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ON

“EXAMINING RESULTS AND ACCOUNTABILITY AT THE WORLD BANK”

Submitted By

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Chairman Barr, Ranking Member Moore, and distinguished members of the Subcommittee, it is an honor to have been invited to testify before the Subcommittee on International Monetary Policy and Trade on the subject of World Bank reform.

I have been asked specifically to address issues that flow from my research on corruption in World Bank projects in Kenya, and to comment on the perspective of beneficiaries and implications for Bank reforms.

By training, I am an economic anthropologist, and since the 1970s I have conducted research in a remote area of Kenya near the Somali border. The people living in this area are similar to many other herders in the drought-prone, arid lands of eastern Africa. They are the poorest of the poor, exactly the kind of people IDA funding is attempting to lift out of poverty.

In 2004, the World Bank Arid Lands Resource Management Project arrived in the village where I have lived and conducted research over many decades. The corrosive effects of the corruption that I witnessed in that community project propelled me into a broader analysis of the Arid Lands Project that served 28 districts in Kenya and ran from 1996 to 2010. As I dug more deeply, it became apparent that corruption had been entrenched in the project since 2000. That conclusion is based upon hundreds of interviews with beneficiaries, Kenyan project staff, members of civil society, World Bank staff, donors in Nairobi, and senior Kenyan politicians and civil servants. Unfortunately, these patterns continue in current Kenyan World Bank projects.

The central component of the Arid Lands Project was community-driven development (CDD). The idea is to empower villagers. Villagers select their own projects and elect leaders to manage the funds, implement the project, and monitor the work. In 2012 there were 400 World Bank CDD projects in 94 countries. These are the kinds of projects that most directly impact large numbers of poor beneficiaries.

In 2007, I reported the Arid Lands case to INT, the World Bank's Integrity Vice Presidency, which is solely responsible for investigating corruption in World Bank projects. As that process played out over many years, I gained insight into how the World Bank addresses corruption. Following an extensive INT forensic audit of the Arid Lands Project, the World Bank eventually shut down the project just as the Board was about to renew it for a further 5 years. In its investigation of 28,000 transactions from 7 of the 28 districts, the INT audit concluded that 62 percent of those transactions were suspected fraudulent or questionable. Significantly, this is the only large-scale forensic audit that appears on the INT website out of a total of 66 posted reports going back to 2008.

Before turning to the lessons learned about corruption from the Arid Lands Project, let's put the case in context. Based upon my experience, this is not an exceptional case, nor is Kenya an outlier among similarly systemically corrupt countries.

Because of the correlation between poverty and corruption, the world's most corrupt countries are where we find many of the world's neediest populations. That said, there are other projects in similarly corrupt countries that have realized better results with less corruption.

The Arid Lands Project ran for 14 years before it was shut down for corruption. What went wrong? Many of the problems can be attributed to project design. In particular, transparency was lacking, and this was compounded by a design that empowered project staff with far too much discretion. Beneficiaries were the victims of both of these failings.

To better understand the failure of transparency, let's consider the situation from the point of view of the beneficiaries. What would a beneficiary need to know in order to better monitor his or her own village project and to ensure that no one is syphoning funds from the project offices? Beneficiaries tell me that they want to see the overall project budget and transaction level data for all projects, training, and administration in their area. They want to know where the money is supposed to be going.

It is never in the interest of corrupt officials to share budgetary and contracting details, which is why they are so often hidden, even when project documents explicitly require that they be made available, as was the case for the Arid Lands Project.

Recently, a villager asked the head of a current World Bank project in his area how much money his county was budgeted to receive from the project. The villager knows that project money has been stolen, and he wants to better understand the magnitude of the problem. This information should be publicly available, but the head of the project in the county refused to provide it to him. Two weeks ago I made the same request of the two World Bank Task Team Leaders (TTLs) who serve as project managers. Despite a second email follow-up request, I have received no response as of this writing. Lack of transparency in World Bank project funding is still a problem in Kenya today.

One of the most harmful features in the design of the Arid Lands Project was the discretion that district project officers had over which villages received projects. This effectively amounted to monopoly control over who got the money, and it vested the project office with immense power over beneficiaries.

By controlling the allocation of future funds to villages, the project staff was able to stifle legitimate protests. When project beneficiaries complained that promised funds and services were not delivered, they were often told to overlook deficiencies and wait for a new project in the next funding round. This strategy almost always worked to silence beneficiaries, even though they often did not get funding in the next round.

When visits by supervisors and auditors were anticipated, villagers were coached to praise the project and say that they had received benefits that they had not. They were persuaded that if they failed to do so they would jeopardize future World Bank funding, and they were promised that there was an even bigger project on the way, which was sometimes true. I have seen this scenario play out many times. If these strategies did not stop protesters, project staffers bought them off with small bribes or cut their community from the project and diverted funds elsewhere. These practices continue today in other Kenyan projects.

The effectiveness of these strategies in preventing most villagers from carrying their complaints forward is one reason that the Arid Lands Project stayed under the radar so long.

But consider how these processes pervert the local culture. The honest altruists who resist project bribes are penalized, and the local villagers willing to be bought by the project are both financially rewarded and elevated to community leadership. Worse, the few who persist in fighting project mismanagement are at personal risk and wind up jeopardizing their communities' access to future project benefits.

Is there a way forward? Absolutely, and models already exist. One step is to improve project design.

Indonesia is often cited as the great success story in community-driven development, and I would agree. We can learn many lessons from the differences in project operations between the Kenyan and the Indonesian projects.

The original Indonesian CDD project (KDP) had many design elements that differed from the Arid Lands Project and from current Kenyan CDD projects. It was specifically designed to bypass the major centers of government corruption. Private firms were used to hire many project staff rather than seconding them from corrupt government ministries. The tone at the top of the project was inspiring, and this attracted reform-minded job applicants. In contrast to the monopolistic discretion of the Kenyan project staff, the Indonesian design allocated projects based upon a democratic and competitive selection process run by representatives of all the villages in a target sub-district.

The Indonesian project was also exceptional in the degree to which it commissioned and incorporated research to improve performance; the project opened itself to uncensored examination by third parties. This resulted in academic papers that are now classics in the study of CDD and corruption.

We know from academic literature that one of the strongest correlates of low corruption levels is a vigorous free press. Capitalizing on this, the Indonesian project created an ingenious blind-funding mechanism to encourage investigative journalists to

write about corruption in the project. All of this speaks to an open, experimental, and organically evolving project dedicated to serving the needs of the poor. The Indonesian project was not without corruption, but its managers were eager to find solutions.

The World Bank has the finest and most productive development research group in the world. The Indonesian project was wise enough to appreciate the advantages of applying this talent to many of their problems, including corruption, and that openness was rewarded with superior results.

We should be encouraged by the Indonesian case, as it means that development aid really can make a difference for the poorest of the poor, even in a highly corrupt country. I would caution, however, against assuming that Indonesia is the norm and Kenya is the outlier. I believe the reverse is true.

Better design and monitoring are important parts of the corruption solution, but sanctions also have a place, especially when faced with extreme capture such as occurred in Arid Lands.

One often hears World Bank senior management say that, “the World Bank has zero tolerance for corruption.” But what does that mean in terms of policy and outcomes? INT is the World Bank’s answer to corruption. They are the sole body tasked with investigation of fraud and corruption in World Bank projects.

It is rarely, if ever, in the interest of a donor organization to advertise to their funders that money has been misspent. There is an inherent conflict of interest between the mandate of INT to fight corruption and operations’ goals of keeping projects funded and client states happy. INT is in the political cross hairs.

Since the Arid Lands forensic audit report of July 2011, INT has posted 48 additional redacted investigation reports on their website. Of these 48, 45 (94 percent) were investigations of companies. The vast majority of these cases involved one company that was found guilty of fraudulently fabricating documentation in order to qualify to bid on a contract. One case, Padma Bridge in Bangladesh, involved huge corruption. Of these 45 cases, 36 resulted in company debarment from business with the World Bank; one company was given a reprimand, and the remainder resulted in no action.

Of the remaining 3 out of 48 investigation reports in the last 5 ½ years, 2 involved fraud by a single project employee. The last case found evidence of large-scale corruption in which about 400 contractors each paid 10 percent kickbacks to the government.

Clearly, the overwhelming focus of work for INT’s external investigations is cases against individual companies that result in debarment. This is important work, but it is

unlikely to touch the significant number of projects like Arid Lands that deliver services directly to the poor. The contractors involved in CDD-style projects are local, they number in the thousands, and they are capable of quickly rebranding and opening up for business under a new name. Going after them would be equivalent to “whack a mole.”

The problem in many World Bank projects is not limited to a few rogue contractors and project staffers. In systemically corrupt countries like Kenya, it is common for World Bank projects to be captured by the government ministry cartels from which the project staff is seconded.

Intensive forensic auditing, the strategy that uncovered large-scale corruption and shut down the Arid Land’s project, is not currently a priority of INT. Debarring corrupt companies sometimes makes better newspaper headlines, and debarment cases are easier and cheaper to conduct than large forensic audits. But this investigative direction leaves a vast segment of the World Bank’s portfolio exposed.

Why else isn’t INT more aggressively pursuing project-wide corruption? Part of the answer is INT’s resource constraints and lack of sufficient, highly qualified staff with formal investigative and forensic accounting experience. However, these constraints are self-imposed, and reflect senior management preferences, both above INT and inside INT.

Understandably, World Bank operations want to see projects through to completion. Corruption investigations can shut down projects and derail careers. They are also inconvenient for senior management in the Bank who are balancing delicate relationships with their country clients. Predictably, pressure is brought to bear on INT. I experienced first hand how operations interfered with the INT investigation of the Arid Land’s project.

It is notable that the Vice President for INT, whose direct report line used to be to the Bank’s President, now reports to the Managing Director and Chief Administrative Officer. At the very least, this recent demotion in reporting status gives the appearance that the World Bank now cares less about corruption abatement and the important work of INT. INT’s declining budget also speaks volumes, as does the small size of its budget relative to the magnitude of the Bank funds it attempts to protect.

What does this mean for the odds that a corrupt team that has taken over a World Bank project is going to get caught? In the Arid Lands case it is amply evident that 14 years of routine project management oversight, supervision missions, monthly financial management reports, and audits, did not catch them. Lest one think that these systems are functioning better today, I see no evidence of that on the ground in Kenya. Given time and resource constraints, many of these tasks have devolved to box checking.

When the probability of getting caught declines, crooks grow bolder. The same principle applies to countries. When countries, or country sectors, show a pattern of high levels of corruption in World Bank projects, or fail to cooperate with INT investigations, the World Bank should be more willing to demonstrate tough political will and cut them off. It has happened, but too rarely to send the right message.

Helping the poorest of the poor in corruption-ridden countries is difficult work. It is also heroic, and that is what has attracted many excellent people to the World Bank. We learn from the Indonesian case that much can be accomplished with the right tone at the top, careful design, transparency, research and experimentation, and effective sanctions.

Below I summarize a few of my key recommendations to reduce corruption in World Bank projects.

INT

- Move INT's direct report out of operations and over to the audit committee of the Board of Directors consistent with standard practice in many firms, and equivalent to the current reporting status of the Inspections Panel.
- Partition INT to create a separate unit to handle complex corruption cases. To be successful, such a unit must be headed by a manager who has professional investigative skills and a staff of highly-trained forensic accountants and investigators with law enforcement experience who know how to handle evidence, witnesses, and the strategic interviewing demanded of such complex cases.
- Set up a few satellite INT offices in global locations to facilitate timely investigations, to develop ties with local law enforcement for enhanced power in investigations, and to increase access to leads from civil society, journalists, and project staff.

Transparency

- The new disclosure policy of 2010 was a laudable step, but it stopped short of helping beneficiaries and third parties fight corruption. Access to project financial information is specifically excluded from the disclosure policy. This should be changed by adding the following:
 - Mandate that projects publish transaction level budget and expenditure data quarterly on the web and on publically accessible boards in relevant local sites. Note that enforcement of the latter is virtually impossible, which is why the web is crucial; web postings can be easily monitored for compliance.
 - Mandate public notice (on the web and in locally appropriate outlets) of contracts, job advertisements, tender advertisements, and details of winning and losing bids.
 - Mandate that projects include similar expenditure and contract information from all donor partners so that World Bank supervisors and interested

parties can detect double dipping from multiple donors for the same project activities.

Neither Congress nor the USED's office has the power to micro-manage World Bank policies. Changes of the sort that I am suggesting would require significant commitment and a great deal of sustained U.S. leadership to win the support of a majority of sympathetic Board members. In the past, the U.S. has been effective in providing such leadership.

I thank the Subcommittee once again for this invitation to share my research findings and suggestions on how we might make the World Bank more effective in the important work of lifting the poorest citizens of the world from poverty.