. In resource-rich countries, the extractive industries have many links to other sectors of the economy. Consequently, governance challenges and corruption are not confined to one sector; they pose a nation-wide development and sustainable growth challenge with dire macroeconomic costs.

To respond to this challenge, it is important to embark on a strategy to improve governance in resource-rich countries, which considers the particularities of such countries, its natural resource endowments (e.g., whether the country is oil or mining-rich does matter), its polity and institutional features. The following elements need to be considered in such country strategies:

- *Toward a new sustained growth strategy in resource-relevant countries.* The political window offered by the downturn in commodity prices, the tendency in some governments to have a “race-to-the-bottom” to attract investments, and the recent corruption scandals offer an opportunity for a strategic reset. Priority should be given to promoting, designing, and implementing a broad-based medium-term good governance strategy aimed at leveraging the resources from extractives to strengthen national institutions and diversify the economy. Such strategies need to be participatory, empowering decentralized

¹⁴ Such clauses mandate that any judicial, administrative, or legal action by government that affects the firm’s income must be compensated.

¹⁵ For more details, see E. Engel, R. Fischer, and A. Galetovic, *The Economics of Public-Private Partnerships: A Basic Guide*, Chapter 6 (Cambridge University Press, 2014).

actors and communities and integrating a sustainable territorial governance focus.

- *Country-based systematic assessment of the governance and corruption vulnerabilities across the natural resource decision chain.* A framework such as the Natural Resource Charter,¹⁶ and its benchmarking diagnostic tool, permits an analysis of the particular risks of corruption in each stage of the natural resource value and decision-making chain. This starts from the upstream (decision to extract, licensing for exploration and production, etc.), via the mid-stream (governments getting a good deal from the companies, revenue management, etc.), onto the downstream (revenue sharing, converting natural resources into development gains for all). Such an approach can ensure that country characteristics are fully taken into account, implying that the priorities in action programs and strategies will vary from one country to another.
- *Reforming state-owned enterprises (SOEs) in extractives industries.* While some SOEs in the region are well governed and managed, reforming many SOEs—including in Brazil, Ecuador, Mexico, and Venezuela, among others—is still pending. Specifically, reform programs to enhance SOE compliance, transparency, and integrity is required, as well as streamlining of their remit, and de-politicizing management, corporate governance, meritocratic recruitment, and promotion.¹⁷
- *Strengthening subnational institutions and environmental standards and mitigating social conflict.* Institutions and mechanisms at the subnational level need to be strengthened. These include innovative and participatory approaches

to address social conflicts around extractives that have been implemented in countries such as Colombia and Peru. Revenue-sharing mechanisms between the center and localities need to be improved, and implementation of environmental standards, particularly weak at the subnational level, need to be strengthened. In this context, it is important to protect and facilitate due diligence efforts by all stakeholders to assess and address social and environmental impacts along the supply chain and during the life-span of an extractives project. In this context, it is appropriate to draw on national and subnational management and sustainability approaches that emerge from a territorial governance perspective. Rigorous empirical cost-benefit tools should also be employed.

- *Enhancing transparency and accountability in the extractive industries sector.* LAC countries should implement the EITI, which has become a global standard to promote transparency and good governance in the sector. The EITI is a powerful entry-level vehicle to introduce the mechanisms for deeper institutional reforms in the extractive sector. This is particularly the case with the recently expanded EITI standard, which goes well beyond the disclosure of revenue payments and *inter alia* also addresses governance challenges around disclosures of beneficiary owners and of contracts. Currently nine LAC countries are implementing EITI, others are in the process of becoming members,¹⁸ and still others could also join this effort. Equally important is to move beyond the EITI national agencies to encourage the integration of these transparency and disclosure standards into broader governmental

¹⁶ The Natural Resource Charter is a set of principles to guide governments and societies in the use of natural resources so that the economic opportunities yield maximum and sustained returns for the citizens. It outlines tools and policy options designed to avoid the mismanagement of diminishing natural riches and ensure their ongoing benefits. The charter is organized around 12 core precepts offering guidance on key decisions governments face. Each precept along the value and decision chain can offer a window to assess the particular corruption risks associated with that topic and value chain stage. See Natural Resource Governance Institute, *The Natural Resource Charter* (2nd Edition, 2014), available at <https://resourcegovernance.org/approach/natural-resource-charter>. See also Natural Resource Governance Institute, *Natural Resource Charter Benchmarking Framework* (2017), available at <https://resourcegovernance.org/analysis-tools/tools/natural-resource-charter-benchmarking-framework>.

¹⁷ Countries might adopt standards like the Transparency International 10 Anti-Corruption Principles for State-Owned Enterprises. See Transparency International, *10 Anti-corruption Principles for State-Owned Enterprises*, available at https://www.transparency.org/whatwedo/publication/10_anti_corruption_principles_for_state_owned_enterprises. See also Heller, P. et al., *Reforming National Oil Companies: Nine Recommendations*. Natural Resource Governance Institute (2014), available at https://resourcegovernance.org/sites/default/files/documents/nrgi_9recs_eng_v3.pdf.

¹⁸ Colombia, Dominican Republic, Guatemala, Guyana, Honduras, Mexico, Perú, Suriname, Trinidad and Tobago are already implementing countries. Other regional countries such as Argentina and Ecuador have expressed their commitment to join EITI.

and industry systems and mechanisms (e.g., to mainstream EITI reforms, such as the ongoing transparency reforms of Mexico's own oil regulatory commission, the Comisión Nacional de Hidrocarburos). For this mainstreaming purpose, wider use of e-governance tools, such as the IDB-supported Mapa Regalías in Colombia,¹⁹ is also warranted.

- *Improved governance and efficacy of sovereign wealth funds, including stabilization and inter-generational development funds.* Pre-conditions for setting up sovereign funds and similar funds will vary across countries. Where they exist, the governance structures can generally be strengthened,²⁰ and more broadly the overall fiscal systems associated with revenues and expenditures from extractives should be made more resilient to corruption risks.
- *Complementary reforms.* Due to the nature of corruption in natural resource-rich countries, reforms within the extractives sector, such as those suggested here, must be complemented by reform of procurement and subcontracting, political finance, and financial transparency. These fundamental reforms also apply to countries that are not rich in natural resources. They are addressed in more detail in the following sections.
- *Special focus on governance and anticorruption in new oil-producing countries.* In a new oil-producing country, such as Guyana,²¹ the discovery has enormous national governance and development implications which transcend the extractives sector. In such countries, the

opportunity for resources to be wholly transformative is present, as is the prospect of corruption, capture, and mis-governance leading to a resource curse. These countries require special attention and support to ensure that transparent institutions and policies governing licensing, contracting, procurement, and revenue management are put in place, capacities are built, and incentives to prevent malfeasance are adopted and enforced.

Political Finance

The consolidation and stability of democracy and competitive electoral processes in the LAC region has had the unwanted effect of opening a window for corruption in and through political financing. Globalization and new technologies have facilitated the circulation of funds and have made it more difficult for national electoral management bodies (EMBs) to follow the money and monitor the origin of political contributions. In addition, in some settings political finance is increasingly coming from organized crime groups, many of which have changed their strategy of political control from financing presidential campaigns to financing local candidates.²²

While political finance has enlarged the playing field especially for grand corruption and state capture, recent scandals involving political financing have also produced unprecedented consequences. They have resulted in investigations of public officials and business executives conducted not by EMBs but by ordinary tribunals. Robust social mobilization against political finance corruption provided crucial support

¹⁹ See <http://maparegalias.sgr.gov.co>.

²⁰ A good governance structure covers and should set the following: a clear fund objective, fiscal rules for deposit and withdrawal, investment rules, ethical and conflict of interest standards while defining responsibilities between authorities and managers, and an independent oversight bodies. See Andrew Bauer et. al., *Managing the public trust: How to make natural resource funds work for citizens*, Revenue Watch Institute and Vale Columbia Center (2014), available at https://resource-governance.org/sites/default/files/NRF_RWI_Complete_Report_EN.pdf.

²¹ Guyana faces the challenge to overcome a potential resource curse, often associated with major governance failures and systemic corruption, ever since the recent massive oil reserve findings in its territory by ExxonMobil. This first discovery is expected to start producing oil in 2020, and its production could scale up to 500,000 barrels a day over a decade (See C. Krauss, *The \$20 Billion Question for Guayana*, *The New York Times*, July 20, 2018). According to some calculations from OpenOil, the government take (or average effective tax rate) from the contract with Exxon is lower than the rate from oil contracts in comparable countries (J. West, *Guyana's Oil Deal is Outlier Low: Government Takes Just Over Half*, Open Oil, March 15, 2018), and the IMF has also found that the contract was not optimal for Guyana (K. Crowley, *Exxon Sparks IMF Concern With Weighty Returns in Tiny Guyana*, *Bloomberg*, April 9, 2018). Further public debate is needed, with full disclosure of all contractual information, to determine the appropriate steps for Guyana regarding these arrangements, the optimal tax and royalty scheme, as well as in ensuring a pro-development and corruption-free use of the massive upcoming resources from oil.

²² F. Dews, *Political Finance and Organized Crime in Latin America*, *Brookings Now* (October 16, 2013), available at <https://www.brookings.edu/blog/brookings-now/2013/10/16/political-finance-and-organized-crime-in-latin-america/>.

to reformist judges and prosecutors. These demonstrations also resulted in the resignation of elected authorities (Guatemala and Honduras) and the repeal of legislative decisions (Guatemala).

LAC countries need to take advantage of this moment to make meaningful reforms that do not just change the rules of political finance but change the balance of powers and skills between regulators and those who wish to evade political finance controls. This requires the following:

- Strengthening the hand of EMBs, judges, and prosecutors not only by assuring the necessary independence, resources, and authorities, but also giving them access to the information and investigations of agencies responsible for money laundering and corruption, including international cooperation arrangements. This access should be mandated by law.
- Greater control over private funding, including bans on anonymous contributions and financing from foreign sources, and limits on contributions from legal entities.
- A public subsidy system for campaigns in countries not already providing public funding. This should be designed to avoid favoring incumbents. Furthermore, legislation should move toward a substantial component of public funding, both for political parties and for campaigns, designed so as to reflect citizens' political preferences.
- Controls to limit campaign spending, such as limits on the length of campaigns, spending caps, and facilitating airtime on public and private television for candidates and parties. These measures should be coupled with controls on using public funds and other resources by incumbents during campaigns.
- Enhancing the transparency of contributions to and from all relevant actors, including candidates, corporations, political foundations, non-governmental organizations (NGOs), and associations linked with candidates or parties. Effective monitoring must also apply to public funds.

- Greater attention to political finance at sub-national levels. Improved legal frameworks to expand the range of penalties beyond fines (e.g., prohibiting participation in public tenders) and *inter alia* applying them to financial officials and to those making illegal contributions.
- Enhanced use of technology to make information on political contributions available to citizens, journalists, and researchers; create channels to denounce corruption cases with appropriate protection for whistleblowers; and assist EMBs in monitoring political finance and exchanging information with other agencies and jurisdictions.

Financial Transparency

Financial transparency is recognized as a key building block of an effective anti-corruption system, particularly to prevent individuals involved in corruption, fraud, embezzlement, tax evasion, and other illegal activities from enjoying the proceeds of their crimes. The international cooperation outlined under Pillar 1, combined with anti-bribery and anti-money laundering laws in a number of major economies, is driving financial transparency developments in LAC countries. It is also highlighting the costs, such as the actions associated with bank de-risking, for countries that have not kept up.²³

As previously noted, countries are adopting international financial transparency standards in law, though implementation is not consistent. Most of the domestic actions required echo the priorities of our regional pillar, including the following:

- Complying with international standards, including open contracting and the use of the Global Legal Entity Identifier.²⁴
- Establishing and publishing a registry of ultimate beneficial ownership of all corporate entities and similar legal vehicles including trusts, adopting effective sanctions for untruthful registration.
- Linking financial and regulatory compliance information sources within a country so that all authorities (including electoral authorities) have

²³ Particularly in island countries of the Caribbean and smaller countries of Central America, international banks have withdrawn correspondent banking relations due to the real or perceived level of money laundering risk posed by certain jurisdictional and business volume considerations. In this regard, see, for example, G.M. Vásquez, Assessing the Impact of the De-risking on Remittances and Trade Finance in Belize, IDB Discussion Paper IDB-DP-558, available at <https://publications.iadb.org/handle/11319/8702#sthash.PBAGVFQ0.dpuf>.

²⁴ See <https://www.gleif.org/en/>.

access to all the information on a single entity. This can be done without combining databases, by providing access across systems to a range of authorized users.²⁵

- Upgrading technological capacities, not only technical infrastructure but innovation skills, of relevant agencies so that they can process the enormous amounts of data on, for example, suspicious transactions, and prepare for new opportunities such as blockchain technology.
- Investing in and supporting those outside government, especially in academia and civil society, to scrutinize government data and propose improvements.

Here we highlight the importance of information on beneficial ownership. Not only is it essential for national and international anti-money laundering and combating the financing of terrorism (AML/CFT) and anti-corruption efforts; it also has salutary effects for companies seeking to avoid legal violations and business risks.

Public Integrity

Conflicts of interest—the overlapping of public responsibilities and private interests—lie at the core of Latin America’s interconnected networks of political, business, and social elites. Conflict of interest is a broad umbrella term that incorporates all sorts of tensions between official and private roles. Not all conflicts result in corruption, yet in many countries they are associated with corruption and even in the more extreme manifestations of regulatory and state capture (see below). Consequently, revealing and regulating conflicts of interest is important for re-establishing the public trust in government that has waned so significantly across the region.

The capture of the state by powerful private, and even criminal, interests operates in part by populating government with officials who also have family or professional linkages to those outside roles. Cross-country results show a correlation between the political connections of business firms and corruption,

and firm value rises if a businessperson enters politics,²⁶ suggesting a confusion of roles.

However, criminal law is too blunt and accusatory an instrument for most conflict of interest cases, except where conflicts result in illegal actions. Reforms should instead seek to balance the risk of conflicts against the need to attract qualified people into government service. These include the following:

- Disclosure of and public access to the financial dealings of politicians and other officials.
- Preventive legal rules that require officials either to divest themselves and their families of certain financial interests or to recuse themselves from taking part in the decision-making process where they have a conflict.
- An independent body to enforce disclosure and recusal requirements in a way that can force the resignation or reassignment of offending officials and review challenges to the rules.
- Ethics training, background checks prior to appointments, pre and post-employment regulations, mechanisms to report wrongdoing and protect whistleblowers, and the creation of blind trusts for managing the assets of high-ranking public officials.²⁷

Open Government and Administrative Simplification

With the middle class now the largest portion of the region’s population, public expectations are shifting toward greater participation in governance and better and more accessible public services. The very poor may have given up on receiving honest services from the state, but even those groups can now expect a better functioning government. Access to information is slowly improving, but access is not sufficient if people do not have legitimate channels to influence and participate in governance individually or collectively. In this age of communication, open government is an essential ingredient not only for transparency and accountability, but also for establishing trust and constructive interaction between citizens, businesses, and the state.²⁸

²⁵ In this area, data bases should follow applicable international standards that require standardization, completeness, updated, curated, interoperability, reusability, and other relevant features for information.

²⁶ M. Facio, Politically Connected Firms, *American Economic Review*, 96 .1: 369–386 (2006).

²⁷ See Americas Business Dialogue, Action for Growth: Policy Recommendations and 2018–2021 Action Plan for Growth in the Americas, Facilitated by IDB (2018), available at <http://americasbd.org/en/report/>.

²⁸ In this regard, see B. Roseth, A. Reyes, and C. Santiso, Wait No More: Citizens, Red Tape, and Digital Government (IDB, 2018), available at <https://publications.iadb.org/handle/11319/8930#sthash.qL3vgXgZ.dpuf>.

To meet these expectations, governments must make their processes and services simpler and more accessible. Information technology provides the means for increasingly tech-savvy populations to achieve their goals most effectively. In turn, administrative simplification is necessary to make technological solutions workable, as well as to improve efficiency and reduce opportunities for corruption. This is a win-win for governments, as digital governance has most often been associated with reduced corruption. To achieve this next step toward effective and accountable governance, countries should take the following steps:

- Implement digital systems allowing citizens to channel their requests online.
- Establish, where they do not already exist, accessible open data portals containing current, complete and reusable information.
- Standardize administrative processes and eliminate requirements, activities, and intermediaries that do not add value, to make processes more suitable for automation (and as a valuable anti-corruption action on its own).
- Adopt and implement standards established by the Open Government Partnership²⁹ and the OECD³⁰ on both open government and administrative simplification.

Information and Communication Technology

It is already clear from the foregoing that information technology and the increased availability of data are facilitating significant innovations in the fight against corruption. Countries that can take advantage of new technology have great possibilities to improve their anti-corruption results and re-build faith in government.

²⁹ See <https://www.opengovpartnership.org/>.

³⁰ See Administrative Simplification and Reducing Burdens, OECD, available at <http://www.oecd.org/gov/regulatory-policy/administrative-simplification.htm>. See also D. Charité et al. International Standard Cost Model Manual: Measuring and Reducing administrative burdens for Business, International SCM Network (2005), available at <http://www.oecd.org/gov/regulatory-policy/34227698.pdf>.

³¹ In this regard, see A. Bhattacharya, Blockchain is helping build a new Indian city, but it's no cure for corruption, Quartz India (July 17, 2018), available at <https://qz.com/india/1325423/indias-andhra-state-is-using-blockchain-to-build-capital-am-aravati/>; C. Bishop, Blockchain Slashes US Govt. Contract Award Time From 100 To 10 Days, Legal Gambling and the Law (March 29, 2018), available at <https://www.legalgamblingandthelaw.com/news/blockchain-slashes-us-govt-contract-award-time-from-100-to-10-days/>; C. Santiso, Will Blockchain Disrupt Government Corruption?, Stanford Social Innovation Review (March 5, 2018), available at https://ssir.org/articles/entry/will_blockchain_disrupt_government_corruption. See also The GovLab, Blockchange <https://blockchan.ge/>.

³² The Open Up Guide is a good example of how to promote citizen involvement and feedback mechanisms concerning the use of open data to combat corruption in Mexico. See A. Echeverria, D. D'Herrera and R. Alanis, Open Up Guide: Testing How to Use Open Data to Combat Corruption in Mexico, Open Data Charter (January 2018), available at <https://drive.google.com/file/d/1de9WwYhUsgY8LJLnQmDJY3RyM2Lw1TN7/view>.

While they would need to be complemented by broader systemic reforms, there are some promising opportunities in utilizing information technology to address corruption. These include using open data to pinpoint and measure corruption, crowdsourcing corruption reports, initiatives in citizen reporting and employee whistleblowing, utilizing predictive analytics to identify corruption “red flags,” and harnessing distributed ledger (blockchain) technology that can create more secure and open procurement and contract management.

Distributed ledger technologies, of which blockchain is one example, when properly designed and governed, can store user identity and transaction information securely and openly. They have the potential to increase accountability, help fight against corruption, and facilitate both efficient tracking and tracing of transactions to prevent corruption in the first place.³¹

To take advantage of these opportunities, policies need to prioritize the following:

- Closing the gap between the scope and quality of currently available open data and the full range of data needed to combat corruption, such as comprehensive government contracting data pre- and post-bid, more “open justice” information about the process of prosecutions and trials, and open publication of citizen complaint data.³²
- Aggressively seeking public input, using multiple channels including web and mobile, but ensuring that citizen inputs, including complaints and whistleblowing reports, once received, are acted upon quickly and feedback provided.
- Building the infrastructure and access the skills to use advanced methods like predictive analytics.

- Investing in pilot projects to test the efficacy of blockchain in improving administration while preventing corruption.

As suggested, none of these possibilities is likely to bear fruit in isolation, without significant investment in revitalizing public institutions and in implementing broader political, regulatory and transparency reforms. In particular, weaker legacy institutions that lack infrastructure, capacity, and a culture of innovation will struggle to adapt. Thus, the focus on reforming and strengthening them is important.

However, while underlying distributed ledger technologies may be a tool to fight corruption, when used, for example, to make government databases more secure and transparent, cryptocurrency transactions rely on the same technology to facilitate illicit deals.³³ Cryptocurrencies, especially the anonymity and privacy of transactions, raise the specter of money laundering and spur the idea that technology will encourage corrupt activities.³⁴ Without knowing the individual's identity, information exchange agreements could become inapplicable for cryptocurrency transactions.

Coupled with the problem of anonymity, there is also a lack of uniformity among domestic legislation. Approaches to cryptocurrency market regulation vary widely.³⁵ Some countries have declared cryptocurrencies a form of commodity or capital asset for tax purposes.³⁶ Depending upon which country, cryptocurrency trades and exchanges shall be subject to income tax, sales tax, capital gains tax, and/or VAT.³⁷

To increase the transparency of the transactions, several nations began regulating cryptocurrency

exchange platforms through the application of anti-money-laundering laws (AML) and Know Your Client (KYC) rules.³⁸ Even with transparency regulations in place, it remains unclear whether cryptocurrency assets must be reported under the standards on automatic exchange information for tax purposes. This is evidenced by the fact that cryptocurrencies are not clearly defined under “financial assets” that must be reported if held in a foreign financial account.³⁹

Without a standardized approach to enforce the regulations above, the continued anonymity in cryptocurrency market exchanges may widely degrade financial reporting transparency between countries. Cryptocurrencies in and of themselves are not the problem. The lack of cohesion in the international regulations over cryptocurrency transactions may create loopholes and legal inaccuracies encouraging tax evasion, money laundering, and corrupt practices.

Policies to address international cooperation on cryptocurrencies regulation could include the following:

- Defining the legal nature of cryptocurrencies to determine (i) if these virtual currencies are money, digital money or another type of asset, and (ii) if they are capable to cancel payment obligations.
- Establishing mechanisms allowing enforcement agencies to track cryptocurrencies transactions. Such mechanisms could include the registration and licensing of service providers, the collection of personal information to make cryptocurrency operations non-anonymous, and the

³³ For a comprehensive discussion on this issue, see The Economist, Technology Quarterly: Cryptocurrencies and Blockchains, The Economist (September 1, 2018).

³⁴ In some jurisdictions, trading platforms can be easily set up, thus creating the possibility for investors to put their money into unaccountable, shady, and corrupt ventures.

³⁵ Italy and Japan, for instance, take a more progressive position, treating bitcoin as legal tender. In Italy, gain from all cryptocurrency transactions are exempt from VAT and in some cases, they are for income tax purposes. Japan declared bitcoin a legal tender and transactions are not subject to double taxation. Mexico recently passed legislation treating cryptocurrency as a virtual asset. On the other hand, China bans its financial institutions outright from using cryptocurrency. See Cryptocurrencies by Country, Thomson Reuters (October 25, 2017), available at <https://blogs.thomsonreuters.com/answerworld/world-cryptocurrencies-country/>.

³⁶ Ibid.

³⁷ Ibid.

³⁸ Ibid. See also European Parliament, On the proposal for a directive of the European Parliament and of the Council amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing and amending Directive 2009/101/EC, available at <http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+REPORT+A8-2017-0056+0+DOC+XML+V0//EN>.

³⁹ CRS-related Frequently Asked Questions, OECD (June 2018), available at <https://www.oecd.org/tax/exchange-of-tax-information/CRS-related-FAQs.pdf>.

potential disclosure of such information for suspicious transactions.

- Aligning institutional and governance models of cryptocurrencies and blockchains on both national and international levels.

Regarding anti-corruption and AML efforts, these ledger technologies, if properly applied, can be part of the answer. Yet lessons from their application still need to be drawn regarding these incipient technologies and at any rate they are unlikely to provide full solutions. Hence complementary actions will be needed. For instance, the approach that has been often taken regarding AML is not only concerned with traceability of transactions, which could be a potential strength of ledger technologies, but such traceability will not be helpful unless the underlying origin of the transaction can be located, whether using cash or any other mean of payment.

Addressing State Capture, Grand Corruption and Petty Corruption

The foregoing recommendations demonstrate that new opportunities to fight corruption are emerging in LAC countries, but alongside greater-than-ever urgency as populations become increasingly aware of the misdeeds of their leaders. The disconnect between the implied social contract of voting and paying taxes, on the one hand, and the evident violation of that contract when citizens seek services or read the news, on the other, is a recipe for the declining legitimacy of the democratic systems that have struggled into existence over the past decades. In this context, both the daily indignities of petty corruption and the increasingly frequent outrages of grand corruption present a renewed challenge. And as the stark evidence of recent scandals and events in the region demonstrate,

grand corruption and state capture have become ‘macro-critical’ in terms of their macroeconomic consequences.⁴⁰

Thus, we end our recommendations for domestic reforms with the serious matter of grand corruption and state capture, the latter referring to the undue influence by the powerful elite on the state laws, regulations, policies and allocation of public assets and resources for their private benefit at the expense of the public good.⁴¹ At times such undue business elite interests are furthered from within the political and governmental elite (“business in government”), where the extreme form of influencing takes place by business interests becoming part of government and the legislature, without effective conflict of interest restraints. And it is also noteworthy that the traditional private sector (and within it, large-scale industry and the financial sector) is often not the sole ‘captor’ of the rules of the game. In some settings some very powerful (and not broadly representative) unions exert undue influence (while many unions do not). In other places drug cartels and mafia play an even more nefarious role in this context.

State capture also has a role in influencing the legality of actions and decisions, which may be unethical and border in the corrupt, yet considered legal according to the laws prevailing in a country at a point in time. In this context, it can help influence the laws and regulations around lobbying, campaign finance, electoral rules, procurement, contracting and licensing in infrastructure, and financial sector regulation.

Importantly, the networked nature of the power elite in many countries means that the mechanisms of corruption can also operate in the opposite direction in terms of power dynamics: politicians or high-level officials exercising their influence to get private entities to do their

⁴⁰ Macro-criticality refers to factors that pose significant macro-economic risks for a country. It is a term recently subject to common use by International Financial Institutions such as the IMF, an organization which now regards corruption risks of critical importance for macro-economic stability and growth in key countries. See IMF, IMF Executive Board Approves New Framework for Enhanced Engagement on Governance, IMF Press Release No. 18/142 (April 22, 2018), available at <https://www.imf.org/en/News/Articles/2018/04/21/pr18142-imf-board-approves-new-framework-for-enhanced-engagement-on-governance>. Also, most recently, see J. Hellman and D. Kaufmann, State Capture in Transition, Submission to the South African Judicial Commission of Inquiry into Allegations of State Capture, Corruption and Fraud in the Public Sector including Organs of State (August 31, 2018), available at <https://www.sastatecapture.org.za/site/hearings/documents>.

⁴¹ For details on the notion of state capture, as originally applied to transition countries, see J. Hellman and D. Kaufmann, Confronting the Challenge of State Capture in Transition Economies, 38.3 Finance and Development (2001), available at <http://www.imf.org/external/pubs/ft/fandd/2001/09/hellman.htm>.

bidding, for example, by having undisclosed financial interests in firms participating in the bidding process. In other cases, collusion between the political and economic/financial elites alters the institutional rules of the game for the elite's own private benefit.⁴²

We have already presented several responses to state capture in other sections—most importantly, a major effort to increase the transparency and monitoring of political finance, along with establishing effective controls on large procurements and infrastructure contracts and revealing and regulating conflicts of interest in government. Shedding light on the ultimate beneficial owners of financial entities will support and reinforce these efforts. Taking on the challenges of state capture requires further steps out of the familiar realm of technical reforms, into the following areas:

- Increasing economic contestation by reducing obstacles to entry for small and medium enterprises, adopting and implementing anti-trust regulations, and implementing a simple and progressive tax system which minimizes discretion, exemptions and loopholes (which the powerful tend to exploit).
- Ensuring mechanisms for civic participation and robust and transparent political competition. In this context, to promote and protect civic space, media freedoms is key.
- Approving legislation and create institutions to regulate lobbying activity in LAC countries where such regulations are absent and strengthen existing regulations and implementation in most of the remaining countries. These regulations should provide easy access to information on lobbying activity, including meetings, topics addressed in meetings, identification of lobbyists and resources spent on lobbying.
- Countering revolving doors by establishing and implementing clear cooling off periods, full disclosure of financial assets and conflicts of interests, and recusal mechanisms.
- Instituting plea bargaining and related mechanisms that provide incentives for unmasking those engaged in grand corruption and capture (such as those utilized in Lava Jato).

Countries in Latin America and the Caribbean must also continue the work of reducing opportunities and incentives for petty corruption—as well as administrative corruption, which is often associated with such corruption, but it is not necessarily “petty”. This daily occurrence chips away at the forbearance of individual citizens, raises costs and produces inefficiencies for productive enterprises, and stifles innovation in public institutions. The policy formulas to reduce petty corruption are not new, encompassing reduction of red tape, substituting legal modes of paying for scarce services for illegal ones, limiting official discretion, and increasing oversight and enforcement. What is new is the critical sense that corruption has become the way of running government and interacting with the public rather than the exception. Alongside the institutional and technical upgrades required to analyze and use data, respond to increasingly engaged and demanding citizens, and be ever more agile in the face of cross-border challenges, these basic reforms, which have been widely advocated and specified for every country, must finally be implemented.

Pillar 3: Engaging the Private Sector and Civil Society

Governments will not be able to bring about systemic change on their own. The private sector has a business interest in improved transparency and in reducing the inefficiencies that corruption creates. Civil society has already established itself as an important force for transparency and accountability. Any vision for systemic transformation must include and promote the substantive contributions these stakeholders will make.

Private companies have made considerable efforts to prevent corruption by developing compliance programs. While compliance is by nature reactive to potential risk, in more recent times work on the more proactive concept of collective action is gaining ground. Traditionally, companies of the same industry have—under the title of collective action—developed common standards. In a later phase collective action was used to find a common voice of industry *vis-à-vis* regulators (e.g., the Wolfsberg Group on combating money

⁴² It is important to note that widespread petty corruption is often rooted in the models and incentives created at the top of the system, hence state capture and grand corruption tends to provide an enabling environment for loss of trust in institutions and petty corruption.

laundering).⁴³ Most recently collective action has been the basis for public-private-partnerships in fighting bribery: in the LAC region the so-called “High Level Reporting Mechanisms”⁴⁴ have emerged (e.g., in Colombia and Argentina, more recently under discussion also in Peru and Panama).

Countries interested in foreign investment have introduced a specialized business ombudsman, independent from law enforcement agencies and judiciary, but able to intervene in the case of solicitation and extortion for bribes.

After the latest corruption scandals, firms are also obliged to rebuild trust in their activity, because they are now under more legal and social pressure to conduct transparent and honest business dealings. Several of the proposals in other sections—such as bureaucratic simplification, procurement reform and financial transparency—are intended to facilitate and make more transparent private sector activities. Additionally, the following specific measures can be promoted *within the private sector*:

- Share the knowledge embodied in companies’ sophisticated risk management methodologies across the private sector, including the possibility of government or industry groups serving as platforms for information sharing, standard setting, and even peer certification.
- Foster cooperation with the public sector for the preparation of guidelines and regulations on corporate governance to ensure compliance with those regulations.
- Promote integrity policies for small and medium-sized enterprises (SMEs), using mentoring from larger firms within their supply chain, collective action and other similar strategies.⁴⁵

- Develop corporate ethics and whistleblowing programs, especially training, even if not required by law.⁴⁶ This could include reporting their anti-corruption plans and compliance with beneficial ownership legislation.
- Establish a private sector-union sector dialogue to ensure a common approach to ethical behavior and rejection of corrupt practices.
- Particularly in the banking sector, a critical gate keeper of legitimate business transactions, adhere not only to state-of-the-art regulations in prevention of money laundering, but also to the highest standards in ethical practices, including transparent financial information.
- Adopt sound corporate governance practices.

There has been exemplary work by Latin American civil society for transparency and public integrity. It ranges from successfully advocating for access to information laws, supporting innovative procurement transparency tools such as Integrity Pacts, monitoring budget execution, to establishing campaign finance and e-reporting tools. Further, initiatives have been conducted to mobilize and sustain support for anti-corruption champions who—often at high personal risk—undertake investigations and prosecutions.

Integrity Pacts can be a useful tool for preventing corruption. After grand corruption scandals and in view of the loss of trust in institutions and lack of credibility of governments, Integrity Pacts—with the intervention of a third party—offers a possible source of credibility for new contracts or the continuity of the previous ones.⁴⁷

Civil society in the region can also benefit from several of the recommended initiatives, including

⁴³ Wolfsberg Anti-Money Laundering Principles for Private Banking (2012), The Wolfsberg Group (2012), available at <https://www.wolfsberg-principles.com/sites/default/files/wb/pdfs/wolfsberg-standards/10.%20Wolfsberg-Private-Banking-Principles-May-2012.pdf>.

⁴⁴ Concept developed by the OECD in cooperation with the Basel Institute on Governance and Transparency International.

⁴⁵ See, for example, B20, Promoting Integrity by Creating Opportunities for Responsible Businesses, B20 Cross Thematic Group, available at <http://www.globalbusinesscoalition.org/wp-content/uploads/2017/05/b20-ctg-rbac-policy-paper.pdf>. See also initiatives from the Alliance for Integrity at <https://www.allianceforintegrity.org/en/alliance-for-integrity/about-us/>.

⁴⁶ These programs should regulate corporate governance (including issues arising from actions, policies, practices, and decisions of corporations, their agents, and other affected stakeholders), conflict of interests, disclosure of ultimate beneficial owners, the delivery of gifts and political contributions, among others.

⁴⁷ According to Transparency International, “[a]n Integrity Pact is both a signed document and approach to public contracting which commits a contracting authority and bidders to comply with best practice and maximum transparency. A third actor (generally civil society organization) monitors the process and commitments made. Monitors commit to maximum transparency and all monitoring reports and results are made available to the public on an ongoing basis.” These types of initiatives have been applied in over 15 countries and 300 separate situations, helping to save taxpayer money, ensure that infrastructure projects are delivered efficiently, and close off avenues for illicit gain. See Transparency International, Integrity Pacts, Tools, available at https://www.transparency.org/whatwedo/tools/integrity_pacts/5.

transparency and access to information and open government. They will be allies of any government that seriously commits to the political renewal required to take on the other challenges we have defined, most notably grand corruption and state capture. International organizations and governments should encourage and support civil society efforts and its participation in anti-corruption initiatives. LAC governments should enact statutes that make it simple and straightforward to register as a non-profit entity (e.g., charity or advocacy group), while these acts should also ascertain that such organizations are not be used as a “front” for corrupt purposes.

In the long term, education is crucially important in the fight against corruption. Education on civic values, integrity principles, and democratic culture is essential to build strong democratic communities. A solid integrity system is the result of the reconstruction of the lost basic social consensus about integrity principles and values which must guide the conduct of people both as private individuals and as social actors in the public or private sector. The sustainability of the social consensus demands ongoing investment in formal and informal education. Civic and integrity education should start at the elementary school level and be mainstreamed in primary and secondary school curricula.

Social reaction against corruption is central in the fight for transparency. This reaction will be stronger if citizens understand the value of the rule of law and integrity as moral and political principles. It is crucial that these values are culturally embedded in the young generations and inform citizens participation and political involvement. As recognized by the OECD, “building a culture of integrity in society necessarily begins with the education of young people. The knowledge, skills and behaviours they acquire now will shape their country’s future, and will help them uphold public integrity, which is essential for preventing corruption.”⁴⁸

Pillar 4: IDB’s Initiative and Leadership

Salient recommendations in this report are aligned with the mandate of a multilateral development

institution such as the IDB, which, thanks to its leadership, expertise, and resources, is well placed to be a major partner for the region in a much-needed scaling-up on anti-corruption.

- At the more general and strategic level, the IDB can take to the next level its support to governments on governance and transparency reforms and on anti-corruption programs. Some of its support and collaboration could incorporate other key actors engaged in governance and anti-corruption programs, including legislators, civil society, media, and think tanks. This is important because experience suggests that fighting corruption requires collective action via a multi-stakeholder approach. Lessons of experience point to failures in many programs that have focused only or mostly on the supply side of governance, such as technical assistance to ministries. The IDB and other regional and global organizations could do more to support and work with think tanks and NGOs that have significant expertise and credibility in this area. They could also help support and protect anti-corruption champions in their countries.

In this context, the IDB, partnering with other organizations, could play a major role assisting countries such as Peru, which, in the midst of a major political transition due to corruption, recently hosted the Summit of the Americas in coordination with the Organization of American States (OAS). Other countries, such as Guyana, are recipients of focused and concrete assistance on good governance initiatives and are addressing anticorruption risks in the context of their newly discovered oil.⁴⁹

- Multilateral institutions and organizations regularly produce assessments and diagnostics (IMF, FATF, OECD, etc.), which, paired with detailed in-country diagnostics and expertise in countries committed to fighting corruption, provide the basis for policy recommendations that are

⁴⁸ OECD, *Education for Integrity: Teaching on Anti-Corruption, Values and the Rule of Law* (2018), available at <http://www.oecd.org/governance/ethics/education-for-integrity-web.pdf>.

⁴⁹ Given the Guyanese people’s hope to transform the country into one that fosters development for all, its weak political institutions and rampant corruption add significantly to this challenge, notoriously the fact that Guyana has been listed as a major money laundering jurisdiction “Guyana Listed as ‘Major Money Laundering Jurisdiction,’” *Guyana Times*, April 11, 2018). The country will require dedicated assistance to strengthen institutions related to financial management and the oil sector, including those that monitor and regulate safe, effective, and environmentally responsible oil operations. Guyana will likely need assistance with the institutional setup of an independent petroleum commission, as well as energy and regulatory agencies.

technically sound and politically realistic. IDB can provide support to these assessments and related domestic efforts to pave the way for designing evidence-based action programs, including dedicated anti-corruption initiatives. Further, there should be close collaboration with the efforts spearheaded by the OAS on anticorruption in the region, particularly the initiatives for an independent judiciary, international cooperation and information-sharing mechanisms against cross-national corruption, and beneficial ownership requirements described in Pillar 1.

- Public procurement reform emerges clearly from our analysis as a priority area for action. The IDB has a significant role to play in this area, by helping establish best practices for contracting of large infrastructure projects, privatizations, and concessions. It could generate knowledge on the market structure and level of competition of industries especially vulnerable to corruption. These could include not only sectors traditionally recognized as vulnerable to corruption—defense, telecommunications, mining, oil and gas—but also less obvious ones, such as education, health, and pensions. In some of these sectors, procurement of goods may benefit from benchmarking exercises, to facilitate price comparisons, when goods are homogeneous and standardized. This type of initiative would be a regional public good. Additionally, the IDB can support the development of cost benchmarks for renegotiation processes to reflect expected actual costs. In this regard, the IDB should ensure that operations and fiduciary departments, including the investigative office, share information and lessons learned on governance and anti-corruption. This will provide the Bank's clients with a broader understanding of the key issues related to transparency and integrity.
- The IDB's Infrascopes index is a pioneering initiative to evaluate the capacity of countries to implement sustainable and efficient public-private partnerships in key infrastructure sectors. A major revision of this initiative, in light of the corruption scandals in the infrastructure sector throughout the LAC region, would be a major contribution. The IDB should also consider developing an analogous index for public provision of infrastructure.
- State-owned enterprises are another area deserving further attention by multilateral development institutions. Some of these entities are at the core of the recent corruption scandals. Transparency and corporate governance reforms could be considered part of the technical assistance of lending engagements with these entities.
- This report highlights the importance of the private sector. In this context, lending to private entities by IDB Invest (non-sovereign lending) should also incorporate transparency and integrity assistance. When dealing with clients from the financial sector, for example, special attention should be paid to AML/CFT standards that are fundamental to ensure integrity in this area. In this regard, IDB Invest's know-your-customer-standards include an assessment of AML/CTF controls, and the Bank has supported member countries interested in strengthening AML/CTF systems. The IDB could also build the capacity of national financial institutions through its loans by including AML/CTF aspects and agreeing on actions to mitigate corresponding risks.
- The IDB can support countries in taking a hard look at recent scandals—regardless of whether they are tied to any activities the IDB has financed—and help identify key lessons learned, including recommendations to prevent similar events of state capture and grand corruption. Specifically, the large number of cases before the courts in Latin America, particularly those based on plea agreements, provide information on corrupt practices that may otherwise remain secret. This information could help identify mechanisms used for corrupt transactions and draw lessons to alter incentives and mechanisms to prevent corrupt practices. It should also be shared across the region to promote a better understanding of how corrupt transactions operate.
- Lessons learned by the IDB's investigative unit could be shared proactively with member countries to encourage institutional reforms from within. Other multilateral development banks (MDBs) publish redacted versions of investigate reports, a practice that fosters transparency and accountability. Additionally, it is important to ensure communication between

the IDB's anti-corruption office and its operational side to inform the Bank's support to the anti-corruption and governance agenda in countries, on one hand, and to ensure that other Bank-financed programs do not face the same issues, on the other.

- The IDB can also help scale up innovations utilizing technology tools, such as the e-transparency extractives revenue-sharing portal Mapa Regalías in Colombia, and Mapa Inversiones.⁵⁰ However, supporting efforts to generate information should be accompanied by activities that promote demand for the information generated.
- The IDB supports many countries in their efforts to open governments and use data to make decisions. It should work on improving the availability and quality of procurement data related to the loans and technical cooperation agreements it finances. It is important that it leads by example.
- The IDB and other MDBs have implemented investigative and sanctioning mechanisms. Firms and individuals found in violation of anti-corruption policies incorporated in the contracts and bidding documents may be subject to investigation, and if found responsible for wrongdoing, debarred from future contracting. MDBs mutually recognize each other's sanctions. The IDB's Sanction Procedures⁵¹ include referrals to national authorities. This mechanism should be reviewed and revised to facilitate information sharing with domestic authorities. The IDB should make full use of this avenue. Empowering countries to take action against corrupt companies and individuals is part of the value-added

of having a sanctions system. Countries should have the possibility to bar companies that have engaged in corruption in IDB-financed projects from participating in the public procurement process. The exchange of information generates lessons that can increase prevention and detection (including via incentives for companies and individuals to come forward when corruption has taken place), in IDB-financed activities as well as technical assistance and collaboration with IDB member countries.

Finally, a broader and higher-level strategic imperative applies to any international financial institution and multilateral development bank, including the IDB. For any organization to have a demonstrable impact on anti-corruption, it is far from sufficient to have many disparate initiatives, provide lending support, or have a public sector, transparency and anti-corruption unit(s). Leadership from the top of each organization—which is being demonstrated at the IDB, as well as at the CAF Development Bank of Latin America, IMF, OAS, and OECD—and from their respective governing bodies and management is also key. Equally important is the integration of governance and anti-corruption as a prominent, explicit, and concrete cross-cutting theme in the organization's own medium-term strategy. This does not mean that each institution would cover the full spectrum of support programs on anticorruption, because their remits and core competencies vary. Some would be able to support some political economy reforms and support of civic space, while others would focus on financial, procurement, or public sector reforms, including transparency.⁵²

⁵⁰ See MapaInversiones in Paraguay (<http://mapainversionessnip.economia.gov.py>) and in Costa Rica (<http://mapainversionescr.mideplan.go.cr/>).

⁵¹ See IDB Sanctions Procedures, available at <http://idbdocs.iadb.org/wsdocs/getdocument.aspx?docnum=39676437>.

⁵² Thus, coordination among the various regional and global organizations is important, ensuring less duplication of activities (often technical 'low-hanging fruit') and avoiding leaving glaring gaps unaddressed (often in the political and accountability realms related to the demand side of governance).

Implications and Conclusions

6

Society and State after Corruption – Overcoming Investment Paralysis

It has been said that much of Latin America faces a problem of paralysis in the wake of corruption scandals. Government work is grinding to a halt, even with critical progress needed for sustainable and inclusive development, as officials seek to avoid the risk of investigation and prosecution, and companies become reluctant to take on government contracts. To overcome these risks, governments need to look at scandals as an opportunity to move toward a renewed legal and administrative structure that allows contracts in infrastructure, energy, extractives, and other sectors to occur in a fully transparent and accountable environment.

Specifically, to avoid investment paralysis going forward, a phased approach could be considered regarding large-scale projects under scrutiny:

- A transitional period in which large projects and contracts are re-examined, and eventually renegotiated, re-bid, or canceled. While potentially costly in the short term, this provides a much-needed signal that business-as-usual no longer applies. Some projects will need to be scaled back and made more cost-effective, but others may have little development potential and should be canceled. However, governments should seek ways to provide transitional aid to workers and honest subcontractors caught up in a cancellation or restructuring through no fault of their own.

- A new period in which large and critical projects go ahead, but under very transparent and accountable procedures, as per the recommendations in this report. The corrupt company may cease operating as a going concern and could be replaced by a new firm whenever possible. This ought not be construed (let alone implemented) as being about providing amnesty to the corrupt individuals, where strict sanctions would still apply. But mechanisms to unlock ongoing projects that have been frozen can be found via the proper set of (positive and negative) incentives, transparency, and effective project management and oversight (including from third parties). To address the bottlenecks arising from fears of prosecution due to uncertainty, governments should clarify the new rules and communicate them clearly within and outside the government and then work diligently to return to a revived pace of business in a more honest contracting environment.
- During this new period, prospective projects should follow honest, transparent, and accountable procedures to avoid repeating scandals and the corruption costs.

Final Reflections – Main Implications for Action

It is abundantly clear that corruption can no longer be treated as a technical challenge that can be met merely by adopting more laws and regulations or forming ethics commissions. Rather, politics matters,

as do the incentives of politicians, public officials, judges and the private sector. Civil society participation is also crucial. Laws abound, while effective practice and implementation of anti-corruption measures is scarce. Corruption is a fundamental threat to democratic institutions and to the stability and prosperity of the region and its citizens.

In closing, we reiterate the salient points of our recommended agenda. The corruption crisis in the region is embodied in the phenomenon of state capture. Breaking the self-reinforcing hold of narrow elites over decision making in the economy and polity, and the culture of impunity for the powerful, is essential to the region's ability to rebuild trust, revitalize growth and innovation, and finally raise the most vulnerable of its people out of poverty and conflict. To achieve this, the countries of the region must make incisive and sometimes painful changes to achieve the following:

- Rebuild the rule of law, including an independent judiciary, with fair, impartial, and transparent courts.
- Ensure a competitive polity and economy, including incentives for ethics in business and reforms in SOEs.
- Re-insert the public interest in the management of public resources, procurement, and contracts, including in infrastructure and extractives.
- Illuminate and regulate the anarchic and distortive flow of political finance and enforce conflict of interest regulations.
- End secretive ownership of companies and sources of finance.

- Embrace innovations such as plea bargaining, technology, and evidence-based solutions.
- Open government to the voices, eyes, and expertise of the citizenry, fully embracing a participatory approach to fight corruption.

This ambitious agenda includes issues that do not often appear in formal policy discussions on combating corruption, particularly in multi-governmental bodies, partly due to perceived or actual sensitivities. As experts with decades of experience in this field, we believe this is the only honest—and ultimately the only successful—approach to take, particularly at this critical juncture in the region. Further, we sense that today many progressive leaders and reformists in the region fully recognize that concretely addressing corruption at all levels is paramount.

The recent scandals in the LAC region pose unique challenges and opportunities. They remind us that building effective and transparent governments is an arduous and nonlinear process. The governance and institutional reforms being adopted in some countries, coupled with the investigations and prosecutions, show that concrete progress is possible. But there is still a major challenge ahead.

Given the current predicament of the region, this challenge must be addressed with audacity. The time is now for the region's political, economic, and civic leaders, along with the people of Latin America and the Caribbean, supported by the IDB and its fellow institutions, to embark on bolder efforts toward systemic transformation.

Annex I

Expert Advisory Group

Short Bios

Eduardo Engel is professor of economics at the University of Chile and director of *Espacio Público*, a Chilean think tank. He holds an engineering degree from the University of Chile, a Ph.D. in statistics from Stanford, and a Ph.D. in economics from MIT. He has published extensively in the areas of macroeconomics, public finance, regulation, and infrastructure economics. Recently he coauthored the book *The Economics of Public-Private Partnerships: A Basic Guide*. He chaired Chile's Anticorruption Commission in 2015. The legislative agenda that followed this commission's report resulted in the approval of major reforms of campaign and party finance legislation, asset and interest disclosure requirements, the civil service system, land use regulations, financial sector regulations, and antitrust legislation.

Delia Ferreira Rubio is an expert on political financing. She holds a doctorate in philosophy of law from the Complutense University of Madrid. She served as chief advisor of various representatives and senators of the Congress of Argentina from 1990 to 2005, advising the constitutional committee of the House of Representatives and the Senate. She also worked as a consultant to the national accounting office for two years. She consults on political finance and anti-corruption and transparency-related matters for international organizations (CAPEL, DEMOCRACY INTERNATIONAL, ERIS, IDB, IDEA, IFES, OAS, NEED, UNWOMEN, etc.) and nongovernmental organizations around the world. Dr. Ferreira has also worked on projects that promote transparency and accountability in the financing of political/

partisan campaigns in Argentina, Bolivia, Colombia, Ecuador, El Salvador, Guatemala, Jamaica, Nicaragua, Paraguay, and Peru. She is currently president of Transparency International. She was a member of the board of directors of Transparency International (2008–2014) and President of “Poder Ciudadano” in Argentina (2008–2010). She is the author of numerous publications on democratic and political institutions, political culture governance by decree, public and parliamentary ethics, political financing and electoral systems, among others.

Daniel Kaufmann is the president and CEO of the Natural Resource Governance Institute (NRGI), a not-for-profit international policy institute operating in all regions of the world focused on governance and anti-corruption in resource-relevant countries. An economist, he is a pioneer in the field of governance and anti-corruption worldwide. He has held various leadership positions in the field and has led innovative approaches to measure and analyze governance. He has practical experience providing high-level policy advice and helping countries around the world to formulate and carry out governance reforms in areas such as anti-corruption, transparency, and natural resources. His research publications cover many other areas as well, including economic development, political economy, investment, privatization, and urban and labor economics. His writings also feature in major international media publications. Past positions include senior fellow at the Brookings Institution, where he remains a non-resident senior fellow. Prior to that, he was a director at the World

Bank Institute, leading work on governance and anti-corruption. He also held other World Bank senior management positions focused on anti-corruption, finance and regulatory reform, was lead economist in the research department, and was also the first head of the World Bank in Ukraine. He was also a visiting scholar at Harvard. He has served on various boards of organizations, as well as high-level advisory groups, such as Integrity and Anti-Corruption to OECD's Secretary General. He is currently a full member of EITI international board. In policy circles and international media, he is associated with innovations such as the Worldwide Governance Indicators (WGI), the Resource Governance Index (RGI), and the study and analysis of legal corruption and state capture. He holds a B.A. in Economics and Statistics from the Hebrew University in Jerusalem, and an M.A. and Ph.D. in Economics from Harvard University.

Armando Lara Yaffar is a partner at the firm Chevez Ruiz Zamarripa, in Mexico City. He is an international tax consultant at the World Bank Group and the Inter-American Center of Tax Administrations (CIAT). He is a former general director on international tax affairs of the Under Ministry of Revenue of the Ministry of Finance and Public Credit in Mexico, with 22 years of experience. He also served as the chair of OECD's Working Party 10 on Exchange of Information and Tax Compliance from 2011 to 2015 and vice chair in the Bureau of the OECD's Committee on Fiscal Affairs from 2014 to 2015. He was the chairperson of the Committee of Experts on International Cooperation in Tax matters of the United Nations from 2009 to 2016. Mr. Lara Yaffar has a Bachelor's degree in law from the Escuela Libre de Derecho and a degree in finance from the Universidad Iberoamericana, both in Mexico. He was appointed as one of the 50 most influential individuals in the tax world on 2013, 2014, and 2015 by the International Tax Review, a specialized publication of Euromoney.

Jorge Londoño-Saldarriaga currently serves as an operating partner of Advent International and serves on the boards of Ecopetrol, Organización Corona, Corona Industrial, and Life Miles. He is also member of the Superior Council of EAFIT University (Escuela de Administración, Finanzas y Tecnología). In 1993 he joined the board of directors of BIC (now BANCOLOMBIA, NYSE CIB) and in February 1996 assumed the presidency for 15 years. In this position,

he conducted a process of growth and internationalization that resulted in the bank being considered the premier bank of the country and one of the first in the subregion. Additionally, during his chairmanship, publications such as *The Banker*, *Global Finance* and *Euromoney* recognized BANCOLOMBIA as the Best Bank of the country and one of the first in Latin America.

Beth Simone Noveck directs The Governance Lab and its MacArthur Research Network on Opening Governance. She is a professor at New York University's Tandon School of Engineering. From 2009 to 2011, she served in the White House as the nation's first deputy chief technology officer and director of the White House Open Government Initiative. UK Prime Minister David Cameron appointed her senior advisor for Open Government. A graduate of Harvard University and Yale Law School, she is a member of the Board of the Center for Open Science and the advisory boards of the Open Contracting Partnership. She is also a member of the Global Future Council on Technology, Values and Policy for the World Economic Forum. Ms. Noveck is the author of *Smart Citizens, Smarter State: The Technologies of Expertise and the Future of Governing* (Harvard University Press, 2015) and *Wiki Government: How Technology Can Make Government Better, Democracy Stronger, and Citizens More Powerful* (Brookings 2009). Her next book, *Public Entrepreneurship: Training the Next Generation of Public Leader and Problem Solver*, will be published by Yale University Press.

Mark Pieth is a professor of criminal law and criminology at the University of Basel, Switzerland. From 1989 to 1993, he was the head of Section, Economic, and Organized Crime at the Swiss Federal Office of Justice (Ministry of Justice and Police). In this role, he drafted legislation on money laundering, organized crime, drug abuse, corruption, and the confiscation of assets. As a government official and later as an independent consultant, he has acquired extensive experience in international fora serving as a member of the Financial Action Task Force on Money Laundering (FATF), member of the Chemical Action Task Force on Precursor Chemicals, and chair of an intergovernmental expert group charged by the United Nations with determining the extent of the illicit trafficking in drugs. From 1990 to the end of 2013, Mr. Pieth chaired the OECD Working Group on

Bribery in International Business Transactions, also participating in the Wolfsberg AML Banking Initiative as a facilitator. In 2004 the UN Secretary General appointed him to the Independent Inquiry Committee into the Iraq Oil-for-Food Programme. In 2008, he was made a member of the Integrity Advisory Board of The World Bank Group (IAB), advising the President of the Bank and the Audit Committee on integrity issues. From 2011 to 2013 he has chaired the Independent Governance Committee (IGC) overseeing the reform process of FIFA. More recently, in 2013, he was appointed chairman of the Sanctions Appeals Board of the African Development Bank (AfDB). He is the founder and chairman of the board of the Basel Institute on Governance (BIG).

Susan Rose-Ackerman is Henry R. Luce Professor of Law and Political Science, Emerita, Yale University. She is the author of *Corruption and Government Causes, Consequences and Reform* (1999, 2d edition with Bonnie Palifka, 2016), *Due Process of Lawmaking: The United States, South Africa, Germany,*

and the European Union (with Stefanie Egidy and James Fowkes, 2015); *From Elections to Democracy: Building Accountable Government in Hungary and Poland* (2005); *Controlling Environmental Policy: The Limits of Public Law in Germany and the United States* (1995); *Rethinking the Progressive Agenda: The Reform of the American Regulatory State* (1992); and *Corruption: A Study in Political Economy* (1978). She holds a Ph.D. in economics from Yale University and has held fellowships at the Stellenbosch Institute for Advanced Study, South Africa; Queen Mary University of London; the Wissenschaftskolleg zu Berlin; Sciences Po, Paris; the Center for Advanced Study in the Behavioral Sciences in Palo Alto; Collegium Budapest; the Guggenheim Foundation; and the Fulbright Commission. She has published widely in the fields of law, economics, and public policy, and she has edited nine books on aspects of corruption and administrative law. Her research interests include comparative regulatory law and policy, the political economy of corruption, public policy and administrative law, and law and economics.

