

# FOCUS ISSUE 10: ECONOMIC GOVERNANCE

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## I. Overview of the Commitments

### Africa:

- ◆ The **2001 Constitutive Act of the African Union**, identified good governance and economic management as an essential prerequisite for promoting economic growth and sustainable development in Africa.
- ◆ The **2003 African Union Convention on Preventing and Combating Corruption** called for the coordination of member States in preventing and combating corruption using harmonized policies and Acts to ensure socio-economic development, transparency and accountability. The Convention entered into force on 5 August 2006, when the requirement of 15 ratifying countries was met. The AU Convention is particular in containing binding provisions on private-private corruption and political party funding. In addition, it obliges state parties to establish laws on asset declaration by public officials and restrictions on immunity of public officials.
- ◆ The **2003 Abuja Declaration on Democracy, Political, Economic and Corporate Governance**, which mandated the establishment of the Africa Peer Review Mechanism (APRM), approved codes and standards including: to promote good economic governance; the creation of well-defined structures; harmonious and complementary fiscal, monetary, and trade policies; coherent development strategies and programmes; a dynamic domestic private sector and monitoring and regulatory authorities for promotion and co-ordination of different economic activities.

### International Community:

- ◆ The **UN Convention Against Corruption (UNCAC)** is an instrument which aims to combat corruption and promote transparency in public financial management. The UNCAC entered into force on the 14<sup>th</sup> December 2005. In its eight Chapters and 71 Articles, the UNCAC obliges the State Parties to implement a wide and detailed range of anti-corruption measures affecting their laws, institutions, and practices. These measures aim to promote the prevention, detection and sanctioning of corruption, as well as cooperation between State Parties.
- ◆ The UNCAC is unique as compared to other conventions, not only in its global coverage, but also in the extensiveness and detail of its provisions. This international instrument calls for preventative measures and the criminalisation of corruption in the public and private sectors.
- ◆ The UNCAC recognises that asset recovery is one of the most significant purposes of the Convention, and therefore it contains a specific chapter regulating the main systems, procedures and stages involved in any asset-recovery process.
- ◆ The **OECD's Anti-Bribery Convention** came into effect in 1999 and is a Convention adopted by the OECD and seven non-Member countries which represent most of the main countries involved in trade and investment. The Convention addresses the supply side of cross-border bribery. It aims at reducing corruption by requiring the criminalisation and sanction of the bribery of foreign public officials in international business transactions carried out by individuals and companies originating or acting from the Convention member countries. Countries that have signed the Convention are notably required to put in place legislation that criminalises the act of bribing a foreign public official.

- ◆ The **2005 Paris Declaration on Aid Effectiveness** defines a clear, practical plan to help improve the quality and positive impact of development aid. Within this framework, donors have committed to giving even greater support to developing countries' anti-corruption and economic management efforts.
- ◆ Most major **multilateral and bilateral development agencies** have pledged support for African economic and corporate governance.
- ◆ G8 leaders at successive **G8 Summits** have committed to strengthen programmes related to economic and corporate governance in Africa. The G8 have committed to increase support for the Extractive Industries Transparency Initiative (EITI) and the APRM, to support the ratification of the UNCAC by all countries, and to strengthen enforcement of the OECD Anti-Bribery Convention. In 2004, there was an agreement by G8 Justice and Interior Ministers to detect, recover and return stolen assets.

## II. What has been done to deliver on these commitments?

### Africa: Implementation of the AU Convention and the APRM

1. As of September 2008, a total of 42 member countries have signed the AU Convention, while 27 have ratified it. It is noted, however, in a recent NEPAD/APRM report that even though a number of countries have ratified the Convention, few have created the conditions for its effective implementation. A common feature therefore in many African countries is the absence of comprehensive national strategies to combat corruption.

2. The APRM is mandated to ensure that the policies and practices of participating countries conform to the agreed parameters in economic and corporate governance. The APRM periodically reviews progress that has been made by member States and fosters the adoption of policies and practices that lead to political stability and economic growth. To date, there are 29 African countries participating in the APRM process, and nine have completed all the stages of the peer review process<sup>1</sup>.

3. The following paragraphs describe how African countries are delivering on commitments contained in the Declaration on Democracy, Political, Economic and Corporate Governance, which are reviewed under the APRM.

4. **Public Financial Management:** Many African countries are now embarking on various public financial management reforms and are developing multi-year budget frameworks. The relaxation of conditionalities attached to official development assistance (ODA) has also in recent years boosted country ownership of the development agenda, thereby enabling African countries to build public finance management capacities to ensure efficient and effective use of development aid. Some African countries are also undertaking monetary policy reforms and are giving greater autonomy to central banks. Tax reforms are aiming at improving both regulation and administration of tax regimes to increase resource mobilization, ensure equity, and reduce corruption.

5. **Parliamentary Oversight:** Some countries are in the process of reviewing their fiscal legislation to empower their parliaments in the national budget formulation processes with the objective of improving non-state actor participation. There are examples of non-state actors providing technical and research support to MPs in their budget oversight functions, particularly in steering budget allocations to meet agreed State development goals. Institutions such as the UNECA, AfDB and the Parliamentary Centre located in Ghana are also helping to equip MPs with the requisite skills to boost their oversight role. In some countries, regulations are being revamped to boost the legal and administrative capacities of the supreme audit institutions such as the Offices of the Auditor-General.

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<sup>1</sup> Ghana, Rwanda, Kenya, Algeria, South Africa, Uganda, Nigeria, Burkina Faso and Benin.

6. **Corporate Governance:** There is a range of initiatives being taken in the field of corporate governance that bears the potential of affecting positively the improvement of corporate governance standards in general. Recent initiatives include the 1994 the King Report on Corporate Governance (King I) that was published by the King Committee on Corporate Governance, and incorporates a Code of Corporate Practices and Conduct. It was aimed primarily at promoting the highest standards of corporate governance in South Africa, the first of its kind. King I was updated in 2002 to reflect the evolving global economic environment and legislative developments.

7. King II acknowledges that there is a move away from the single bottom line (that is, profit for shareholders) to a triple bottom line, which embraces the economic, environmental and social aspects of a company's activities. In addition in 2002, UNECA prepared the *Guidelines for Enhancing Good Economic and Corporate Governance in Africa* at the request of the NEPAD Steering Committee. These Guidelines provide relevant codes and standards that African countries should give priority to as minimum requirements to improve economic and corporate governance, and to inform their legislative processes in this area.

8. The adoption of good corporate governance is constrained by a lack of capacity. Entities such as the Pan-African Corporate Governance Forum (PACGF)<sup>2</sup> and the Centre for Corporate Governance (CCG) have been providing training and capacity-building across the continent. In addition, the UNECA and AfDB, have been hosting international forums, learning workshops and seminars to share best-practice case studies, while specialist organizations such as the CCG and the IFC's Global Corporate Governance Forum have developed toolkits on corporate codes and standards, which have been used as training tools in several training workshops in Africa.

9. A number of companies, notably in the extractive sector, have signed agreements such as those of Transparency International (TI) and the Kimberley Process to entrench good business ethics, respect for human rights and reduce corruption. Several of these corporations have also developed and adopted formal policies on corporate social responsibilities in key areas such as health, education and protection of the environment.

10. **Extractive sector transparency:** The EITI sets a global standard for companies to “publish what they pay” and for governments to disclose what they receive. The follow-on EITI++ initiative seeks to build on the initial EITI effort by supporting committed governments in Africa to implement good policy and practice along the entire natural resources value chain/development process. The EITI++ initiative is being launched against the backdrop of high commodity prices to ensure that resource-rich countries distribute revenues equitably and spend resources effectively for sustainable development and growth.

11. Several commodity and oil exporting African countries are either committed to or are actively implementing EITI in Africa. 16 of the 23 “Candidate Countries” implementing the EITI are in Africa with several countries working towards achieving Candidate Status. 10 countries have produced EITI reports and several are preparing to undertake EITI validation, the country led-process that establishes whether a country has become EITI compliant.

### **International Community: Support for sound economic management**

12. **UNCAC:** To date, 140 countries have signed the UNCAC and another 93 have ratified it. As of March 2007, 24 of 53 AU member states had ratified the UNCAC. The Convention can be used as a legal tool for reforming governments and can serve as a framework instrument to effectively address corruption. With the ratification of the UNCAC by partner governments, corruption can now be part of the political dialogue on development.

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<sup>2</sup> PACGF brings together professional and trade organizations that are interested in the promotion of good corporate governance in Africa.

13. The international community has strengthened their efforts to implement the UNCAC. The UNCAC project<sup>3</sup> aims at supporting the capacity of developing countries and countries in transition to prevent and combat corruption as well as to assist them in meeting their needs for implementing the Convention. The UNCAC project is engaged in the activities of the OECD/DAC GOVNET where anti-corruption in the context of promoting governance is an effort for bringing donor harmonization in development cooperation forward.

14. The United Nations Office on Drugs and Crime (UNDOC), the UN agency tasked with supporting the signatory parties efforts to implement the provisions of the UNCAC is currently drafting a Legislative Guide to support the process. The main objective of the guide is to assist member States seeking to ratify and implement the UNCAC by identifying legislative requirements. UNDOC has also produced a toolbox – “The Global Programme Against Corruption – UN Anticorruption Toolkit”- systematizing the main aspects of witness-protection programmes. Several legal models are identified that could be useful for designing an adequate protection system. The success of the UNCAC is largely dependent on effective follow-up monitoring processes. At present the Convention lacks the necessary monitoring mechanism.

15. **OECD Anti-Bribery Convention:** The OECD Anti-Bribery Convention has been hailed as key to overcoming the damaging effects of foreign bribery, given that most major multinational companies are based in OECD countries. To date, 37 countries have ratified the Convention<sup>4</sup>. All 37 Parties to the Convention have criminalized the bribery of a foreign public official; before the Convention came into force, few of these countries had laws that sanctioned this conduct.

16. Since the entry into force of the Convention, there has been a marked increase in the number of investigations and prosecutions. There have been over 150 investigations and more than 60 convictions of foreign bribery by various Parties to the Convention. Prison sentences have been handed down in several countries: individuals and companies found guilty of foreign bribery have been fined, in some cases up to EUR 30 million, and profits of bribes have been seized. According to the 2008 Transparency International Report, there has been significant enforcement in sixteen countries<sup>5</sup>. Moreover, four out of the five largest exporters have prosecutions against major multinational companies.

17. However, there is still a lack of enforcement in over half the OECD countries. A much higher level of enforcement will be needed before the criterion for success – widespread recognition by international business that foreign bribery is no longer acceptable will be achieved.

18. **Other economic governance initiatives:** The OECD and the African Development Bank are developing a joint Anti-Bribery and Business Integrity Initiative for Africa to support African countries in strengthening their frameworks and practices to curb bribery of African officials in business transactions. The initiative will provide a mechanism to assess progress against international instruments, primarily the OECD Anti-Bribery Convention and the UN Convention Against Corruption.

19. The Bretton Woods Institutions are supporting African countries efforts to adopt good economic management. The IMF's *Code of Good Practice on Fiscal Transparency and Guide on Resource Revenue Transparency* is active in promoting transparency and combating corruption in public financial management, targeting oil-producing countries in particular. The Bank for International Settlements' Basel Committee on Bank Supervision provides a forum for regular

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<sup>3</sup> The UNCAC project is funded by the Federal German Ministry for Economic Co-operation and Development (BMZ) as a first contribution to support the implementation of the UNCAC.

<sup>4</sup> The Convention was ratified by South Africa in June 2007 – the first African country to do so.

<sup>5</sup> “Significant enforcement” is based on the number and importance of cases and investigations taking into account the size of the country's exports. (Cases are defined here to include prosecutions, judicial investigations and civil actions). Investigations are important as the initial step towards prosecutions or civil actions. However, the number of investigations is important only if they lead to prosecutions or civil actions (2008 Transparency International Report).

cooperation on banking supervisory matters. The committee seeks to enhance understanding of key supervisory issues and improve the quality of banking supervision worldwide, including in Africa.

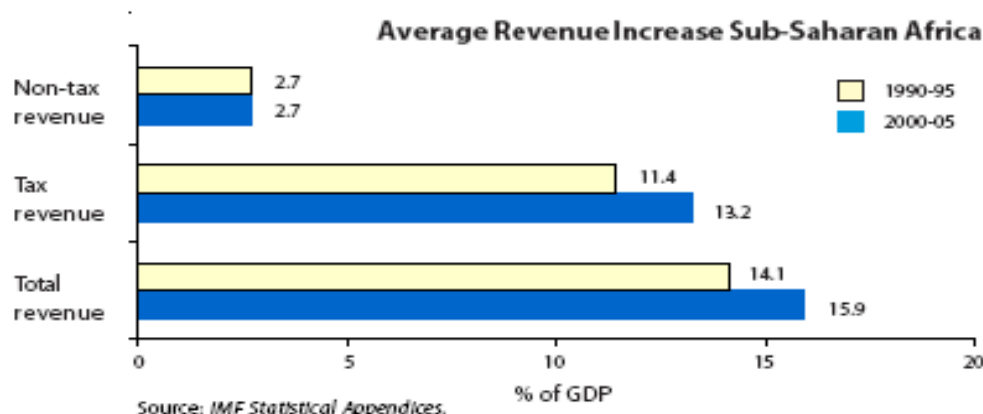
20. **Recovery of stolen assets:** With regard to asset recovery, the G8 has planned “accelerated response teams” of forfeiture-related mutual legal assistance experts to be committed at the request of victim states whose assets have been secretly hidden abroad, as well as coordination task forces for specific cases. The G8 Justice and Home Affairs Ministers have undertaken to advance recovery of the proceeds of high-level, large-scale corruption, taking into account final disposal of confiscated property, including through holding G8 regional asset recovery workshops and the creation of best practices for modalities of disposition and return of recovered assets.

21. In September 2007, the World Bank, in partnership with the United Nations Office of Drugs and Crime (UNDOC) launched an initiative - The Stolen Asset Recovery Initiative (StAR initiative) - to help developing countries recover assets stolen by corrupt leaders. StAR calls for its ratification by all countries that have ratified the UNCAC and operates on the premise that both developed and developing countries must work in partnership. The UNDOC-WBG StAR initiative is an integral part of the World Bank Group’s Governance and Anti-Corruption Strategy, which recognises the need to help developing countries recover stolen assets. The international legal framework underpinning StAR is provided by the UNCAC.

### III. What are the results?

22. **African governments have markedly improved their revenue mobilization efforts.** ECA’s African Governance reports that African governments have substantially improved their revenue mobilization efforts and an unprecedented number of African countries have recorded budget surpluses in recent years. Excluding Nigeria and South Africa, the increase in government revenue as a share of GDP rose sharply from 18.8% for 1997-2002 to 25.4% in 2007. This is due to a mix of factors, including increased revenue from buoyant commodity prices as well as more effective tax administration.

**Figure 1: Average Revenue Increase Sub-Saharan Africa**



Source: IMF Statistical Appendices

23. **Improvements in public financial management (PFM) have contributed to a stabilised macroeconomic environment** and reduced annual inflation rates -- from an average rate of 25% in the 1990s to single digits in 2002 (IMF World Economic Outlook, 2008). Similarly, budget deficits have receded, supported by development partners’ efforts to reduce public debts through Heavily Indebted Poor Countries Initiative (HIPC), the Multilateral Debt Reduction Initiative (MDRI) and other initiatives.

24. In 2007, over 20 African countries were at some stage of implementation of their Medium-Term Expenditure Frameworks (MTEFs). MTEFs involve the development of a strategic expenditure, resource allocation, and budget framework. There is some empirical evidence that shows that MTEFs are improving PFM through reallocations to subsets of priority areas and greater budgetary predictability. MTEFs are having greatest impact where there is strong political support.

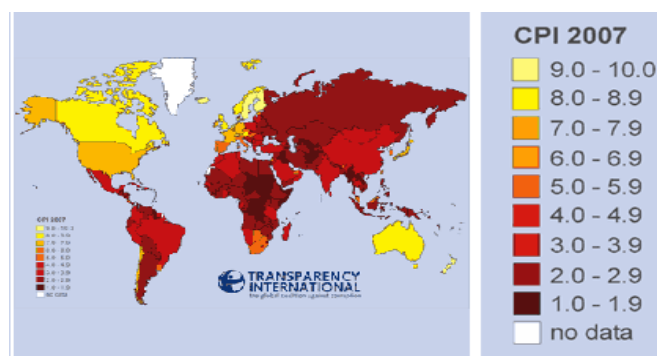
25. **Parliamentary oversight in budgetary processes is increasing.** In practice, parliaments in Africa are generally considered ineffective. The 2005 African Governance Report found that: “In terms of enacting laws, debating national issues, checking the activities of the government and in general promoting the welfare of the people, these duties and obligations are rarely performed with efficiency and effectiveness in many African parliaments” (UNECA, 2005, p.127).

26. To boost parliamentary oversight in budgetary processes, a number of African countries are now enacting Acts to give parliaments powers to amend the Executive’s budget proposals. Development partners are re-energising their efforts towards building the capacity of African parliaments, including through information and communications technologies (ICTs) and financial management training, facilitating the exchange of best practices among Members of Parliament, and providing hardware to support parliamentary administration.

27. **There are huge annual losses in Africa due to corrupt practices.** While great progress has been made in improving governance and entrenching democracy in Africa over the past years, the fight against corruption and economic mismanagement is still to be won. In many African countries, corruption has pervaded the entire public sector affecting human resources management, public services provision and the management of public resources – particularly for tax receipts and expenditure management. The poor regulation of the privatisation process in many African countries has also contributed to corruption in the executive branch and throughout the bureaucracy.

28. A report by the African Union noted that Africa loses an estimated US\$148 billion annually to corrupt practices, a figure that represents 25% of the continents gross domestic product. Similarly, the African Development Bank (AfDB) indicates that corruption leads to a loss of approximately 50 per cent of tax revenue in Africa which is greater than some countries’ total external debt.

**Figure 2: Corruption Perception Index (CPI 2007)**



Source: Corruption Perception Index - CPI (Transparency International (2007))

29. The impact of corruption is felt first and foremost by the poor. According to a recent NEPAD/APRM report, lower income households spend an average of 2-3 per cent of their income on bribes, while rich households spend considerably less (an average of 0.9 per cent of their income). According to the 2005 ECA African Governance Report, corruption ranks high on the list of problems

for many African countries. Similarly, the 2008 Corruption Perception Index issued by Transparency International (TI), states that six of the 10 lowest ranked countries are African states<sup>6</sup>.

30. While the focus of the international community has been on addressing corruption and weak governance within developing countries, corruption is often hidden in the financial centres of developed countries. Bribes to public officials from developing countries often originate from multinational corporations. High-level, large-scale corruption – where state assets have been secretly hidden abroad – continues, and efforts to recover these assets are fraught with difficulties. According to a World Bank publication, the problem of stolen assets is most acute in Africa. It is estimated that \$20 billion to \$40 billion per year is acquired by corrupt leaders and stashed overseas.

31. **Significant changes have been made to address corporate governance weaknesses but, by and large, problems persist.** More countries are adopting regulations and developing institutions to enforce contracts and property rights. However, corporate governance has not advanced much in Africa, and the data show that laws to protect shareholders, especially small shareholders, are not effective. Africa ranks as the region with the lowest protection of shareholders.

32. As Africa struggles to attract a fair share of the world's FDI, it has to assure its investors that their investments will be secure and efficiently managed on the basis of a transparent and accountable process. This can be assured through good corporate governance. The financial crisis has also made clear the relevance of good corporate governance as a key structural and institutional feature of a functioning market economy. In a globalised economy, the implementation or otherwise of good corporate governance will increasingly determine the fate of individual companies and entire economies.

33. Experience from countries that have embarked upon reform measures with some success show that the reforms are likely to succeed when comprehensive strengthening of external sources of discipline and internal incentives are provided to improve corporate governance. Making corporate boards more effective and competent in the discharge of their oversight duties and control over management, for example, have proven especially effective. The reforms typically involved the following elements:

- Establishing competitive markets;
- Requiring transparency;
- Enforcing financial discipline;
- Fostering growth of well-regulated and liquid securities markets;
- Updating and strengthening the legal, judicial, and tax systems; and
- Building required capacity.

34. However, because of the transitional state of African economies and political systems, many African countries are ill-equipped to implement the corporate governance systems that have evolved over the centuries in developed market economies. Among the major constraints in this respect are; the ownership structure of the corporate sector, interlocking relationships with government and the financial sector, weak legal and judiciary systems, lack of or undeveloped institutions, and limited human resource capabilities.

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<sup>6</sup> There are however some notable improvements. Nigeria jumped 26 places higher to 121 on the TI index; Mauritius rose 12 places to 41; Ethiopia 12 places; and Kenya 3 places.

## IV. What are the key priorities?

### Action by Africa:

- ◆ More countries to ratify the AU Convention on Preventing and Combating Corruption.
- ◆ Sustain positive growth trends through improved economic management and effective regulation and supervision of banks and other financial institutions to ensure stability and credibility in the financial system.
- ◆ For oil-exporting countries - improve the management of oil revenues and economic diversification which are essential for reducing vulnerability to oil price shocks.
- ◆ In light of the commodity boom, improved management of resources to ensure they are spread equitably and broadly shared with the aim of poverty reduction.
- ◆ Improvements in business transparency to ensure better management of natural resources.
- ◆ Empower parliaments so that they can participate in policy making, implementation, monitoring and evaluation of results.
- ◆ Embrace good corporate governance to contribute to the creation of a credible policy environment in which domestic and international investors can have confidence and trade can be advanced.

### Response by the international community:

- ◆ More countries to ratify the 2003 UN Convention on Corruption and support its implementation and develop a review process to follow the implementation of the Convention.
- ◆ Develop effective compliance and monitoring mechanisms to track UNCAC implementation.
- ◆ Encourage new major economies to join the OECD Anti-Bribery Convention.
- ◆ Support initiatives, notably by the business sector, to prevent and detect foreign bribery, and intensify efforts across the board for an increased enforcement of the OECD Anti-Bribery Convention.
- ◆ Deepen support for the EITI through providing more financial and political support.
- ◆ Increase support for the StAR initiative and assist the asset recovery process of African countries by providing loans or grants to finance the start up costs, provide advice on hiring legal counsel, and facilitate cooperation between countries.
- ◆ Political will and legal reform regarding the return of stolen assets from the African continent.