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Fitzsimons, Vincent G.

University of Bradford

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A troubled relationship: corruption and reform of the public sector in development.

Vincent G. Fitzsimons

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Abstract

Corruption is an issue of increasing visibility in the academic and policy literature on governance and public policy. Whilst it is often talked about, there appears to be some lack of clarity on both its nature and the nature of its determinants. This has led to some increase in the effort to combat it (in light of its significant costs for society) and it is questionable how effective these attempts have been to date.

Corruption has a complex relationship with public sector reform. Reform is often executed which has as one of its objectives the control of corruption, but reform itself may be a cause of corruption according to some evidence from recent rounds of economic and public sector reform.

The nature of the relationship is complicated by the fundamental nature of public sector reform. This is often 'dual' in nature, combining both destructive and constructive phases that redistribute the relative power of internal and external interest groups, create grievances, and present new opportunities for incumbents when compared to the pre-reform position.

This paper presents an analysis of some of the data on corruption in relation to public sector reform, and attempts to clarify the nature of the corruption phenomenon in order to answer the question whether corruption can categorically be said to be a problem of public sector reform, or a consequence of it.

Vincent G. Fitzsimons
Bradford Centre for International Development
University of Bradford
Bradford BD7 1DP, UK
v.g.fitzsimons@bradford.ac.uk

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Introduction

There exists a strong relationship between the theory of corruption and public sector reform. Whilst many areas of public policy proceed without necessary reference to corruption, the reform of the public sector appears inextricably linked to the problem of corruption. Economic bases for public sector reform now emphasise the need for transparent governance structure, and 'checks and balances' that may prevent abuse of any individual's position. Reform packages will now typically recognise some issues of corruption - the nature of the relationship between the two concepts, however, is less straightforward than is normally suggested.

Corruption is arguably a costly and economically damaging problem that governments, particularly in developing countries, need to address as part of any overall pattern of reforms. Williamson (2003) reviews the list of standard reforms of the 'Washington Consensus' of the late 1980s and 1990s that reflected the political position of several dominant Western governments of the time who followed 'monetarist' economic doctrine. The reforms required on this 'shortlist' of policies were: fiscal discipline, reordering public expenditure priorities; tax reform; liberalization of interest rates; a competitive exchange rate; trade liberalization; liberalization of inward foreign direct investment; privatization; deregulation; and property rights (p.10). These would, overall, reduce the extent of the involvement of the state in domestic and international markets, reduce the extent of its spending programmes, reduce its levels of employment, and reduce the 'imperfections' that prevented markets from solving fundamental economic problems such as unemployment or trade imbalances. Versions of these reforms can be seen wherever the international financial institutions were active from the mid 1980's (or even earlier) right into the late 1990s and the present day.

This consensus on economic reforms paralleled another generally neoliberal movement of the time, the New Public Management, which sought for governments to enforce a clear separation of roles between political and administrative members of the state, and to refocus the state administration towards clear objectives of the government at the same as performing its tasks more efficiently. Whilst this oversimplifies the movement considerably, it can be summarised as the pursuit of

more for less, and the removal of the administration from political processes of the state to a large degree. The rhetoric surrounding this movement emphasised the clear inefficiency of existing systems of administration where, in many countries, the lines between political and administrative actors was blurred. The emphasis on monitoring the extent to which services were delivered and at what cost reflected a general view that the state could be run along economic lines, and that it should be as small as possible to fulfil its core functions. It suggested that governments implementing these reforms would see clear benefits in terms of both cost reduction and improvement in the quality of services provided to the public.

Many years on, now, the evidence does not appear to support the optimistic pronouncements of either school, partly due to the complex nature of the developed and less developed countries in which the theories were put into practice, and possibly also due to the fundamental inadequacies of the theoretical approaches that underpinned these reforms. In particular, the New Public Management appears to have produced only limited savings that are hard to quantify, and definite costs to the public administration of many developing countries (Andrews and Shah, 2003). This paper attempts to examine one particular aspect that constituted a weakness in both sets of reforms, that of corruption and its control. This is arguably both an economic policy problem (affecting the implementation of many of the 'micro-management' elements of the economic reform programmes suggested) and public administration problem, as well as having demonstrable negative effects on the economies of those countries afflicted with the problem. The paper takes the approach of examining the connections between different sets of reform and corruption using a review of corruption theory to analyse the likely outcomes of such programmes. In reviewing the evidence of 'completed' reform programmes executed in the former-socialist states in Central and Eastern Europe, in particular, it demonstrates the long-term changes in levels of corruption that follow economic and public-administrative reform programmes of the types referred to above. In practice, both sets of reforms were simultaneously introduced in the process of post-socialist transition, and the effects of 'standard reforms' can therefore be considered in a way, although the examination of particular elements is of course not possibly due to the simultaneity of the effects on the economic system.

Public Sector Reform

The creation of packages of reforms for the public sector appears, strangely, to have been a largely theoretical exercise in many respects. Elements of the theory of

economic governance and motivation theory have obvious implications for the reform of administrative structures, and make it possible to predict the likely reactions of individuals caught up in these programmes. It is strange, however, that little attention was paid to the possible differences between developed and less-developed countries, and how this might affect the suitability of particular reform packages. It would appear logical to analyse the differences in the problems experienced by different types of countries before suggesting the solutions, in the form of a reform package, but this appears not to have happened to any significant extent. Rather there has been a set of pragmatic responses amongst those attempting to implement policies, resulting in a divergence, to some extent, between the developed and less-developed forms of the public sector reforms. Arguably this may have been a useful strategy to apply in the implementation of the economic reform strategies of the period which were generally very uniform in their imposition. The 'particularism' of the reform strategies may potentially have increased their effectiveness in particular countries, but also makes a scientific comparison almost impossible.

1. Developed countries?

The standard set of policy reforms aimed, in developed countries, to trim the size of 'over-large' states and make them more fit for purpose, according to the general approach of the New Public Management. This involved a refocusing on separation of political and administrative responsibilities; on policy objectives; on roles; on structures; and on performance and its monitoring. This, pushed by the common neoliberal agenda of the 1980s and 1990s has not yet been sufficiently examined in terms of the impact on the relationship between the political and administrative state, and the impact on the political activity internal to the administration.

Typically, the policies in 'Westminster model' countries (where the British system of government had been imposed or influential at some point in history) encouraged the exaggeration of the existing separation of powers in those countries. This move towards a more 'professional' civil service, rather than a more political one, would help clarify roles and focus efforts on the official goals of the administration. This has met with problems, however, for a number of reasons. The considerable autonomy of political 'masters' means that some moves have been made to redistribute power back to the administrators due to the potential for new governments to reverse previous benefits of the outgoing party after an election loss. This argument shows through in transition states keen to imitate Western political models, such as the political changes of the presidential system in Russia with both a strong president

enabling strong-state promotion of reform; but also a constitution with high costs of adjustment to help fix the reforms and make flip-flopping difficult. President Yeltsin showed, however, that no system is proof against reversal of beneficial policies, when the political situation is complex and unstable or at least frequently shifting. Thatcherism and the reform of the public sector in US, Australia, and Norway, and to some extent recent reforms in Finland, are other significant cases of this tendency. Initial stages focussed on service delivery and the execution and implementation of the policy choice of politicians.

Later developments in some countries suggest a move away from Woodrow Wilson's separation of politics and administration – possibly due to this problem. There is for instance significant use in the UK of 'special advisers' that are 'extra-establishment', and political appointments. This reflects research on the nature of individuals involved in public administration in some developed economies. This research suggests that two types of administrator co-exist, classical or those expecting separation of duties along 'classical' lines, and political, or those expecting more active involvement in the forms of implementation and effectively 'politics on the ground' operate in modern administrations. When examining the detail of many countries that have in principle implemented reform of the public administration, it is often obvious significant exceptions exist.

Overall, a debate exists, still, over the effectiveness of the separation of political and administrative functions as it can be argued that reducing the autonomy of public administrators restricts their ability to act rapidly and therefore efficiently. This suggests the need for 'light touch' streamlined regulation and controls. The accountability agenda, however, calls for increased monitoring (and therefore also 'voluntary' reporting to create auditable information on the work of the administration) and public scrutiny, which may lead to increased interventions from political masters into the administrative process, as the politician is motivated by the need to mollify the public concerns. Thus the reform programme attempts to pursue conflicting goals simultaneously, which results in difficulties for the administration.

2. Developing countries?

The obvious question arises when considering the use of standard reform packages in developing countries, does the problem fit the solution? Andrews and Shah (2003) identify a range of weaknesses in the public administration of developing countries.

These range from the purely economic to the largely social in nature, reflecting the complexity of the process of reform of developing countries (Table 1)

Table 1: Common Governance and Administrative Weakness in Developing Countries

[Insert table 1 about here]

Reforms are sometimes internally motivated as countries address the problem of achieving difficult targets in terms of service provision and often important elements of economic development from highly restricted resources. The external influence often shows itself in the need to demonstrate particular attributes that will for instance satisfy external donors, or perhaps alter the positioning of the state in the opinions of influential powers. The 'trickledown' of the neoliberal NPM policies into developing countries is demonstrated in a range of studies. Unfortunately the higher degree of resource scarcity increases the difficulties of implementation of any of the policies enormously.

The general elements of the reform strategies have been divided into four main areas in the work of the UNDP:

- '(i) Civil service reform, which is concerned with human resources in the public sector such as capacity, wages and conditions.
- (ii) Increasing the efficiency and responsiveness of the policy-making system.
- (iii) Reforming the machinery of government, which is concerned with the rules, institutions, and structure of the administration necessary to carry out government policy, including new tools for public administration, notably e-governance and e-government.
- (iv) Reforming the public sector revenue and expenditure management system.'

(UNDP, 2004, p.6)

Given the points considered above, some distinct elements of reform can be identified for developing countries. Typical Public Administration Reform elements for Commonwealth countries have been identified by Kaul (1997). Miller (2005) summarises these as:

1. redefinition of the political and administrative interface: clarify the roles between political policy makers and administrative policy implementers – 'distinguish between strategic objectives and operational processes' (p.22);

2. selection of appropriate reform options (from both private sector and international experience);
3. raising accountability (government or donor led initiative) – ‘performance measurement, devolution or resource control, improving monitoring and evaluation techniques, clarifying incentives and aligning functions with strategic objectives’ (p.22);
4. initiating public-private sector partnerships;
5. efficiency: ‘emphasis... placed on the public service to achieve developmental priorities.’ (p.22);
6. audit of staff cost and skills;
7. anti-corruption initiatives;
8. change, fundamentally, public sector values.

(adapted from Miller, 2005, p.22)

The UNDP Governance project has encouraged the reform of public sectors to pursue both political and economic/administrative aims for many years. In their review of best practice in the field of public sector administration, they come to two strong conclusions. Firstly, the nature of the developing economy makes a significant difference to the nature of appropriate policies, with a powerful and ‘over-large’ state being a necessity rather than a burden. In many cases it needs to substitute for the absent or under-developed private economy: ‘In the LDCs and post conflict countries in particular, underdeveloped private sectors require the public administration to play a major role in the delivery of services’ (UNDP, 2004, p.3). Secondly, the nature of the state is not simple, and it appears unlikely that a clear separation of duties can be effective, with administrators performing specific goal-oriented processes and politicians setting strategy. This over-simplifies the role and character of both administrative and political actors in developing countries. In particular, public sector management also involves: ‘fostering dynamic partnerships with the civil society and the private sector, to improve the quality of service delivery, enhance social responsibilities and ensure the broad participation of citizens in decision-making and feedback on public service performance.’ (UNDP, 2004, p.3) This explains the contradiction between the objective of minimising state involvement in the economy and increasing focus on specific administrative functions, whilst also suggesting the use of private-public partnerships.

Overall, the situation is still unclear whether the New Public Management approach was effective or not in helping to achieve its goals. Moreover, it remains unclear

what the wider impacts are on the operation of governments. As Peters and Pierre (2001b) state: 'administrative reform has ... had a profound impact on the nature of politics within the public sector, and especially on the relationship between civil servants and their nominal political masters' (pp.1-2). What that impact is, exactly, remains unclear.

Corruption theory

Some confusion exists between the different approaches to corruption, relating to the exact nature of corrupt administrators. The question is, are they 'bad', or 'mad'? The relationship between the administrator that 'chooses' to be corrupt and the state in which they operate is relevant to this problem, obviously, but this is often neglected from some theoretical approaches. Alternatively the relationship between the administrator and the 'clients' that they deal with may similarly be significant in the explanation of the corrupt act. Many of the deviations from expected behaviour in the 'principal-agent' relationship between the state and individual administrators may be interpreted as corruption. Some corruption definitions stretch to over forty types of corruption, but even simple models are relatively complex (Figure 1).

[Figure 1 about here]

Broadly speaking, the economic approach to corruption, which is possibly the dominant one, would discount relationship factors in favour of explanations based in the calculation of self-interested strategies, given the incentives which surround individual administrators. This is clearly assuming that the administrator is 'bad'. People are selfish unless incentives are created to keep them honest – a simple extension of the standard economic assumption that individuals are selfish, calculating optimisers. In this sense everyone, not just administrators, might be assumed to be 'bad'. Alternatively, it can be assumed that individual administrators are inherently good, but are turned by environmental factors or group decision making into someone 'bad' – this is an explanation of 'bad, but understandably so'. Gorta (1998) sees this tendency in some of the sociologically based criminology literature as of potential value in combating corruption, in the case of Australian public administration following its implementation of the New Public Management approach. Finally, they may be categorised as 'mad'. This would either involve non-calculating corruption that does not benefit the individual (the closest an economic approach may come to a definition of irrationality) or it may be seen as 'annoyance' or loss of reason. The literature on fraud uses 'fraud triangle' (Figure 1) based on

Cressey's (1953) research into the motivation of offenders to explain the decision to perpetrate a fraud, and this may be similarly applied to corrupt acts. In Cressey's model, the act of the crime depends on the existence of a motive, an opportunity (to commit crime and potentially get away with it), and 'rationalisation'. Individuals who are de-motivated or hold some grievance may be tipped over from being honest to dishonest by the existence of this third factor, which reduces the reluctance to harm ones victim.

Figure 2: The Fraud Triangle

[Figure 2 here]

The implications of these models for public administration reform can be briefly sketched out if we consider the position of individual administrators and compare this to the 'decision factors' used in each of the approaches.

Firstly, the economic approach is quite simple to apply to the case of administrative reform, and Stiglitz (2002) examines just such a case from a developing country. Faced with the changing administrative structures and, in particular, with the reduction in the scope of activity of an individual administrator in the process of 're-focussing', there exists a strong incentive for individuals to take some benefits while the opportunity still exists. In transition countries this resulted in the phenomena of 'insider privatisation', where state officials took control of and, effectively, plundered many state owned operation before they could be privatised in order to strip some benefits out of the system. Often the ability to do this with relative impunity existed due to the closed nature of the state administration and the strong networks between branches of administration and legal institutions. Similarly, Stiglitz cites examples of administrators used to taking small occasional bribes (minor corruption) from state service provision who, faced with their privatisation, decide to compensate themselves with one-off windfalls through acts of major corruption.

Figure 3: Impact of post-socialist reform on corruption scores (CPI)

[Figure 3 about here]

In both of the above examples, there would be a severe deterioration in corruption in a country experiencing particular types of reform (specifically relating to economic

reform, but more generally to any reform where public administrators could derive an income, if inclined to do so, pre-reform). These short-term effects would be severe, but shortlived on the face of it. Experience of corruption has shown, however, that the growth of crime such as corruption is a 'ratchet effect' which is easier to raise than to lower. The growth of corrupt practices has a range of knock-on effects in the economy that are likely to reinforce the tendency to corruption. Whilst many models of corruption exist, a strong and significant correlation exists between levels of income and corruption. This may account for the distinct and prolonged decline in the corruption scores of those transition countries for whom historical data exists.

This characteristic behaviour, in terms of the corruption performance, of post-socialist reformers is potentially of significant concern for those considering the implementation of public administration reform. The evidence suggests that corruption both deteriorates and then stagnates for a significant period, with many of these countries experiencing a decline for the best part of the following decade.

At the most basic level, higher incomes are likely to reduce the need for further income (Figures 4 & 5; also Ehrlich & Lui, 1999). Relating this to the fraud model, higher income is likely to reduce the dissatisfaction of individuals and so reduce the potential 'rationalisation' of the act. Accordingly, this can be seen as evidence in support of the fraud approach to corruption.

Figure 4: Relationship between corruption control and income levels

[Figure 4 about here]

*Figure 5: Relationship between **legal** corruption control and income levels*

[Figure 5 about here]

This correlation is not sufficient explanation, however, of the phenomenon of corruption. Whilst income is a strong determinant of corruption, the evidence from non-OECD countries is much less conclusive showing wide variation that is not explained by income levels. Factors such as culture have been cited as potential explanations for these differences, as well as social and political institutions. In this respect, many of the international donor agencies are keen to use elements of each of the models in turn. Cultural change or use of 'social' discouragement are key to some anti-corruption strategies (Gorta, 1998) whilst the general approach of the New Public Management, with its emphasis on transparency of administration supports

the economic view, which would conclude that the increased chances of being caught in a corrupt act should significantly discourage potentially corrupt officials.

Figure 6: USAID Determinants of Corruption

[Figure 6 about here]

The related models for dealing with corruption similarly attempt to incorporate all the elements of the theoretical perspectives reviewed above. Public sector reform is central to the anti-corruption strategy used by the World Bank, which is perhaps the most developed of those used amongst the International Financial Institutions. The institutional structure that results from political and administrative structures may act to either discourage or encourage corrupt practices, and only a comprehensive strategy to deal with the many incentives to corrupt activity and patterns of corruption.

Figure 7: Multi-pronged strategy for state capture and administrative corruption

[Figure 7 about here]

In truth, the need to marshal a range of resources to the anti-corruption programme means that it is in many ways an all-encompassing concept. Public sector reform and changing levels of corruption are likely to have many determinants in common. An active civil society is likely to reduce corruption due to its ability to give voice to those victims of corruption that would otherwise be powerless to complain. It is also likely to increase the moves toward an open and responsive public sector. In this way we would expect in many cases lower levels of corruption to be associated with administrative reform programmes. In view of the evidence to the contrary from the transition cases, this needs further examination.

In practice, a factor which is frequently significant in the introduction of public sector reform is the existence of external factors such as aid donor pressure that encourage the adoption of reform. In this way, developing countries may easily demonstrate such contradictory evidence. The lack of domestic pressures to reform may suggest, however, that an absence of civil society pressure exists that may create a vacuum in the post-reform system. This may firstly undermine the ability of individuals to take advantage of nominal transparency in the administrative systems, and secondly the reforms may create incentives to corrupt practices amongst officials without the

'countervailing power' of an active civil society that might otherwise have mitigated the excesses of corrupt officials.

Conclusion

Corruption has a complex relationship with public sector reform. Reform is often executed which has as one of its objectives the control of corruption, but reform itself may be a cause of corruption according to some evidence from recent rounds of economic and public sector reform.

The nature of the relationship is complicated by the fundamental nature of public sector reform. This is often 'dual' in nature, combining both destructive and constructive phases that redistribute the relative power of internal and external interest groups, create grievances, and present new opportunities for incumbents when compared to the pre-reform position.

Overall, the outcome of a 'New Public Management' style reform programme is, on the basis of the evidence presented above, impossible to judge. This stems from differences in the nature of the economic or political system in which reform takes place; the differences in social and cultural institutions; and the varying levels of development of necessary supporting institutions that might support the effectiveness of the reform programme. It is however likely that reforms may create incentives to corruption that, unless checked, can cause significant and prolonged problems with corruption that may undermine the benefits of the administrative reform. Whilst New Public Management appears to demonstrate only limited benefits, the consequential corruption appears on the basis of statistical evidence likely to have significant negative economic impacts. This brings into question the advisability of such programmes without some sensitivity to the particular situation of the countries in which the reforms are implemented.

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Table 1: Common Governance & Administrative Weakness in Developing Countries

Low capacity:	Low personnel capacity Low systems capacity
Organizational centralization and top-down governance:	Process orientation Permanence and non-innovation
Service monopolies:	Uncompetitive and unaccountable public production processes Weak incentives for production efficiency
'Social insulation', low transparency and poor participation:	Social exclusion based on process and 'normal professionalism' Internally biased, non-responsive incentive structures
Poor organizational evaluation and accountability mechanisms:	Weak internal evaluation mechanisms Few external (social) evaluation mechanisms

Source: Andrews and Shah (2003) p.6.4

Table 2: Public Expenditure Tracking Surveys: Capture of non-wage funds in primary education

Country	Year	Expenditure programme	Sample size	Capture (% of non-wage budget)
Ghana	1998	Non-wage spending in primary education (multiple programmes)	126	49
Peru	2001	Utilities	100	30
Tanzania	1998	Non-wage spending in primary education (multiple programmes)	45	57
Uganda	1995	Per-student capitation grant	250	78
Zambia	2001	Fixed school grant	182	10
Zambia	2001	Discretionary non-wage grant programme	182	76

Source: Reinikka & Smith (2004), table 2.1, p.36

Figure 1: Forms of Corruption



Source: UNODCCP (2002) p.3

Figure 2:: *The Fraud Triangle*

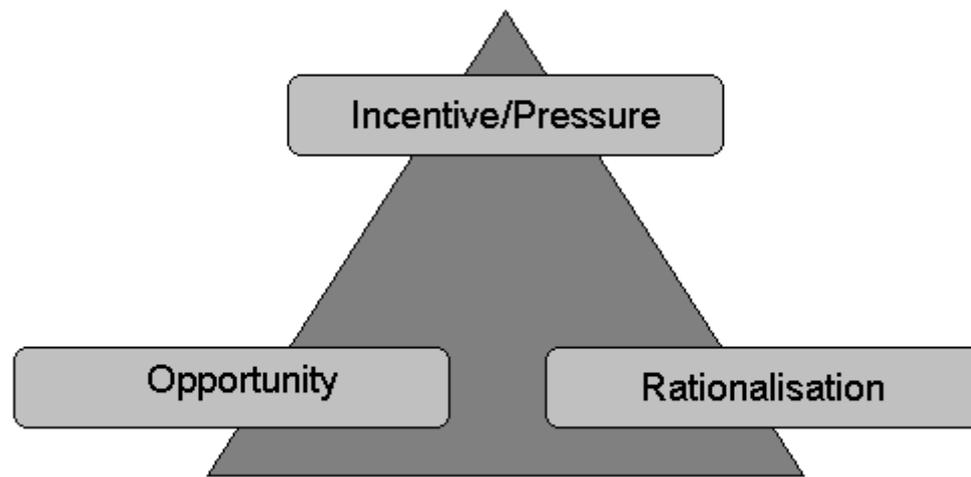


Figure 3: Impact of post-socialist reform on corruption scores (CPI)

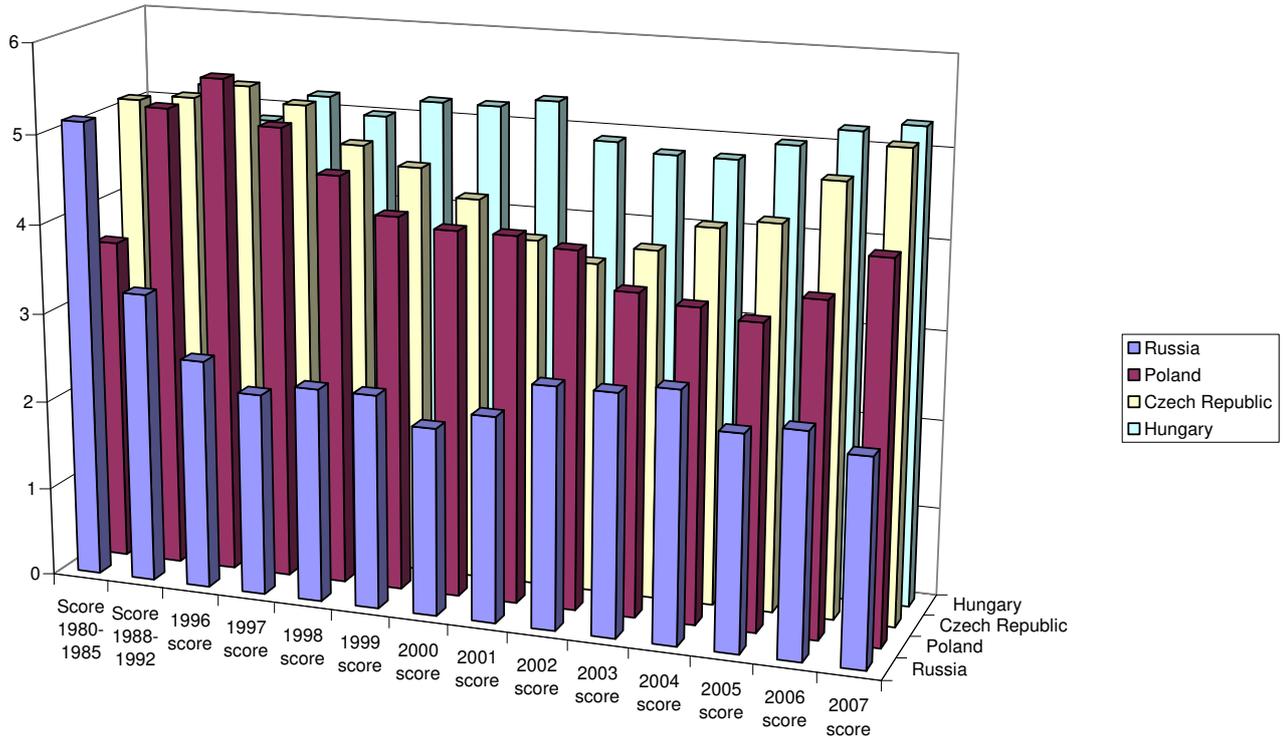


Figure 4: Relationship between corruption control and income levels

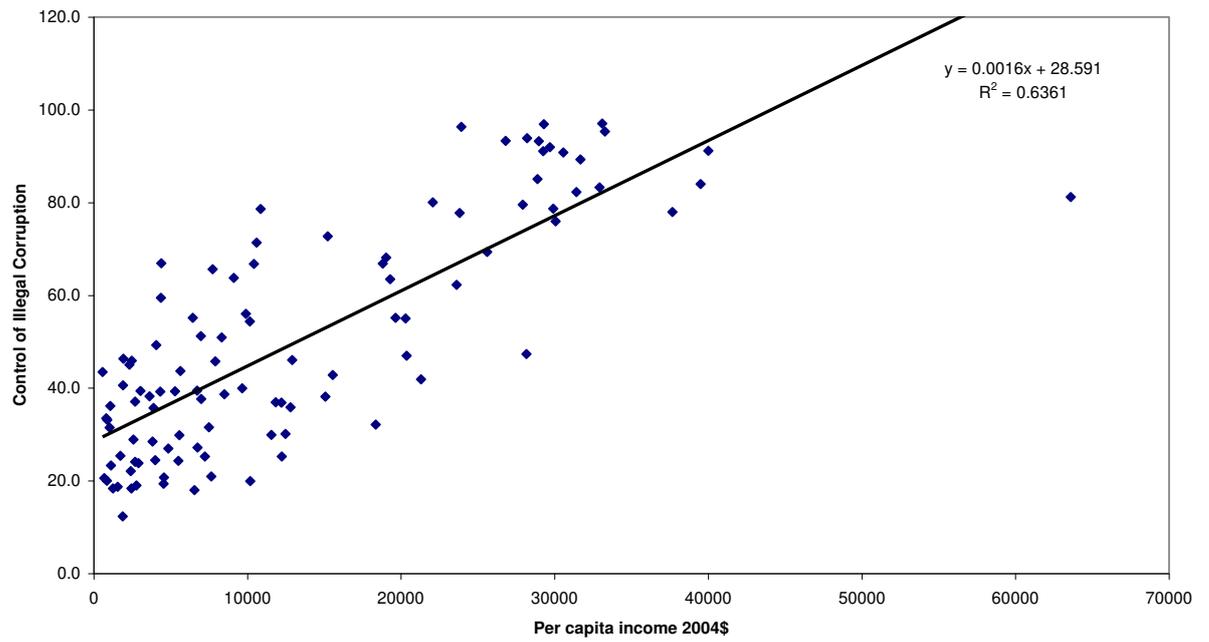


Figure 5: Relationship between **legal** corruption control and income levels

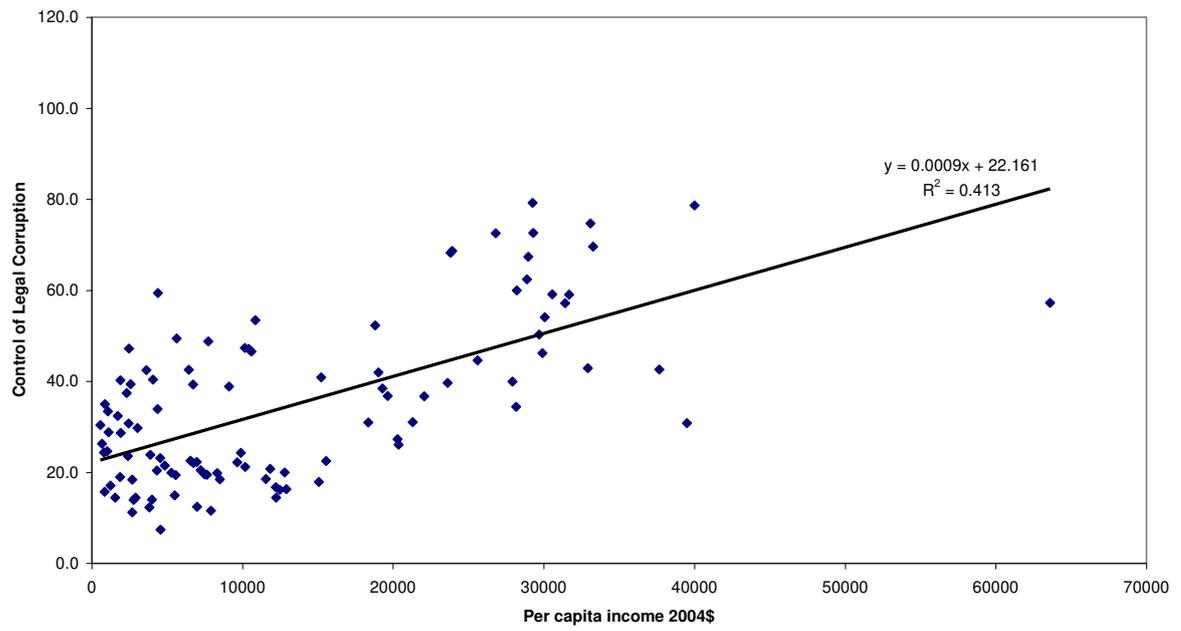
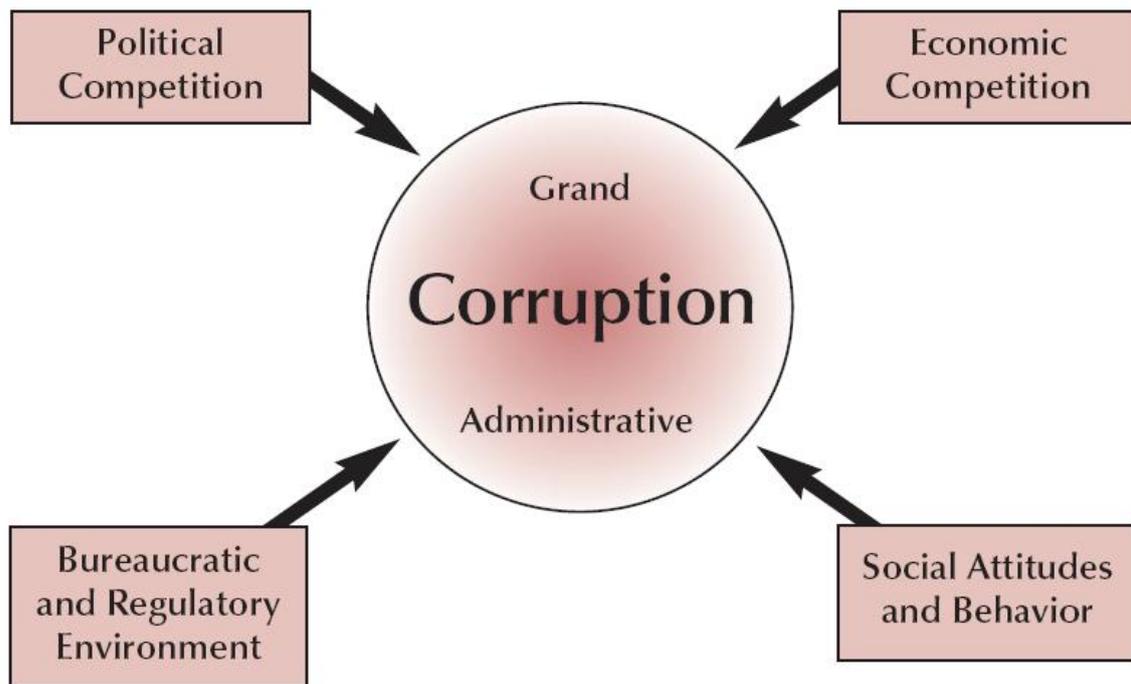
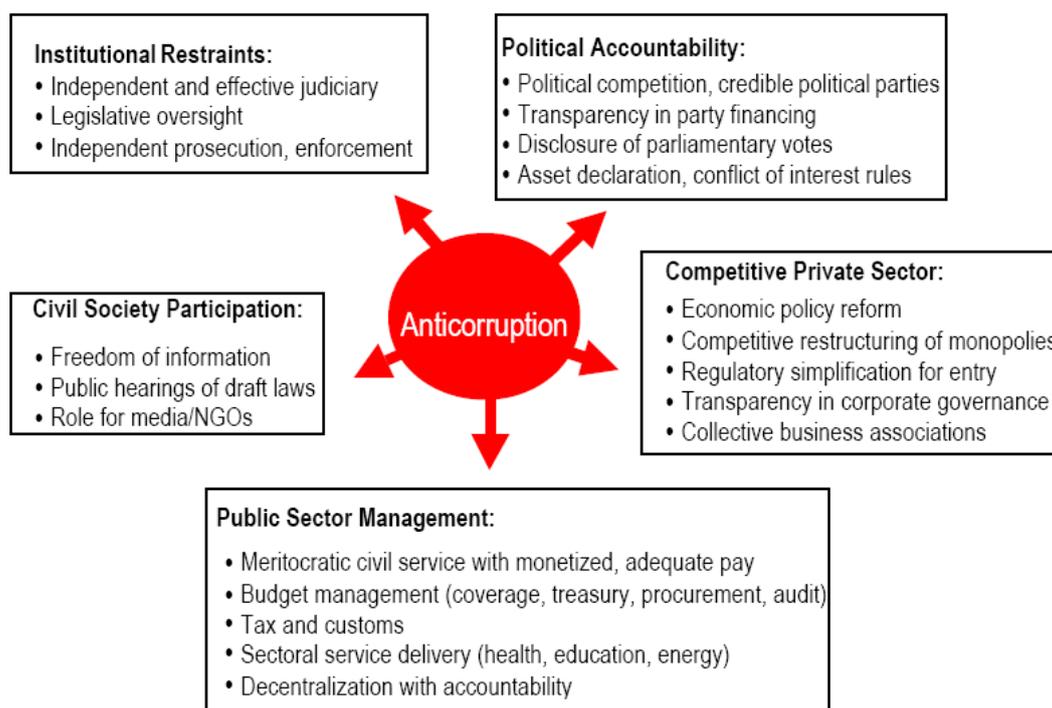


Figure 6: USAID Determinants of Corruption



Source: USAID (2005) p.15

Figure 7: Multi-pronged strategy for state capture and administrative corruption



Source World Bank (2000), p.xxii

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