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## FIGHTING CORRUPTION IN CUSTOMS ADMINISTRATION: WHAT CAN WE LEARN FROM RECENT EXPERIENCES?

by

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Research programme on:  
Developing Countries and the Millennium Round  
and Fighting Corruption in Developing Countries

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## TABLE OF CONTENTS

ACKNOWLEDGEMENTS.....	5
PREFACE .....	6
RÉSUMÉ ANALYTIQUE.....	7
EXECUTIVE SUMMARY .....	9
I. INTRODUCTION AND CONTEXT.....	11
II. THE PROBLEM OF CORRUPTION IN CUSTOMS ADMINISTRATION.....	13
II.1. How Do Customs Administrations Function? .....	13
II.2. Different Corruption Practices.....	15
II.3. How Can We Understand This Phenomenon? .....	17
III. FIGHTING CORRUPTION IN CUSTOMS: SOME FIRST ELEMENTS.....	22
III.1. Measures That Do Not Work: Examples from Pakistan, Bolivia and the Philippines .....	22
III.2. The Need For Extensive Reform Programmes .....	24
IV. THE REFORM EXPERIENCE OF THREE DEVELOPING COUNTRIES .....	28
IV.1. A Recent Initiative in Pakistan: The PRS Project .....	28
IV.2. A Major Reform Programme in Bolivia: <i>Programa para la Implantación             de la Nueva Estructura de Aduanas</i> .....	31
IV.3. Philippines.....	35
V. LESSONS TO BE DRAWN .....	45
V.1. The Necessity to Re-engineer the Customs Environment.....	45
V.2. How to Manage Re-engineering .....	46
V.3. The Broader Conditions which Facilitated the Philippines Success .....	50
VI. CONCLUSION .....	51
NOTES .....	54
ANNEX 1. EXAMPLES OF CORRUPTION CASES OBSERVED IN BOLIVIA, PAKISTAN AND THE PHILIPPINES.....	58
ANNEX 2. COMPARING THREE POLICY PAPERS.....	62
BIBLIOGRAPHY.....	65
OTHER TITLES IN THE SERIES/AUTRES TITRES DANS LA SÉRIE.....	66

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## PREFACE

The last few years have seen a growing awareness of the crippling effect of corruption on economic development. Corruption increases inequality, distorts the state's redistribution role, wastes human and financial resources and degrades public services. Several empirical studies have shown that it significantly lowers investment levels and the productivity of capital. These effects are especially harmful in developing countries, which have few resources and higher average levels of corruption than the industrialised countries.

Recognising the importance of helping developing countries to fight corruption, the OECD Development Centre launched a research programme on the subject. The aim of this programme is to analyse corruption in greater depth and to provide guidance to the actors directly engaged in the fight against corruption. It supplements the OECD's other activities relating to corruption issues, which have led *inter alia* to the signing of the International Convention on Bribery in International Business Transactions and to a Recommendation concerning measures to ensure ethical conduct among public employees in OECD Member countries.

Elsewhere, our work on anti-corruption strategies tackled the question by setting the scope of analysis at the national level. In practice, curbing corruption requires a combination of measures taken at the national level and of measures taken at the level of the different public and private organisations that constitute the social fabric. This paper complements our previous work by focusing on the problem of corruption in one particular service, the customs administration.

Two reasons guided the choice of the customs administration. First, in developing countries, customs are usually among those administrations where corruption is most entrenched. Second, customs administrations play a crucial role in the security of the populations and in the functioning of these economies.

This research benefited from the support of the UNDP Programme for Accountability and Transparency (PACT). It compares the reform experiences in three developing countries: Bolivia, Pakistan and the Philippines. Although these countries are very different, analysis of their experiences highlights the problem of corruption in customs administrations and provides the basis for some conclusions on which solutions should be envisaged to curb it.

Jorge Braga de Macedo  
President  
OECD Development Centre  
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## RÉSUMÉ ANALYTIQUE

Dans de nombreux pays en développement, l'efficacité de l'administration des douanes est mise à mal par la corruption endémique. Cette situation est un obstacle à l'expansion des échanges commerciaux. Elle a aussi des conséquences désastreuses pour la sécurité nationale et les finances publiques.

Ce Document technique du Centre de Développement de l'OCDE analyse la nature de la corruption dans les douanes et propose quelques solutions concrètes pour améliorer l'intégrité. Il s'appuie sur l'examen des récentes réformes de l'administration des douanes engagées en Bolivie, au Pakistan et aux Philippines. Ces études de terrain ont été confiées à des spécialistes de la question, particulièrement qualifiés de par leur expérience personnelle, « de l'intérieur », pour identifier, décrire et évaluer les problèmes inhérents au service des douanes considéré, et leur évolution. Ces études rendent compte en détails et en profondeur, des pratiques de corruption, des rapports de forces hostiles ou favorables aux réformes ainsi que des résultats obtenus dans chacun des trois pays. Sur la base de l'analyse des sérieux revers rencontrés en Bolivie et au Pakistan, et du succès relatif obtenu aux Philippines, ce Document technique émet des propositions à la fois réalistes et pragmatiques pour remédier à ces pratiques.

Les évolutions observées depuis la réalisation de ces études de cas ne diminuent en aucun cas la pertinence de l'analyse ou des principes qui se sont dégagés de ses résultats.

Cinq conclusions principales se dégagent.

La première est la nécessité de distinguer les grands types de corruption :

- une corruption « de routine », où les opérateurs privés paient pour faire exécuter ou accélérer les formalités douanières ;
- une corruption frauduleuse, dans laquelle l'homme d'affaires ou son agent cherche à obtenir des services des douanes soit qu'ils ferment les yeux, soit qu'ils coopèrent pour diminuer le montant des taxes ou accroître le bénéfice extérieur ;
- une corruption criminelle, dans laquelle des agents criminels versent des pots de vin pour réaliser des opérations lucratives et totalement illégales (trafic de drogue, utilisation abusive de mesures de promotion des exportations, etc.).

La deuxième conclusion est que les stratégies de lutte contre la corruption fondées sur la conjonction enquêtes/sanctions — qui peuvent se révéler efficaces pour réguler une situation de corruption modérée et limiter son développement — sont impuissantes en cas de corruption endémique. Dans la même logique, même si le niveau outrageusement bas des salaires de la fonction publique est souvent cité comme l'une des principales causes de la corruption, l'étude montre que — une fois la corruption inscrite dans les habitudes — les bénéfices illégaux qui en résultent

sont tels que même des augmentations substantielles du salaire des fonctionnaires n'ont plus d'effet réel sur le niveau de pratiques illégales bien plus lucratives.

La troisième conclusion met en lumière la nécessité d'identifier les étapes du processus de contrôle douanier qui offrent aux fonctionnaires des occasions particulières de demander des sommes irrégulières et aux hommes d'affaires et à leurs agents d'en proposer.

Au cœur d'une stratégie de réforme devrait figurer une révision des procédures afin de limiter fortement les occasions de corruption. Ces occasions résultent de trois conditions préalables : une interface discrétionnaire entre le personnel des douanes et les opérateurs privés ; la possibilité pour le personnel des douanes de fonctionner au sein d'un réseau de complicités ; et l'absence de contrôles efficaces. La provision de signatures, de décisions sur la valeur ou la classification des marchandises, la décision en matière d'inspection, l'inspection elle-même et le règlement des conflits sont susceptibles de générer des occasions de corruption.

En quatrième lieu, l'environnement général compte largement dans l'émergence et le maintien d'opportunités de réforme sérieuse. Les études illustrent l'impact que peuvent avoir les groupes d'intérêt douaniers, les lobbies et les élites politiques, et les organisations du secteur privé sur les problèmes d'intégrité dans les douanes et sur les possibilités de réforme.

Enfin, les études de cas ont permis d'identifier quelques éléments cruciaux pour la réussite des réformes : une volonté politique au plus haut niveau ; une approche stratégique de la réforme ; une évaluation attentive de la scène institutionnelle et de l'équilibre des pouvoirs, accompagnée d'une gestion prudente des rapports de force favorables et défavorables ; la sélection et l'ordonnancement judicieux de mesures concrètes, ainsi que le renforcement du professionnalisme dans les actions au niveau des individus, en gardant un œil attentif sur l'ensemble des procédures douanières et en consolidant soigneusement chaque amélioration obtenue.

Ces études de cas comparatives devraient attirer l'attention des pouvoirs publics et des milieux d'affaires mondiaux sur cette question de la corruption dans les douanes, négligée jusque-là, mais dont les conséquences politiques, économiques et sociales sont très importantes. Les pouvoirs publics dans chaque pays doivent reconnaître et corriger les malversations dans les douanes qui viennent à l'encontre des objectifs politiques prioritaires visant à favoriser l'investissement à l'intérieur des frontières, à réduire le coût des importations et à renforcer les performances à l'exportation. Ils devraient être encouragés à adopter un regard neuf, critique et détaché sur la manière dont une corruption chronique peut miner le développement économique. Ils peuvent également apprendre de ce Document technique comment concevoir et mettre en œuvre une stratégie de réforme efficace.

## EXECUTIVE SUMMARY

In many developing countries, customs efficiency is hampered by widespread corruption. This creates a major disincentive and obstacle to trade expansion. It also leads to disastrous consequences in terms of national security and public finance.

This OECD Development Centre Technical Paper examines the nature of customs corruption and suggests some practical paths to integrity. It is based on fact-finding studies of recent experience of customs reform in Bolivia, Pakistan and the Philippines. These studies were entrusted to experts, especially qualified, by personal, inside experience, to identify, describe and evaluate the problems and developments in each of the relevant customs services. They provide a detailed, objective and intimate account of the character of corruption practices, the forces at work for and against reform and the outcome in each of the three countries. Based on the analysis of the serious setbacks in Bolivia and Pakistan and relative success in the Philippines, the study proposes realistic and pragmatic suggestions for remedial action.

Additional developments since the periods covered by the studies will, in no way, diminish the value of the insights they provide or the principles that can be deduced from their findings.

The analysis throws up five key conclusions.

The first is the need to recognise the main types of corruption. They are:

- routine corruption, in which private operators pay bribes to obtain a normal or hastened completion of customs operations;
- fraudulent corruption, in which the trader or agent seeks “blind eye” or active, collusive customs treatment in order to reduce fiscal obligations or enlarge external earnings;
- criminal corruption, in which criminal operators pay bribes to permit a totally illegal, lucrative operation (drug trafficking, abuse of export of promotion incentives, etc.).

The second shows that strategies based on investigation and sanctions — which can be effective in regulating a situation of low corruption and preventing its further development — cannot correct a situation of widespread corruption. Likewise, although grossly inadequate official salary levels are often cited as a major cause of corruption, the studies tend to show that, once corruption sets in as a settled background, the resulting illegal benefits are such that even substantial increases in official salary levels may have no real effect on the level of much more profitable irregular practices.

The third highlights the need to identify those points in the customs process that afford special opportunities for customs to seek irregular payments and for traders and agents to offer them.

A re-engineering of procedures that leads to an important reduction of the opportunities of corruption should be at the core of a reform strategy. Corruption opportunities arise from three preconditions: a discretionary interface between customs officers and private operators; the possibility for customs officers to operate within a network of accomplices; and a lack of efficient controls. The provision of signatures, decisions on value and classification, selection for inspection, inspection itself and dispute settlement traditionally provide such opportunities.

Fourthly the broader environment is a crucial element in opening up and preserving the possibilities of serious reform. The studies afford a range of examples of the ways in which customs interests groups, political lobbies and elites, and private sector organisations operate and interact in relation to customs integrity problems and improvements.

Finally, the case studies have helped identify some powerful elements for successful implementation — political will, at the highest level, a strategic approach to reform, a careful assessment of the institutional scene and balance of powers, with sensitive management of opposing and supportive forces, the selection and sequencing of practical remedial measures and the professional improvement of individual procedures, with a keen eye to the total procedural chain and precautionary securing of every improvement.

These comparative case studies should draw intergovernmental and global business attention to this previously neglected, but crucial economic, political and social problem of customs corruption. Individual governments need to perceive and correct customs malpractices which diverge from primary political aims to encourage inward investment, reduce the cost of imported goods and enhance export performance. They should be encouraged to take a new, critical and detached look at the ways in which entrenched customs corruption can undermine and frustrate economic development, and they can learn, from this OECD Development Centre paper, how best to embark on and pursue a logical, effective reform strategy.



## I. INTRODUCTION AND CONTEXT

In the past years, two policy trends to reform customs administrations, reflecting two different perspectives, have become more and more important. The first one targets trade facilitation. At the Uruguay Round, developed and developing countries committed not only to reduce substantive trade barriers, but also to implement significant reforms in trade procedures, for example the GATT Valuation Agreement. This agreement is in tune with the efforts of the World Customs Organisation (WCO), an independent intergovernmental body, created in 1952 to enhance the effectiveness and efficiency of customs administrations<sup>1</sup>. The WCO's most recent achievement has been to revise the existing Kyoto Convention, on simplified customs procedures, to reflect modern requirements including use of automated systems.

At the same time, there has been a growing awareness of the crippling effect of corruption on economic development<sup>2</sup>. Customs maladministration in developing countries contributes strongly to this situation, which has disastrous consequences in terms of national security and public finance. Taxes collected through customs in developing countries still represent an important share of the public revenue, up to 30 per cent and more for countries in South Asia and sub-Saharan Africa<sup>3</sup>; hence losses caused by fraud and corruption are all the more important. This problem was acknowledged by the WCO as long ago as 1993 when it adopted a declaration concerning customs integrity (Arusha Declaration). International finance institutions, for example the IMF and the World Bank, have accorded the corruption issue central importance, developing specific programmes and including this new element of concern in many of their activities. The issue has also appeared on the agenda of regional customs co-operation groups, including APEC and PHARE.

There is a strong convergence of views in the analysis of the corruption problem and desirable remedial actions. There are only marginal variations between the WCO Arusha Declaration and other landmark documents such as the IMF Integrity Paper "Practical Measures to Promote Integrity in Customs Administrations"<sup>4</sup> and the conclusions of the Central and Eastern European PHARE working group on customs ethics<sup>5</sup>. All concur that there is no quick solution to the problem of customs corruption and that a comprehensive approach is needed. These documents identify a number of elements contributing to high integrity in customs administrations.

There is much less insight and guidance in respect of the crucial question of implementation. How do you reform a seriously corrupt administration? The difficulties of implementing even individual policy measures such as the Valuation Agreement have already been well noted by Finger and Schuler (2000). It is one thing to define the characteristics of what an ideal corruption-resistant, efficient customs administration would be like; it is quite another actually to drive and manage the transformation.

The objectives of this OECD Development Centre research are, first, to document the difficulties of reforming customs administrations in developing countries and, second, to examine methods of opposing and overcoming these

difficulties. For this purpose, it presents an analysis of the reform experiences in three developing countries: Bolivia, Pakistan and the Philippines<sup>6</sup>.

Various sources attest the widespread character of corruption in customs in these countries. In Bolivia, two recent surveys<sup>7</sup> show that customs are perceived as the most corrupt public administration, followed by the garbage collection services and town councils. In Pakistan, customs, of all administrative services, have earned an unparalleled notoriety for corruption. In the Philippines, a survey conducted in 1990<sup>8</sup> ranked the Bureau of Customs as the most corrupt official agency<sup>9</sup>. In these three countries, specific measures to curb customs corruption and more extensive reform and modernisation programmes have been undertaken in the last decade. The present work analyses failures and successes.

Part II of this paper describes corruption in these three countries with basic information on the functioning of customs administrations. Part III outlines common recommendations for anti-corruption programmes. Part IV analyses their reform experiences. Part V draws conclusions from this empirical material and proposes suitable strategies. The concluding note in Part VI relates customs corruption to dynamic elements in economic development<sup>10</sup>.

## II. THE PROBLEM OF CORRUPTION IN CUSTOMS ADMINISTRATION

### II.1. How Do Customs Administrations Function?

All customs administrations serve similar objectives of controlling goods crossing frontiers (imports, exports and transits), in order to collect duties and taxes, implement trade policy, combat smuggling and protect the public. The precise mandate of customs administrations will vary from one country to another, as other actors — commercial banks, private control agencies as well as other government departments, for example the Ministry of Finance or the Ministry of Interior — may participate in some tasks. These mandates will also differ with the level of development of the country concerned, as well as the tools and resources at its disposal. Nevertheless the paper describes a general pattern common to all customs administrations<sup>11</sup>, which will help understanding of subsequent detail.

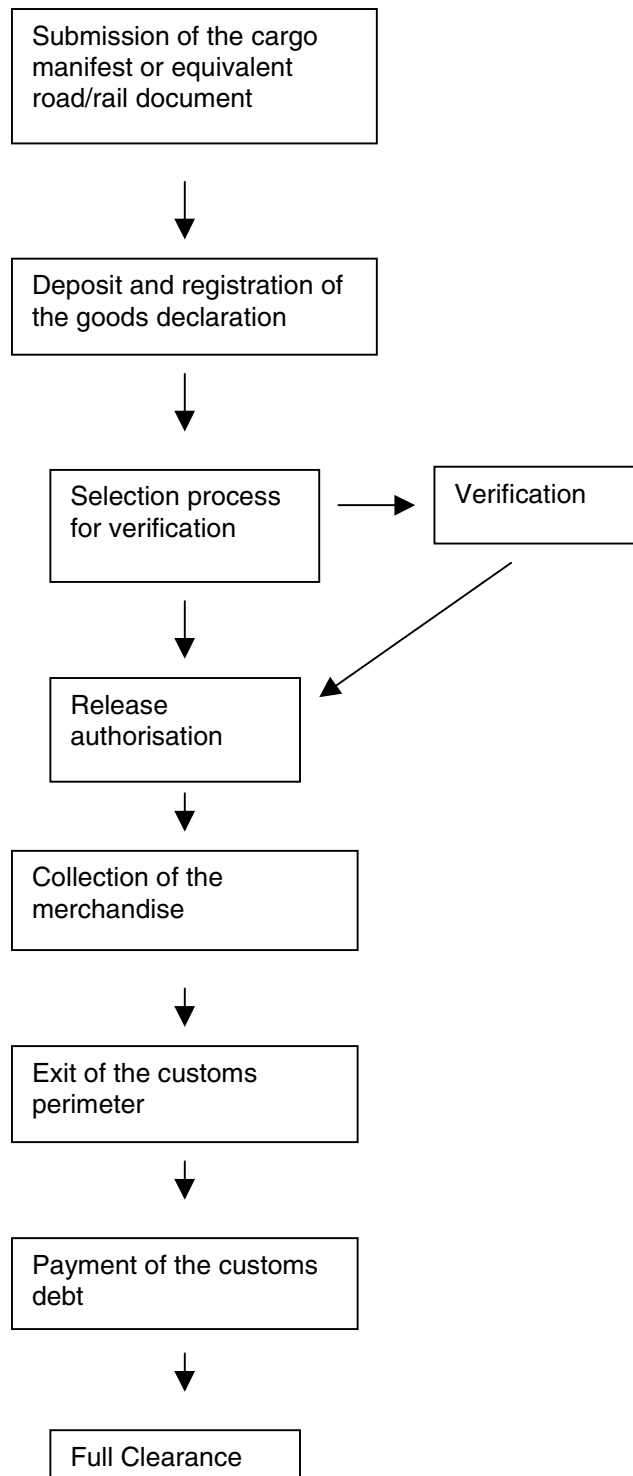
Cross-frontier goods flows are of three types: imports, exports and transits. All have to comply with customs requirements. Private operators prepare a legal document called the *customs declaration* in which they customarily give consignment details, including the nature of the goods, their quantity, their origin, their value and their destination. They may also be required to produce a number of documents such as invoices and origin certificates to support this information. The declaration is the key document in customs release and clearance as it establishes a legal relationship between the operator and the customs. The following account concentrates on customs processing of imports, as this is more comprehensive and complex than for export or transit.

In many countries, different *customs regimes* are usually available depending on the usage of imported goods. These are most frequently sold on the domestic market and are therefore cleared under the *regime for home consumption*. But goods may also be imported for use in a subsequent production and exportation, or for stocking or temporary use prior to re-exportation. For these purposes, operators can request the benefit of *suspensive regimes*, which allow for duty-free usage, stocking, transport or transformation of the goods in question pending their transfer to a final definitive procedure.

Under the regime for home consumption, a customs clearance procedure would include the following steps (see Chart 1). On arrival of the cargo at the frontier, the operator submits a cargo manifest<sup>12</sup> or an equivalent road/rail document to customs. The importer or his agent submits the goods declaration for registration by customs. Some customs services authenticate the content of the document at registration, others treat this as a preliminary formality.

In most customs, documentary and physical verification is selective rather than comprehensive. Selection may have a random basis but modern practice is to use risk assessment criteria. Where verification is necessary, there may be an examination of supporting documents, for example certificate of origin, followed, on occasions by physical inspection on the goods by reference to samples or the total consignment. If customs note inaccuracies, these may be the subject of dispute and appeal or may lead to penalties and litigation.

Chart 1. **A Standard Customs Clearance Procedure**



At this stage, goods may be released, subject to suitable arrangements for payment, and then leave the customs area. Eventual full clearance of dutiable goods will usually be subject to satisfactory payment of duties and taxes, and evidence of compliance with other customs requirements. The customs debt, calculated on the basis of declaration, may be liquidated in cash or information or recorded under a standing credit or guarantee arrangement. In a reducing number of countries, clearance and release are still carried out in a single procedure: goods receive notice of release only after having accomplished the formalities to ensure the payment or the custom debt. Full clearance then follows.

The steps set out above are the full normal procedure. Most customs administrations offer other clearance procedures that are simpler for the operators. The normal procedure is based on two principles: the deposit of a customs declaration and the presentation of the goods at a customs post. The other procedures that can be available depart from these two requirements. For instance, under the post-entry audit procedure, goods consigned to traders with satisfactory compliance record can be released on the basis of very limited control data, and the transaction is then cleared by subsequent provision of full relevant information by the importer derived from his commercial computerised system, which has been audited and approved by customs. Under the procedure of clearance on trader's premises, goods are directly transported to the importer's offices. The importer informs the customs administration that the goods have arrived, usually in sealed containers or road vehicles and are available for examination.

When a specified time has elapsed without customs appearing or informing the traders that they intend to do so, the goods are considered as released, subject to the subsequent completion of declaration and related procedures.

Operators have to apply to the customs authorities for the authorisation to operate under these simplified procedures in the same way as for suspensive procedures.

## **II.2. Different Corruption Practices**

The practices observed in the three countries (see Annex 1) show that each step of the customs chain can present an opportunity for a corrupt act (see also IECC, 1998)<sup>13</sup>.

While all such acts involve the use of public office for private gains (a customary definition) they vary in nature. They may be of three types:

- *Routine corruption*: private operators pay bribes to obtain a normal or hastened completion of customs operations.
- *Fraudulent corruption*: operators try to pay less tax than due or no tax at all, by not accomplishing properly the customs clearance process. They pay bribes to buy customs officers' blind eye or their active co-operation.
- *Criminal corruption*: operators pay bribes to permit a totally illegal, lucrative operation (drug trafficking, abuse of export of promotion scheme, etc.).

Field information indicates that routine and fraudulent corruption practices were so strongly present in the three countries, as to be commonplace. In the Philippines, for instance, according to Parayno, customs employees seemed to consider they had the right to compensation for their service. Likewise, most businesses had become accustomed to giving small bribes for customs services as part of their standard operating procedures. It was a general view that it was necessary to pay to “facilitate” even fully legitimate transactions, and to have the services of someone personally friendly with customs in order not to be unduly harassed<sup>14</sup>. Similarly, in Pakistan, Younas describes an elaborate system of bribes where money was levied for each and every transaction and shared thereafter among officials.

*Smuggling syndicates* operated an underground channel of trade in parallel with the normal customs process in the Philippines during and before the 1980s. They used all types of smuggling methods, including “technical smuggling” (i.e. smuggling done through a customs house) and “boat in the night” smuggling, but most operations would involve corruption of customs personnel. The involvement of officers could vary from sins of omission to a direct participation in the criminal activity. This underground channel was not solely anecdotal, as smuggling was estimated to represent in the 1980s from a low 12.2 per cent to a high 53 per cent of recorded imports. Lahiri, Nasim and Ghani (1998) give figures for an estimation of illegal trade in Pakistan of a comparable *ordre de grandeur*. “In 1993, it was estimated that illegal imports amounted to Rs. 100 billion compared to total legal imports of Rs. 259 billion. Industry sources estimate that the level has increased substantially since then”.

Arduz describes a similar system in Bolivia, where very few of the smuggled goods escaped totally from customs control. Most of them went through a system of *aduana paralela* (“parallel customs”), in which customs officers levied their own taxes for not registering the flows in the official system. In operational posts, smuggling and the permissive corruption arrangements were part of the daily activities. This was particularly important in customs posts far from the central office, for instance Puerto Suarez, where the smuggling of merchandise was alleged to be the main source of economic activity for the population. It was frequently said that only 20 per cent of the goods went through this post’s legal system, 80 per cent passing through the parallel customs.

Hence routine and fraudulent corruption practices were frequent and involved a great number of actors. The collection and redistribution of these rents were organised according to unwritten, commonly understood, rules. In Reisman's terms (1979), a double normative structure operated in these customs. The official laws and procedures, as set by the policy maker — the *mythical system* — fixed the ideal values and representations of the group, independently from the question of their practical pertinence and applicability. In parallel, a set of rules — the *practical code* — was applied *de facto*, which regulated when, how, for and with whom operators could do things forbidden by the mythical system.

Routine bribe collection for normal or accelerated implementation of customs formalities, as described above, became a practical code that ran alongside or replaced the mythical system of regular customs operations. Similarly, an arranged implementation of the tax structure replaced the official, mythical one.

Criminal corruption does not seem to have been so systematic. Information from the field leads us to think that these practices were more prevalent in Bolivia and Pakistan than in the Philippines. For instance, drug smuggling in the Philippines did not seem to involve the participation of customs officers. Although the Philippines are a known transshipment point for heroin and cocaine, from other countries (mainly Thailand) to the United States, there were no indications of any form of involvement of Filipino customs officers in any of the cases investigated. Nor was there any evidence that customs officers knew of or participated in smuggling, for use within the country, of methamphetamine hydrochloride (the poor man's cocaine, locally called *shabu*). This drug was, in fact, found to be mainly smuggled through shipside discharges, on the high seas, by fishing vessels and not through customs posts.

### **II.3. How Can We Understand This Phenomenon?**

A simple framework for analysis of corruption practices can be derived from observation of corruption practices in the three customs figuring in the study. This would distinguish between the *opportunity* for corruption and the *rationale* of the actors in seizing that opportunity, their *logic of action*.

Corruption was widespread in the countries studied because the customs environment provides numerous opportunities arising from three preconditions:

- a discretionary interface between customs officers and private operators;
- the possibility for customs officers to operate within a network of accomplices; and
- a lack of efficient controls.

At the same time, public and private actors have developed corrupt logics of action, which motivate them to seize these opportunities. The distinction, already made, between routine, fraudulent and criminal corruption, introduced different logics of action for those private persons engaged in these practices. Corresponding distinctions could also be made among the logics of action of the officials concerned. These logics of action depend on the personality of the individuals, but more importantly, they refer us to the broader social environment in which they operate.

Part a) describes those defects in the customs administrations studied that contributed to create opportunities of corruption. Part b) sets out characteristics of the broader environments that contributed to the development of logics of action<sup>15</sup>.

### ***a) Opportunities in the Customs Environment***

- **Discretionary Interface**

According to Parayno, complex and bureaucratic procedures in the Philippines required face to face interactions between operators and customs officers in practically all transactions — import entries, export entries, requests for transit and others. Customs handled about 4 million transactions annually. Each transaction required, on average, 10 separate processes. Taking into account the lack of controls and an encouraging broader environment, he estimates the number of corruption opportunities to have been not less than 40 million...

Similarly, Arduz reports that excessive discretion was common in the management of customs operations in Bolivia. Consignments were selected for control on a discretionary basis, without the application of objective criteria. Controls were based on physical inspections, with little use of technical methods. There was no efficient information system to enable control of operations in distant posts.

- **Possibility to Operate Within Networks of Accomplices**

The case studies also show how entrenched corruption affected the human resource management systems. The fact that appointments and promotions were influenced by corruption greatly facilitated the formation and maintenance of networks of accomplices. In Pakistan, for instance, recruitment, postings, transfers and promotions were not merit-based. Postings, which would lead to large receipts from bribery, were auctioned to highest bidders who, besides making down payments, undertook to make higher officials regular payments of specified amounts from their corrupt earnings.

- **Lack of Efficient Controls**

Another characteristic, common to all three customs environments, was the lack or inefficiency of controls, which left opportunities open for malpractice. In Pakistan, the Government Servants Conduct Rules adopted in 1964 specified the standard of conduct required from civil servants. The Efficiency and Discipline Rules provided an adequate legal framework to deal with cases of corruption, improper conduct and dereliction of duty. The 1969 Customs Act contained provisions to prosecute customs officers who connived at revenue leakage. The Chairman of the Central Board Revenue was responsible for drafting charge sheets for officers and supervisory officers in collectorates and directorates were responsible for lower employees. Yet, without the will to enforce the law, all these internal discipline mechanisms were purely decorative.

Another sanction in Pakistan is to post officers, thought to be corrupt, as “Officer on Special Duty” (OSD). They are then temporarily excluded from the public administration until a special OSD post has been created for them. Yet whenever this measure has been exercised<sup>16</sup>, there has been no follow up action. No charges have been framed, no sanction implemented. Shortly after posting as OSD, the affected officers manoeuvred their rehabilitation and returned to regular assignments.



Similarly, in Bolivia, the authorities lacked the will to implement controls and sanctions. Given its secret nature, corruption is, in any event, difficult to prove, but the process of incrimination on corruption charges was further constrained by the law SAFCO, passed in 1990<sup>17</sup>, which stipulates that corruption practices must be handled through formal regular judicial channels, rather than through administrative procedures.

The potential deterrent effect of repressive mechanisms was further weakened by inadequate sanctions. The maximum punishment for irregularities in the operation of customs procedures was dismissal from the customs administration. The 1986 Tax Code imposed important sanctions on private operators going through customs illegally, yet, these were never applied. Customs agents never denounce such commonplace fraud practices.

Furthermore even when cumbersome disciplinary procedures were initiated they took months, slowed down by the high turnover in customs staff, leading to a lack of continuity in the gathering of evidential proofs. When these were not completed within time, incrimination proceedings were usually abandoned.

## ***b) Influence of the Broader Environment***

### ***b.1) Public Actors***

#### ▪ Contrast Between Remuneration Level and Personal Expectations

One of the most important arguments invoked to explain customs corruption in developing countries is that of the *low level of wages*. In Pakistan, for instance, salaries have taken no account of inflation and the prices of essential living requirements. The salaries of low-ranking customs employees make it impossible for them to maintain reasonable standards. An employee living within his salary cannot rent a house or educate his children.

At higher levels in the customs hierarchy, however, this argument does not apply, as salaries are more than comfortable. This illustrates the development of *social expectations* linked to the posts in customs administrations. Among senior Pakistani officers for instance, ostentatious living and extravagant expenditures have become the norm. This attitude of customs officials has been conditioned by the mode set by a wider elite, customarily indulging in illegal activities and parading ostentatious riches.

In such different circumstances it is very difficult to draw the frontier between need and luxury. It would be erroneous, in this context, to try to make arbitrary judgements. There is probably a continuum of gradually changing situations between officers who are practically obliged to engage in corruption to provide for basic needs and those who are drawn to bribery by the pressures of social emulation and greed for opulence.

- Functioning of the Political System

Corruption can enter the political scene in various ways. For instance, an important feature of the Bolivian problem was the struggle between networks of power, seeking control over sources of rents provided by the customs administration and its system of parallel customs.

Once a network group obtained access to the administration, it placed its men at key points in personnel. Part of the resources subsequently levied from bribes was given to the authorities, which had backed their appointments, in return for that support. Groups excluded would then pressure and manoeuvre until they too would get part of the benefits. Once in power, in their turn, they would get rid of the past officers and introduce new ones...

This situation had serious consequences for human resource management in the Bolivian administration. Needless to say, recruitment had no relationship to objective criteria. Few employees were qualified to do their job. There was a very high rotation rate. About 70 per cent of the staff had less than one-year's experience. The figure was 100 per cent in frontier posts, which afforded the highest illegal returns.

#### *b.2) Private Actors*

- Growth in the Volume of Trade

When serious imbalances between supply and demand for public services appear<sup>18</sup>, market forces will progressively replace the administrative system of free resource allocation. In Pakistan, the growth in the volume of trade has not been followed by a subsequent increase in the means allocated to the customs administration. The resulting imbalance led to bottlenecks in the customs systems and long queues for import processing. As many private sector activities are time sensitive (especially in moving perishable goods), these delays in release/clearance encouraged customs officers to seek, and operators to propose, financial inducements for timely processing.

- Trade and Other Fiscal Policies Managed by the Customs Administration

The *high level* of taxes levied by the customs administrations provided strong incentives for fraud and corruption, especially where controls were inefficient, and where there was general distrust of the State.

In the three countries, the amount of tax amount collected was still substantial, although at different levels.

Pakistan like most developing countries applied an import substitution strategy, which relied on high tariffs, import quotas and exchange rate overvaluation<sup>19</sup>. In 1993-94, a major policy initiative envisaged a three-year phased reduction in maximum tariff rates, from 92 per cent in 1993-94 to 35 per cent by 1996-97. Good progress was made, in reducing maximum tariff rates down to 70 per cent in 1994-95 and then 45 per cent in 1997 but this latter figure was still high.

*Tax structure* is also an important factor. Private operators saw the grant of numerous exemptions as some justification for fraud, as there were no clear grounds on which certain privileged groups were allowed to pay less or no taxes at all. Such treatment was felt to be patently unfair.

It had been planned to compensate for the loss of revenue, consequent on reductions of the tax level by the withdrawal of tariff concessions and exemptions, and the receipts from a broadly based sales tax. But the flattening of the tax structure, which remained extremely complex, had only partial results.

As the Bolivian study shows, taxes, collected by customs, are not limited to import duties. In that country, Dr. Victor Paz Extensoro launched an important tax reform, in the wake of the 1985 New Economic Policy, leading to significant reductions in import duties. A simple formula, based on only three categories of goods, was introduced and is still in force. This taxed general merchandise at 10 per cent, capital goods at 5 per cent, and books and journals at 2 per cent. This radical simplification of tax structure greatly reduced abusive exercise of discretion by customs officers.

However, the customs administration was also mandated to collect internal taxes, such as VAT, on imported goods. These internal taxes exceeded the previous level of import duties. In 1998, for example, internal taxes collected on imported goods represented 70 per cent of the total taxes collected by customs, whereas import duties only amounted to 23 per cent<sup>20</sup>.

Hence even if import duties are further reduced, in tune with general trends towards globalisation and economic integration, customs will retain a major fiscal role, and incentives to bypass legal customs procedures will not disappear simply because of progressive trade liberalisation.

Developments in the Philippines seem to confirm the importance of tax levels. In the 1980s, many companies there were forced to connive with the smuggling syndicates, mentioned earlier, for reasons of business survival. Tight foreign exchange controls, a ban on a wide range of imports that were considered as “non-essentials” and high rates of import duty, combined to make the underground trade channel of trade a preferred route, even for legitimate businesses.

At the end of the 1980s, the two major reforms, primarily aimed to strengthen export competitiveness, the Tariff Reform Program and the Import Liberalisation Program, brought about a radical change in the nature of customs corruption.

With import liberalisation, accompanied by lower tariff walls and the removal of foreign exchange controls, many businesses realised that they could import without recourse to the syndicates. Consequently, they made less frequent use of such traditional “ways” as misdeclaration, misclassification and undervaluation, in formal entry declaration processing.

### III. FIGHTING CORRUPTION IN CUSTOMS: SOME FIRST ELEMENTS

#### III.1. Measures That Do Not Work: Examples from Pakistan, Bolivia and the Philippines

Several past measures to fight corruption and secure sustainable improvements proved ineffective.

- Purges

The Pakistan and the Philippines governments made several attempts to rid the administration of corrupt agents. These had, at best, only temporary effects. In Pakistan, under the Martial Law in December 1969, 303 higher-level officers, including 12 from the Pakistan Customs and Excise Service<sup>21</sup>, were removed from service. All were asked to make comprehensive declarations of moveable and immovable assets held in their own name and by family members. After due scrutiny, proceedings were undertaken against those who had assets out of relation to their legal income.

While this was generally perceived to be fair, the effects were short-lived. Civil unrest and turmoil after the separation of East Pakistan in 1971 created strong political instability and diminished respect for controls.

In the Philippines, the formation of a New Society, free of corruption, was one of the avowed aims of the martial law regime that came into force in September 1972. Massive purges of government personnel took place, affecting, particularly, the Customs Service. This was said to have produced some initial results, but as in Pakistan, these were short-lived while the martial law administration, itself, soon admitted a return to previous conditions.

Massive public protests, driven notably by a general discontentment in the face of notoriously corrupt State institutions, led to the February 1986 People Power Revolution. The subsequent change in leadership, toppling the 14-year old dictatorship, ushered in a renewed effort to combat graft and corruption, but, as the 1990 survey shows, the overall results were disappointing. At the Customs Bureau level, over 300 customs personnel, many of them senior officers, were purged on the grounds of an office reorganisation. These officials challenged the legality of these events in the courts and the subsequent legal battles were taken all the way up to the Supreme Court.

The end result was an effective block to all efforts, by the customs leadership, to make significant headway in its anti-corruption campaign.

- Reinforcing Investigation

In Pakistan, a specialised enforcement team, the *Enquiry Wing*, was created within the Central Board Revenue in October 1993 to improve the enforcement of internal discipline. The officers of this specialised body were to conduct inquiries and

monitor the progress of disciplinary cases once initiated, but the Wing had no real impact. During the period 1994-95, 220 disciplinary cases were opened in customs. Only 32 of these were of corruption, even though it was known that this was rampant. Forty two per cent were opened against *sepoys*, the lowest grade in the hierarchy. No case was laid against higher officials (i.e. assistant collector, deputy collector, additional collector and collector) who have important responsibilities in respect of collection of revenue and without whose collusion large-scale evasion is impossible.

After Mian Muhammad Nawaz Sharif assumed power in February 1997, the Prime Minister's *Accountability Cell* undertook investigations. In April 1997, 87 officials were suspended, including a number of senior customs officers. This was followed with action under (E&D) Rule, 1973. Charge sheets were issued. Enquiry officers were appointed and reported, but the cases initiated by the Prime Minister's Accountability Cell were perceived as highly coloured and one-sided. Far from eradicating corruption, across the board, it was made a highly politicised issue.

Earlier, in April 1973, a system of rewards, offering financial incentives to detect and denounce corrupt practices had been put in place, but this was ineffective because it was diverted to provide a new source of rents. In order to receive rewards investigating officers listed fictitious informers. Higher officers forced subordinate investigators to include their name among those responsible for detection and so entitled to rewards. In the end, the budget for this reward system proved inadequate.

In the Philippines, in the late 1980s, enforcement was entrusted to a select group, backed up by intelligence units from the private sector. These registered significant progress, resulting in the investigation and prosecution of many officers. Yet according to Parayno, this proved insufficient to produce any lasting change in the propensity to corruption.

- Verification Firms

In 1993, the Pakistani government offered a five-year contract to two preshipment inspection service (PSI) companies, Cotecna and SGS, to provide advice on valuation and assessment of customs duties and taxes for imported goods of more than \$3 000, leaving customs to collect payments. In November 1996, the government was dismissed on charges of corruption and the conditions under which PSI contracts had been concluded were investigated by the Accountability Cell, revealing that the two companies had made payments, into foreign bank accounts, in favour of the then President, Benazir Bhutto and her spouse.

In Bolivia, authorities tried to offset the institutional weakness of customs by resorting to PSI companies. In 1986, 1988 and 1990, successively, three companies (SGS, Veritas, and Inspectorate Griffith) were recruited by the government to check the nature and value of shipments (physical inspection of the goods, control of origin, control of quality and quantity)<sup>22</sup>. These firms were paid 1.85 per cent of the FOB value for imports, 1.55 per cent of the value for non-traditional export products and 1.6 per cent of the value for traditional export products. Importers, themselves, had to meet PSI costs for imported goods, whereas costs related to the control of exports were covered by the Bolivian State.

While the services provided by these firms reduced the abusive exercise of discretion by customs officers, in respect of verification, they made no real impression on the corruption problem. Firstly, corrupt practices were displaced to other points in the clearance process. Secondly, once identical shipments were found to have been valued differently by the same verification firm, the information on value, provided by these services, was no longer considered as reliable.

According to Arduz, the personnel of these firms, themselves, were not immune from corruption. Competition between the three firms, intended to lower costs borne by importers, stimulated the development of corrupt practices, for example the under-valuation of consignments in order to attract customers.

- **Systems of Rewards**

A system of rewards and commendations was set up in the Philippines, in the framework of the reforms initiated in 1986. But the same group of officials: the intelligence and enforcement officers kept on receiving these. According to Parayno, practically no one from the assessment group or any office outside of intelligence and enforcement benefited. Even among the privileged law enforcement personnel, very few officers were motivated by the prospects of receiving awards and commendations for doing a good job. Most made only occasional apprehension as a reminder that they should not be neglected. In fact, awards and commendations had little motivational value compared to the payoffs and other benefits they could get by simply closing their eyes and taking no action against smuggling syndicates.

### **III.2. The Need For Extensive Reform Programmes**

#### ***a) Analysis of These Failures***

These examples show clearly the difficulty of setting up efficient mechanisms of control<sup>23</sup> in a context of cumbersome procedures and loose management. Three conditions are required for the deterrent effect of controls to be effective: a strong, sustained will to succeed, a high probability of detection and reasonably severe sanctions.

There is little point in setting up control units if these, themselves, are not resistant to corruption and collusion develops between the controllers and the controlled. In Bolivia and Pakistan, sanctions of dismissal were obviously too weak. Even in the Philippines, where the investigation unit was considered to be efficient, results were lacking.

It might, therefore, be tempting to see harsher sanctions as a way to increase efficiency, but one might hesitate before following the example of the Chinese Anti-smuggling Investigation Bureau, with a strength of 6 000 special police officers and recourse to the death penalty. In any event, Ostrov (2000) considers that the professional integrity of this Bureau warrants concern. There is no mechanism to prevent the excessive use of force or the abuse of Chinese citizens' rights, as defined in the PRC Constitution. Moreover, as 35 per cent of the proceeds from

confiscated goods revert to the anti-smuggling units, there is a built-in incentive to be aggressive in the enforcement of regulations or even to manufacture evidence.

The participation of PSI or other private firms in the handling of some operations may yield some positive results, but it seems that the changes so introduced have no real effect on corruption. Experiences studied show that resorting to private firms poses several problems. Firstly, their controls can be diverted or manipulated. Secondly, the introduction of a private firm may improve the conduct of one operation, but if the full chain is not covered, corrupt arrangements can be shifted to along the line. Finally it is now well known that these firms, themselves, can be corrupted.

Installing positive incentives, through awards and commendations, also appear ineffective, when not accompanied by other reforms. In the Philippines experience, such inducements to honesty had little attraction compared with the bribes and other advantages derived from corruption and collusion. This is borne out from a case observed in Indonesia where a water supply concessionaire firm under contract to the Central Government had to face the hostility of the staff of a partner local firm. The concessionaire firm proposed a 20 per cent increase in the wage level, whereas through corruption, employees would multiply their wage by 3 or 4 (see Michelon, 2000).

#### ***b) A Convergence of Views on the Outline of Reform Programmes***

The conclusions drawn from these failures support the now commonly accepted view that there is no quick solution to the issue of customs integrity. Grafting control or reward mechanisms on complex and burdensome procedures does not produce results. A comprehensive approach is necessary. Landmark documents, including the Arusha Declaration drafted by the WCO, the IMF Integrity Paper and the conclusions of the Working Group on Customs Ethics in Central and Eastern European countries, yield convergent views on sound remedial action (See Annex 2 for a detailed comparison). These institutions recommend the following changes in customs administration:

- Organisation of Customs Operations:
  - define targets and standards of service quality;
  - segregate functions strategically and build checks and balances;
  - frame customs procedures so as to reduce to a minimum the inappropriate exercise of discretion;
  - computerise customs operations;
  - minimise the requirements of information and documentation from traders.
- Staff Rules:
  - develop a code of conduct and explain its implications to customs officers;
  - define corruption and related offences in legal texts and in the customs internal rules;

- set corresponding sanctions at a reasonably dissuasive level (including in internal disciplinary measures the possibility of dismissal).
- Internal Culture:
  - promote customs service standards and ideals;
  - develop an “esprit de corps”, based on a sense of loyalty and pride in the customs service.
- Information Production and Investigation:
  - give line-managers the prime responsibility for identifying weaknesses in working methods and in the integrity of the staff;
  - set up internal audit mechanisms;
  - conduct regular external audits;
  - set up an internal affairs unit with the specific task of investigating all cases of suspected malpractice, in complement to internal audit;
  - allocate examinations of customs officers randomly;
  - take measures to allow feedback from private operators;
  - follow the employees' assets, by organising disclosure.
- Human Resource Management:
  - adopt an objective recruitment process, immune from interference, based on knowledge and standards of personal ethics;
  - adopt an objective promotion process, immune from interference, merit-based and jeopardised by inappropriate behaviour;
  - relocate regularly the staff;
  - provide professional training to customs officers throughout their careers, including on ethics and integrity issues.
  - provide a remuneration sufficient to afford a decent standard of living, including, in certain circumstances social benefits such as the health care and housing facilities.
  - set up incentive payments.
- Relations with Customs Brokers and the Business Community:
  - facilitate access of private operators to information on regulations and procedures;
  - organise liaison committees with the business community;
  - make appealing against customs decisions, with, in the final instance, recourse to independent adjudication, possible.



In addition, all three study papers link the reduction of corruption with broader policy measures, at the national level. Import tariffs should be reduced where possible and the number of rates limited. Administrative regulation of trade should be reduced to an absolute minimum and exemptions to the standard rules should be as few as possible. Additionally, the customs administration should enjoy sufficient autonomy and should notably be insulated from the interference of politicians, whose influence should be limited to definition of the customs mandate.

It is important to outline these elements of remedial action, answering to a diagnosis of organisational defects and those characteristics of the broader environment that are conducive to widespread corruption, but much additional information and guidance is required to set up a full-fledged strategy.

The Arusha Declaration and the IMF Paper identify several essential conditions for successful reform. Both stress the importance of “a firm commitment at the highest political and administrative levels” (Arusha Declaration) or in the terms of the IMF Paper “a clear and unequivocal commitment from the Government”. The IMF paper goes further and points out three supplementary conditions: an atmosphere where importers and exporters will come forward and discuss the decisions that are being made and the existence of an independent judiciary and a free press. Analysis of the reform experience of Pakistan, Bolivia and the Philippines complements these assertions.

## IV. THE REFORM EXPERIENCE OF THREE DEVELOPING COUNTRIES

### IV.1. A Recent Initiative in Pakistan: The PRS Project

#### *a) Description of the Project*

The Central Board of Revenue (CBR) of Pakistan had repeatedly failed to reach assigned revenue targets. It collected Rs 282 billion against Rs 336 billion for 1996-97, Rs 293 billion against Rs 354 billion for 1997-98 and Rs 308 billion against Rs 355 billion for 1998-99. Proportionally to their fiscal weight, customs accounted for the largest shortfall in this latter period: Rs 61 billion of customs duties were collected against the budget estimate of Rs 90 billion (shortfall of 32 per cent).

In 1998, in the framework of an enhanced structural adjustment programme, the Pakistani government accepted an IMF condition for extensive reform and reorganisation of the CBR. Expert studies, funded by the World Bank, recommended that the CBR be converted into a modern, autonomous, “non-political system that provides equitable treatment to all tax payers”, the Pakistan Revenue Service (PRS). In support of this reform, a technical assistance project, partly financed by the World Bank, had been designed, to “improve taxpayer compliance with tax laws, reduce compliance costs and assist in raising tax revenues”.

The PRS project planned to<sup>24</sup>: re-engineer existing processes, as well as the human resources, training, facilities and information system support areas, enhancing where appropriate, the use of information technology; create information, advice and education services for taxpayers; and use improved methods to increase compliance.

Corruption in the tax collection machinery was acknowledged to be one reason for shortfalls<sup>25</sup>. The fourth section of the draft Public Revenue Authority (PRA) Bill<sup>26</sup>, the legal basis for the PRS, concerning discipline and integrity management included:

- i) the induction of persons having the highest levels and standards of skill, honesty, integrity and professionalism into PRS;
- ii) the methods of promotion, transfer, deputation, demotion, removal and dismissal applicable to employees of PRS, the highest consideration being given to integrity, merit and administrative justice;
- iii) the establishment of performance standards for employees of PRS including the framing of rules allowing the PRS to give rewards, entitlements and bonuses to such employees on the basis of merit and performance standards;
- iv) the prescription of fair and expeditious rules setting forth disciplinary procedures and methods applicable to the employees of PRS;
- v) the prescription of methods of continuous appraisal for employees of PRS; and
- vi) disclosure by employees of PRS of assets owned directly and indirectly by them and their family members.”

Legislation establishing the PRS was to be presented for enactment to Parliament by 31 December 1998. In the end, however, the PRA Bill was never enacted and the government lost interest in the project.

### ***b) The Reform Context and The Reactions of Different Actors***

Why did this project fail? Firstly, the reform project did not have the benefit of a straightforward reduction in tax level and simplification of structure. Groups benefiting from concessions and exemptions were opposed to any reforms that would eliminate these. Although good progress has been made, hesitation in reducing maximum tariff rates, while partially due to the effect it may have on revenues is related, more importantly, to the effect it will have on these special interest groups.

Quoting Lahiri, Nasim and Ghani (1998): “These interest groups benefit from a wide range of discretionary concessions: some groups are allowed imports at zero duty and others at reduced rates. The concessions are considerable. In 1994-95, revenue foregone due to these concessions amounted to Rs. 68 billion (55 per cent of potential tariff revenues). Well-organised groups, typically representing a limited number of large organisations, obtain such concessions through lobbying.

Those who would benefit from overall reduction in tariff rates, however, are typically less well organised than these groups and consist of a large number of small firms. Thus policy is influenced, largely by default, in favour of groups currently enjoying concessions. Having obtained such concessions, these groups are not interested in overall reduction in duty rates. Indeed duty reduction would decrease the comparative advantages of concessions. In effect, therefore, the government is constrained to continue with a high tariff regime, because of extensive concessions already given to influential lobbies”.

Secondly, even if the general public and segments of the private sector would tend to support a reform programme, the way this was designed and implemented failed to assemble and exploit these favourable elements.

The problem of corruption has attracted much attention in Pakistan in recent years. Successive governments have been dismissed on corruption charges<sup>27</sup> and, after each dismissal, there has been a public demand for across-the-board accountability and punishment for culprits. Several associations of entrepreneurs have agitated, specifically, for customs reform. The Committee on Taxation of the Federation of Pakistan Chamber of Commerce and Industry (FPCCI) have asked the Prime Minister for a drastic cut in the level and number of taxes and for a reduction in harassment by collecting agencies, so that managers can devote their time and energy to promoting their businesses. Similarly, the Pakistan Hosiery Manufacturers Association (PHMA) threatened a sit-in by its members at Karachi Press Club if the government failed to remove “corrupt” CBR officials.

The PRS project arose from a decision of the Prime Minister of Pakistan in consultation with a committee set up to restructure the CBR, but this consultation did not involve protesting associations of entrepreneurs or taxpayers. The diagnostic reports, justifying the PRS project, were never made public, and matters progressed without any public participation. Finally, the PRS project was presented in an unfavourable light by the media, as a conditionality linked to an IMF structural adjustment programme.

Also, difficulties were foreseen regarding the transfer and recruitment process. While the PRA bill proposed to select cadres from the two constituent CBR bodies, the Pakistan Customs and Excise Service and the Pakistan Taxation Service, and, after three years, to recruit from the private sector, there was no clear published information regarding this process or the appointment of top management. Doubts have been expressed as to whether it would be possible to conduct objective recruitment, free from the influence of various power groups.

It is equally uncertain how defects in enforcement capability would have been rectified within the newly created PRS. The provisions to ensure integrity and curb corruption were no more specific or stringent than those in the Government Servants Conduct Rules of 1964 and of the E&D Rules of 1973<sup>28</sup>.

There was no indication how implementation would have been improved in the new framework.

The reform programme confronted opposition from several quarters. Not surprisingly, employees in customs and other affected departments have opposed the PRS reform through covert lobbying. As we have seen, previous years had witnessed growing interference in customs administration by the political elite, leading to an all-pervading sense of insecurity amongst customs officials, who see corrupt practices as the best way to achieve their main aim of early financial security. At the same time, government servants who do not comply with the wishes, desires and undue demands of ruling politicians have to face transfers and at times even removal from their service. Honest officers, despite good work, are open to condemnation at the whim of political leaders.

The reform also attacked the interests of the huge underground economy and crime syndicates. Enforcing taxes and combating smuggling implies stiffening resistance to the mafias who control smuggling, fraudulent transit trade, illicit arms and ammunition or narcotics. Government enforcement agencies have to combat the combined muscle of a range of intertwined criminal structures. This could explain why the government has done so little to curb markets, which sell smuggled goods and flourish without any fear of repression. The last government action against open sale of smuggled goods was a raid at Rawalpindi in April 1975. This was called off after a few hours and confiscated smuggled goods were returned. Since then markets for smuggled goods have operated, without any intervention, in all major towns.

The government has now established a new task force to develop a new tax administration reform programme, and may again seek World Bank support.

#### **IV.2. A Major Reform Programme in Bolivia: *Programa para la Implantación de la Nueva Estructura de Aduanas***

Between 1991 and 1997, an important customs reform programme, the *Programa para la Implantación de la Nueva Estructura de Aduanas*, was undertaken in Bolivia. It was supported by the Inter-American Development Bank (IDB) through two successive agreements which extended between April 1991 and May 1995<sup>29</sup> and between December 1993 and April 1997<sup>30</sup>. It helped progress on several fronts, notably through strengthening general logistics of the administration, but failed significantly to improve integrity.

The reform programme was designed to attack all the weaknesses of the institution in the following directions:

- the consolidation and modernisation of the legal bases of the customs administration;
- a revision of the human resource management system;
- the construction of additional posts;
- a revision of customs procedures with the introduction of management and computer systems.

##### ***a) The Reform Context***

The objective of the programme was to increase the collection of public revenues. The reduction of corruption was not explicitly mentioned among the objectives. At the time of the reform, politicians were not so sensitive to the corruption problem, as they are today. After the period of high inflation of the beginning of the 1980s, attention was focused on the need to stabilise macro-economic indicators, and, more generally, consolidate the economy.

At the beginning of the 1980s, the public condemned corruption, in general terms, but their attitude was relatively passive. In the private sector, some companies had demanded reforms as smuggling brought goods on to the market with a price advantage of 20 per cent, but the reform failed to associate the private sector, either in the design of the programme or in its later implementation process.

Not surprisingly, there was opposition from certain politicians and power groups as well as from those individuals engaged in the parallel activities of customs posts. In Bolivia, this opposition was covert and failure to take underlying forces and interests into account contributed to the failure of a number of measures.

## ***b) Analysis of the Impact of Some of the Measures Taken***

### ***b.1) Selection of Honest Agents***

One of the measures conditioning IDB financial support for the second agreement was a transparent and objective process for the recruitment of qualified human resources. One hundred and twenty civil servants had to be recruited within 10 months. The difficulty of implementing this simple measure showed the strength of the networks' hold on the customs administration.

In 1993, the entire staffs of airports customs posts, from lowest grades to managers, were replaced, and qualified personnel were hired. Similarly, new staff were recruited in the Central Office.

These changes gave positive results. Even if, in the beginning those in restructured posts did not have the support of computerised operational systems, tax collection increased and the quality of service to private operators improved. The efficiency increase was such that it was observed that some flows were reported to other customs posts.

The advances were of short duration. As elections approached previously selected officers were gradually replaced, under strong pressures from political circles. Those who remained in place ended up either entering the corruption system or resigning from the service. As a result, even if at some stage more than 120 agents had been properly incorporated in the customs staff, yet at the end of 10 months after its initiation the programme had not met the target imposed by IDB.

In 1997, a last attempt was made to meet the IDB requirement as part of a broader reform of the human resource management system (Implementation of the *Sistema Integral de Recursos Humanos*). Special software was acquired, including a module for recruitment process. Sixty agents were selected, but none of them was ever integrated into the customs work force. First, national elections delayed the process, then the new government team, invoking political interference into the selection process, failed to validate the nominations.

### ***b.2) Remuneration and Employment Conditions***

Remuneration levels for customs officers were raised in parallel with the recruitment process, but this did not produce the expected results. One reason was that the administration refused to offer job security. Officers, fearing that their stay in customs would only last a year or so, continued to abuse the powers implicit in their responsibilities to levy as much as possible for their personal benefit while still in post.

### ***b.3) Privatisation***

The reform strategy included a partial privatisation of customs functions. One of the first actions taken in the framework of the programme was a resort to private firms to operate several customs posts. In 1993, inland posts and several airport posts<sup>31</sup> were privatised. In 1997, newly constructed frontier posts and several sub-administrations were also partially privatised. The private firms were selected through international bidding procedures.

Key tasks of document and physical inspection continued to be handled by customs officers. Private firms were entrusted with registration and numbering of customs documents, custody of merchandise, valuation of merchandise and recovery of tax due.

These firms, like PSI companies, are not, themselves, immune from corruption. For example, concessionaires operating at the Cochabamba post were detected in fraudulent activities. Yet, again as for PSI, the participation of private firms in the handling of some operations had some positive results. In the end, however, the changes thus introduced had no significant impact on the corruption problem.

#### *b.4) Changing the Norms and Procedures and Reinforcing Computerisation*

In the last two years of the reform programme, 72 texts defining norms and procedures, based on work in international trade fora, were developed<sup>32</sup>, yet few were implemented.

Some of these changes were supported by the introduction of computer applications. For example:

- working procedures for the inland, airport and frontier posts were revised and this was accompanied by the introduction, at inland and airport posts, of the first computer system to support customs operations (*Sistema de Administracion de Recintos Aduaneros, SARA*);
- a control system was developed to identify transit consignments failing to arrive at the outgoing customs post. Supporting software was introduced in 1996 and this enabled the identification of a number of missing transit consignments;
- in 1997, after their partial privatisation, a computer system was set up for frontier posts (*Sistema de Aduanas de Frontera, SAFRO*);
- software was used to revise the procedures and technical specifications of the census system for forwarders.

These measures had mixed results. In the case of the transit control system, smuggling through diversion of consignments to the internal market was not eliminated, as corrupt practices shifted to the point of approval of the documents presented by transporters to SNA to certify that consignments had arrived at the outgoing customs post.

Some computerisation projects were conducted hastily, without a proper analysis and revision of the procedures beforehand; timetables were cut and technicians without customs expertise were used. Lacking understanding of previous customs operations and associated failures, these technicians incorporated inefficient procedures including excessive intervention by customs officers, into the computerisation process.

While rapid large-scale computerisation is impracticable, the build-up in Bolivian customs left many serious gaps.

In the end, computerisation failed to cover implementation of such tasks as the control of merchandises in transit, the verification of the values estimated by PSI firms and the verification of certificates and authorisations presented to customs, and so left important opportunities for corruption.

Moreover, computer systems were not always reliable. Once the technical experts responsible for systems installation left, these often broke down. Finally, the various computer systems were developed using different platforms (Unix-Informix, Wang, SID, DOS, and Access). As they have not been properly integrated, exchange of information remains difficult.

### ***c) A Programme Finally Given Up***

Withdrawal by the IDB in April 1997 from its commitment to the reform programme led to its suspension. Among the reasons invoked by the Bank were failure by the reforming team to meet three conditions; the incorporation and training of 120 officers, the construction of a customs post at Arroy Concepcion<sup>33</sup> and a number of recommendations in the development of an audit system.

Mistakes in the management of the reform process contributed more generally to the failure of the programme. There was no strategic thinking behind the implementation process and sequencing. Mechanisms to control implementation of reform measures were inadequate and, in many instances, operative customs posts did not apply specified improvements.

Furthermore, it was only at the end of the reform effort in 1996 that a general framework and schedule was established to co-ordinate reform efforts between different parts of the tax administration, with clearly spelled out objectives and responsibilities.

While a Committee was then set up to monitor the reform process, this made no attempt to draw on representation from civil society and the private sector, and, in the end, failed to fulfil its intended role.

Even if the reform programme had not been designed to reduce corruption, the measures planned could have made a contribution in this direction. Indeed most of these figure in common recommendations on how to fight corruption, set out in Part III of this study.

Unfortunately, however private operators and journalists testify that what happened was just the contrary. Corruption increased rather than decreased. Since mid-1997, there has been hardly a week without the publication in the press of an article on rampant corruption in customs. While this may witness to the emergence of a stronger sensitivity to the problem, resulting in its wider exposure, it nevertheless proves that corruption is still very present. The current government has initiated a new reform programme, which takes a much more central account of the corruption problem, but it is too soon to evaluate the results.



### IV.3. Philippines

In the Philippines, even if major economic restructuring reforms were already in an advanced stage, in the late 1980s, there were still many incentives to commit fraud. Corruption flourished in a customs administration choked by red tape and cumbersome procedures. Import restrictions and exemption laws, with unclear guidelines and procedures for application, were numerous; tariffs were still significant. Consequent inefficiencies placed the Philippines and the local operators at a considerable economic and commercial disadvantage regionally and internationally.

In 1992, one of the immediate concerns of the newly elected government was the budget deficit. The customs administration, in particular, was behind its revenue target by over 3 billion pesos (\$115 million). Four days after assuming his post in June 1992, the newly elected President Fidel Ramos called the incoming customs commissioner and gave him a very simple marching order "to remove all 'kalokohan' (foolishness) in customs". The resulting reform programme, *Customs Development Towards the Year 2000*, enabled significant progress in the improvement of tax collection and the reduction of corruption. It was also beneficial in terms of trade facilitation. Several testimonies bear out these achievements.

The President of the Federation of Customs Brokerage Companies in the Philippines reported:

"You have to be really blind not to see the impact of the reforms and computerisation of the Bureau. We must acknowledge at least two things: first, you can see the great improvements in the physical structure. Second, we are seeing today the remarkable improvement in the rendition of basic service to insure the smooth flow of trade."

In June 1996, the Civil Service Commissioner Ereneta, testifying before the Committee on Civil Service and Professional Regulation on bureaucratic red tape gave the top 10 offices where red tape is most pervasive. The Bureau of Customs which years before was perceived to be among the most bureaucratic was no longer on the list.

#### ***a) The General Philosophy of the Programme***

The primary objective of the reform programme was to increase the efficiency of tax collection, but it was clearly understood that this required a solution of the corruption problem in collection agencies. An innovative approach, based on an extensive re-engineering of the customs environment, was developed. Its philosophy can be summarised in three points.

First, the existence of abundant opportunities was recognised as a crucial feature of widespread customs corruption. As mentioned earlier in the study, the total number of opportunities, each year, could be estimated as not less than 40 million,

so reform had to aim at a drastic reduction of interactions between officers and private operators.

Second, the strategic assumption was made that providing a convenient and efficient customs service, free of routine corruption, to private operators would greatly facilitate the attack on other corruption problems. This line of action would get the support of all firms willing to pay their taxes. It would also contribute indirectly to reduce opportunities of corruption linked to illegal practices. The legitimacy of tax collection would be reinforced. Finally, personal networks to facilitate customs processing, which could easily develop into corrupt arrangements, would not be needed anymore.

Third, it was acknowledged that, while the support and commitment of the formal and informal leadership in the customs organisation was highly desirable, it was not realistic to expect real commitment and support from the staff. The compensation package of customs officers paled in comparison with the rewards they gained through corrupt practices. Even with increases in wage levels, the interest of the staff could not be substantially aligned to the programme objectives and it would be ill advised to depend heavily upon the customs personnel to stop smuggling or to reduce routine corruption. It would be counterproductive to increase the level of control and discretion of customs officials over the flow of goods and the processing of documents. Reform leaders had to be prepared to apply sanctions.

The reform programme eventually benefited from import liberalisation and tariff restructuring (removal of quantitative restrictions and the lowering of duty rates respectively). The country's accession to the WTO, general business acceptance that protection of industry with high tariff walls had not been good for the economy and the country's commitment to the APEC, were trends rightly perceived as irreversible. As already mentioned, misdeclaration, misclassification and under-valuation in the formal entry declaration processing became less frequently used as smuggling methods.

The reform programme took advantage of this development. Whereas, before, customs had to spread modest resources thinly across all these threatened points, the level of controls could, in future, be reduced.

Resources could be deployed from low risk importers and procedures (mainly in formal entry processing) to those operations that remained high risk such as consignments going to the bonded warehouses, container yards and container freight stations.

### ***b) Outline of the Programme***

A customs reform undertaken, at a quite rapid pace, over more than five years, involves many measures. The following paragraphs set out the overall approach as well as the general lines of the implementation process, which included several axes.

The first reform axis was a comprehensive computerisation of many of the traditional customs activities: computation of duties and taxes, collection of duties and taxes, determination of payments made, issue of release instructions for shipments to the cargo handler, record-keeping of documents receipts and releases by various offices, selection of consignments for examination and the assignment of the customs officer who will conduct the examination. These changes produced a significant reduction in paper work and in the number of steps and signatures needed to complete a transaction.

A second axis was the introduction of a risk assessment system that would allow customs to limit the number of transactions needing to go through intensive processing. In such a system, the probability that a shipment may be subject to violations is assessed by comparing its details against a number of reference tables and files. Only those ascertained to be high risk are required to go through the regular clearance process. Those profiled as low risk are channelled through a green lane, with a clearance process that does not involve coming to customs or seeing any customs officer.

In the re-engineering systems and procedures, careful attention was given to placing necessary controls outside the normal process flow. Apart from the selectivity system, mentioned above, this applied to other arrangements such as post audits, advance processing and the segregation of control and enforcement activities from the declaration, assessment, and collection and cargo release operations.

This made sense in two respects. First it made it possible to offer a fast customs clearance process to firms who were co-operative and fully compliant with customs requirements in a transparent manner, and so facilitate trade. Second, it enabled empowerment of those officials who sincerely wished to contribute to organisational objectives, while at the same time reducing the discretionary power of the majority who were utilising their positions for personal aggrandisement.

Finally, in view of the propensity of internal staff to suppress any objective picture of the level of corruption as well as to cover up for one another, the leadership used external help — an independent auditing unit, reporting directly to the top leadership and the business sector.

Specific measures undertaken to fight routine corruption included:

- reduction of face to face customs/trader interactions in the cargo clearance process;
- removal of queues and bottlenecks;
- formulation of clear, simple assessment rules;
- privatisation of certain operations;
- rationalisation of the issuance of hold, alert and mission orders;
- enhancement of transparency in the conduct of operations;

- comprehensive application of information technology to replace manual processes with automated systems;
- provision of a paperless and cash-less clearance process.

To ensure that revenue generation was protected, even though drastic steps were being applied to fight routine corruption, a number of short and long-term revenue enhancement programmes were set in place to free the system from weaknesses and vulnerabilities, as follows:

- empowerment and encouragement of relevant private sector associations to detect and report instances of smuggling, at the same time as they rid their own ranks of violators;
- encouragement of friendly and constructive competition, among the various law enforcement units, in the fight against smuggling and other forms of revenue fraud;
- extensive application of information and encryption technology in the electronic transmission and utilisation of payments, release instructions, exemptions and other sensitive customs data;
- use of advanced technology (such as global positioning system) in the tracking and accounting of transit cargo;
- closure of customs warehouses, container yards, freight stations and other customs facilities used as conduits for smuggling, at the same time as regulations for licensing new facilities were being tightened;
- strengthening of the audit process;
- strengthening of investigation, prosecution and intelligence offices.

### ***c) The Reform Context***

The political will, at the highest level, was strong. President Ramos was strongly committed to the reform and, in line with generally accepted anti-corruption principles, supported by a like-minded team, including the Secretary of Finance and senior officers of the Department.

The media expressed general support for the fight against corruption, and, once started, for customs reform. On repeated occasions, however, these media have been bought by opposing interests.

The private sector was a crucial ally and two of its major interest groups clamoured for reforms. On the one hand, the Philippine Chamber of Commerce and Industry (PCCI), grouping exporters and export-oriented manufacturers, complained that the excessive bureaucracy in customs discouraged investments (especially foreign direct investment) in the economy and made exports uncompetitive. The delays associated with inefficient clearance procedures made manufactured exports, dependent upon imported inputs, less attractive than those from other countries. Importers serving highly competitive export markets are unable to absorb these

additional costs of bureaucratic red tape, unlike other importers who are able to pass them on to local consumers.

On the other hand, the Federation of Philippine Industries (FPI) demanded greater vigilance from customs in assessing and enforcing import controls because of the unfair competition of smuggled goods. Members of PCCI from the legitimate trading sector also complained that smugglers were practically forcing them towards underground trade and illegal channels. Smuggling, facilitated by corruption, threatened business viability.

The main opposition to the reform was expected to come, and, in fact, came, from the rank and file of customs itself. Even before joining the administration, a customs officer already had a pre-conceived notion that corrupt practices would ensure his enrichment. Customs officers objected to the “loss of control” that resulted from the reengineering of the clearance process and the conversion of the Customs Clearance System from manual and paper based methods to an electronic, paperless and automated system.

The main features of the new clearance system that internal staff had the principal difficulty in embracing, or agreeing to, were, effectively, those that did away with the face-to-face interactions with traders. Prominent, among these, were electronic lodgement and processing of entries, the selectivity system, mandatory payment through the commercial banks including use of in-house banks, automated verification of payments, electronic on-line release of goods and post audit mechanisms which drastically reduced the opportunities for corruption.

Customs employees undertook judicial and legislative actions to try to delay the reform process<sup>34</sup>. They tried to negotiate with the commissioner to leave some manual processes that they could still use as opportunities for the commission of corrupt acts, on the pretence of wanting to help the proper enforcement of customs laws and improve revenue generation.

Smugglers and other adversely affected private sector groups could hardly complain publicly against these reforms, but they took action against the “tightening of the noose” by, for example, instigating brokers to undertake a “sit-down strike” against a measure which addressed the modus operandi of breaking up a shipment into small parts to avoid or circumvent controls.

When many bonded warehouses, used as conduit for smuggling, were closed, a number of operators filed civil and criminal cases in court against the customs commissioner and used the press to attack him in the eyes of his superiors and the public.

#### ***d) How was the Reform Implemented***

The programme was never presented as a frontal attack on corruption, though those in charge of its implementation were fully aware that the major difficulty of the reform would lie in opposition from those benefiting from corrupt practices. The strategy developed, in response, rested on the following elements.

#### *d.1) Action of the President and His Team*

President Ramos demonstrated his support by coming to the customs yearly, without fail, to express, before the entire officialdom, his keen interest in the reforms being undertaken, to see for himself what had been accomplished, to recognise those who contributed most and to warn all those who opposed the changes. He augmented the budget for reform and modernisation by certain amounts from the President's contingency and social funds. He set the example in complying fully with customs laws, rules and regulations and making his family, relatives and friends do the same. Furthermore, the President provided the customs commissioner with strong moral support, and accepted the commissioner's recommendations on many sensitive issues.

The Secretary of Finance and the senior officers of the Department regularly mentioned the reforms, being undertaken in customs, in their speeches and press conferences. The commissioner, himself, devoted a significant portion of his time to communications. He gave regular interviews to the media, and had information brochures, leaflets and video documentaries produced to inform all stakeholders in customs activities, including the Senate and the House of Representatives.

#### *d.2) Monitoring Progress*

The commissioner personally monitored the progress of reforms to reduce the opportunities for corruption in the cargo clearance process. For that purpose, he kept track of the number and percentage of imports going through the green lane as against those going through the yellow and red lanes, the number of manual interventions remaining in the green lane processing, the length of time to complete cargo clearance for all three channels — green, yellow and red — and the number and percentage of declarations going through the remote entry lodgement procedures as against those going through the service centres. These statistical controls were complemented by on-site inspections through which the commissioner checked the correct implementation of reform measures.

#### *d.3) A Real Involvement of the Private Sector*

The active participation of the private sector was sought, up to the point at which responsibility in the conduct of reforms was shared. Associations were not just informed and consulted but made a partner in the design and implementation of these reforms and several private associations participated in the monitoring process. In the end, they took pride in the success of the programme and in its reports.

Some private associations assumed the role of adviser. Associations such as the Chamber of Customs Brokers, the International Federation of Customs Brokerage Association, the Federation of Air Cargo Forwarders and Brokers, the Customs Checkers and Representatives Organisation were regularly consulted on various reform components. These associations provided constructive advice on the draft rules and regulations and frequently called attention to areas that had been overlooked or needed strengthening. They likewise gave constructive advice on how best to implement initiatives.

These associations and the Association of Port Users also participated in orientation and training programmes for sectors affected by the reforms. The Chambers of Commerce also contributed to reporting the progress and results to the media, and through their internal communication and publication networks. They played a key role, by organising workshops, in informing private operators of new developments in customs they ought to know about and take advantage of. These organisations were motivated in making such reports to their memberships because the customs accomplishments were their accomplishments also.

Private associations also assembled material and financial support for some of the reform projects. Private sector groups who were benefiting directly from these funded several early information technology initiatives. The airlines and shipping lines, the banking community and the chambers of commerce contributed technical personnel, hardware and even office furniture and equipment. The Chamber of Customs Brokers sponsored a yearly golf tournament, the customs commissioner's Cup, a fund raising campaign, all the proceeds of which were spent on the programme. This chamber made possible customs interconnection with SITA, the *Société Internationale Télécommunication Aéronautique*, for advance submission of cargo and passenger manifests. They also funded the renovation of collection and assessment offices in the port of Manila.

The Chamber of Customs Brokers were designated, by the Philippine Chamber of Commerce and Industry as the managers of the Community Trading Centres, showing a close collaboration between this group and the customs authorities in ensuring that the system functioned correctly. These centres provide entry-coding services to digitise paper declarations into electronic files, so that these can be processed, electronically, by the Bureau's Automated Customs Operating System.

#### *d.4) Sequencing to Manage Change and Oppositions*

Many potential difficulties, linked to the management of change, were avoided because timing, sequencing, and methods of introducing the various components of the programme were carefully thought out, ahead of time.

Payment accounting and reconciliation components, identified as the most vulnerable stage of the clearance process in many cases of detected and publicised fraud, were among the earliest to be addressed. The first deployments were perceived as the management's legitimate response to serious threats and were thus taken favourably by the majority of internal staff.

These first actions were preceded by the renovation of the associated working areas, to make them harmonise with and support the re-engineered process. Collection offices were renovated to first class standards. This development was welcomed by internal staff who showed appreciation for these changes, although some had an early inkling of the purpose of the exercise. It helped create favourable expectations for ensuing reforms.

The main software for the customs clearance process was introduced in stages and by modules, taking account of the learning capacity of the personnel as

well as their attitude to change. The first module put in place was the automated computation of the duties and taxes payable. On the morning of implementation, the commissioner addressed the entire workforce to explain that the change simply equipped assessment personnel with powerful calculators to help them in the computational aspect of their work, and that, with these “oversized calculators”, they could concentrate on the more important and sensitive aspect of their work, the correct classification and valuation of shipments.

It was only much later, after the staff became proficient with the non-controversial components of the software, that the sensitive modules were introduced. Before the selectivity system was implemented, the commissioner again met the staff, assuring everyone that no one would be removed or asked to resign because of the reforms. He explained that they would continue to have important functions in the clearance process and that the controls against customs fraud were not being reduced but simply being moved to where they could not interfere in the efficient clearance process particularly of legitimate importation.

In the same way as for the payment system, the implementation of the clearance software was preceded by the renovation of working areas to first class standards.

#### *d.5) Measures to Overcome the Resistance*

A communication programme was undertaken, to counter the adverse information campaign conducted by some customs employees, and to develop support for the reform programme, by highlighting public sector endorsement and creating a wave of indignation against customs personnel and others opposed to the reforms.

Special efforts were also made to develop communication and information materials on customs reform to help supportive managers in customs explain the need for, and the expected benefits and outcomes of, the reform, describe its salient features, and answer personnel reservations and fears.

Visits of business leaders, importers’ and exporters’ groups, national and local government officials from the three branches of government, as well as other stakeholders including high government officials from other countries and international organisations, were organised to develop an appreciation of the importance of the reforms they were undertaking among customs personnel.

Port Founding Anniversary celebrations were used as a vehicle for showing what the ports had accomplished in reform and modernisation. Similarly, participation in conventions and exhibitions provided occasions for the Bureau of Customs to present itself to the public and for its officers to demonstrate the results of the reforms.

Finally, the commissioner personally reached out to the employees’ association, held dialogues with leaders and issued printed materials to address their concerns.



### ***e) Private Sector Support in the Face of a Risk of Reversal***

The 1998 national elections brought in an administration with other priorities, whose officials had no part in the reform process instituted under the previous administration and even had strong suspicions about the programme. The new commissioner had been with the Bureau formerly and was thus a career customs officer, but he had previously been twice removed from the Bureau. This change in leadership was the opportunity that opponents to reform had been waiting for. They shifted the focus for ventilating opposition from external influence groups to an internal group led by the top leadership. The reform process was slowed down and some of the programme components even experienced setbacks.

The commissioner and his staff initiated what they termed as “Critical Review” of the system. The state of computerisation, from June 1998, was dismal due to the lack of support by the new administration. Thereafter the project progressed at a “snail’s pace”.

The green lane clearance process took several steps backward. Previously, the green lane procedure followed the international best paperless practice of full automation, without any intervention by a customs officer, prior to the transmission of the release instruction to the private cargo handler. Customs clearance processes were performed after release of the goods.

The new administration inserted manual processes that made the green lane process pointless, to such an extent<sup>35</sup>, that, for some companies, being selected for green lane treatment had become a serious burden. In some customs posts, for example, the port of Cebu, computerised matching of payments and payables was replaced by a manual procedure. The Direct Trader Input System, remote entry lodgement and clearance process, which had significant take-up, particularly by semiconductor and electronic manufacturing companies, was discontinued at the Ninoy Aquino International Airport Customhouse as customs officials claimed that there were unable to earn overtime payments under this system.

Fortunately, after an initial reluctance to intervene, the business sector mobilised to recover lost ground and to get the reform process back on track. For instance, the Semiconductor and Electronics Industry Federation and other interested private sector groups moved strongly for the resumption of the Direct Trader Input system at the Ninoy Aquino International Airport. The business sector led by the Federation of Customs Brokerage Companies of the Philippines met with customs management to remove the unnecessary, bureaucratic manual appendages, which had become occasions for graft. Its President appealed for the immediate removal of all barriers and obstacles to the clearance of goods introduced by the new administration and warned that *personeros* (broker’s representatives directly dealing with customs officers in the clearance of goods) were threatening to go on strike.

Under the leadership of the private sector and with the support of that section of the internal staff in favour of reform, pro-reform members of Congress, in their turn, called for congressional investigation of the “destruction of the programme”. This was a wake-up call and although Bureau officials took no immediate visible

move, it was enough to arrest the further dismantling of the programme and bring the private sector back into participation in the implementation and further development of the programme.

#### ***f) Weaknesses of the Programme***

##### ***f.1) Failure to Provide Adequate Compensation and Lack of Adequate Preparation for Moving Personnel Affected by the changes***

Congress failed to pass legislation that would have provided adequate compensation and rewarded good performance. There was inadequate insight into, and preparation for, the task of moving those officers affected by the changes to other activities. Despite re-engineering and the implementation of automation there was still much work to be done in customs, yet many officials became idle instead of being reallocated to other jobs.

##### ***f.2) Late Institutionalisation of the Reform Process***

As early as 1996, there had been several expressions of concern about the sustainability of the reforms, urging that the commissioner should take steps to ensure that the programme would not be abandoned once he left the Bureau. Several measures were put in place, including the formation of the Management Information and Technology Group, the hiring of a deputy commissioner to concentrate on the modernisation programme, the leadership training programme and other change management programmes and the strengthening of the various customs-private sector groups to act as guardians of the reform process.

## V. LESSONS TO BE DRAWN

A comparison of the achievements of the Philippines reform with the less successful attempts in Pakistan and Bolivia reveals the factors and forces that made this success possible. Four key factors in the Philippines success can be identified:

- the content of the reform programme;
- the approach developed for the implementation of this reform programme;
- the strong commitment and support of the highest political level; and
- the facilitating environment.

The following paragraphs present the lessons gathered from a comparison of the case studies.

### V.1. The Necessity to Re-engineer the Customs Environment

As seen in Part III.1, previous attempts at reform in Pakistan, Bolivia and the Philippines had confirmed a common view that a comprehensive approach is necessary. Isolated measures of repression, or positive incentives mechanisms alone, cannot reverse a situation of entrenched corruption, but the analysis of the Philippines' success enables us to go one step further. The spearhead of this reform programme was an extensive *re-engineering* of the procedures of the customs administration. While improvements were made on all fronts, the core of the Philippines achievement is a change in the overall organisation of the customs work and the replacement of existing procedures by others, presenting reduced opportunities for corruption. Other measures undertaken may be seen as accompaniments to the reform dynamic.

This throws into relief, among the long list of recommended remedial actions in III.2b), the crucial importance of the block dealing with the organisation of customs operations.

Why is an approach based on re-engineering more likely to bear fruits than measures more strictly limited to changing incentives?

Two reasons may be suggested. The first one can be seen as derived from a cost-benefit analysis. Purges, reinforced general controls through more efficient inspection bodies or mechanisms to secure spontaneous compliance, aim to modify negative and positive incentives *at each station* of the customs chain. It is in fact more efficient to first rethink the customs chain, in order to reduce the need for controls and positive incentives and to facilitate those still necessary. Controls cannot be avoided, but, by reducing the interface between public and private actors, simplifying the procedures and reducing discretion in the definition of tasks, it becomes much easier to ensure compliance with the normal rules of the customs game.

Second, political difficulties can be much more easily handled by this type of reform approach. It is much simpler to oppose or criticise an effort based on law enforcement than a reform aiming at modernising operational systems. In the

Philippines for instance, in the anti-corruption drive which followed the revolution, the judiciary, the legislative and even part of the executive (the Civil Service Commission) joined hands with affected personnel to reverse the resulting purges. If the focus of a reform programme is systems and processes rather than people, it becomes difficult for any sector openly to oppose it. Even the internal staff of an administration, who may see how the reform could cut across their practices, will find it difficult to take up a publicly opposed position.

## **V.2. How to Manage Re-engineering**

The Bolivian programme was based on re-engineering. Yet it failed. As in the Philippines, the primary objective of this programme was to increase public revenues, but unlike their counterparts in the Philippines, Bolivian reform leaders failed to take fully into account that a re-engineering process to increase public revenues implied a fight against corruption. Indeed re-engineering can arouse opposition, as shows examples presented in Box 1. It follows that precautions and an appropriate implementation strategy are essential.

### **Box 1. Different Ways to Resist to Re-engineering**

There are different ways to make re-engineering fail. The case studies provide us with a number of examples. Operational staff can simply refrain from implementing measures. In Bolivia, some reformed procedures were not applied in operational posts where cumbersome procedures were purposely maintained. Similarly a number of decrees were never implemented. Tools supporting new procedures can be put out of order as observed in Senegal, where radios, which should have permitted an efficient communication between frontier posts, never worked (see Duhamel, 2000).

Another way to make re-engineering fail, and thus another means of expressing opposition, is to divert individual measures. Officers can try to implement them partially, in such a way that they do not hinder corrupt practices. The useless acquisition of software, in Bolivia, to recruit new staff on objective criteria is a good illustration of this incomplete implementation, as the selected personnel were never integrated in the customs administration.

The reversals observed after the change of administration in the Philippines are in the same vein, for example, insertion, by the new administration, of manual processes in the green lane, completely against its underlying principle of no interaction between customs officers and traders.

More examples of this form of resistance can be drawn from other countries. For instance, in Benin, a system of random allocation of control officers had been installed, in order to break relations of collusion between traders and officers, but customs staff learned the codes of the different control officers, and ran the software as often as necessary until a "suitable" officer was selected. It is likely that this new "service" also was sold. Again, in Benin, the main software, introduced to handle the declaration of flows and computation of duties, was manipulated, by astute officers, to maintain parallel registers. The arrest, in June 1999 of 20 vehicles exiting Cotonou Port with fake declaration forms, established according to the software norm, is clear evidence of this subterfuge (*Source*: Sinzogan and Soule, 1999).

Finally, when the re-engineering affects only one link, in a chain of operations, corrupt arrangements may just be shifted to another part of the chain, so that while that particular measure can be a success in terms of improving the efficiency of the operation, it makes no contribution to solving the corruption problem. This was demonstrated in Bolivia, where computerisation of part of the transit control system did not reduce smuggling as corruption shifted to the approval of documents presented by carriers to certify the arrival of merchandise in the outgoing customs post.

In Bolivia as in Pakistan, the capture of the administration by power groups was an important aspect of the corruption problem. While it might be reasonable not to explicitly mention the target of fighting corruption when launching a reform programme (as was the case in the Philippines experience), the corruption problem and its consequences need to be taken into account in the reform effort. In Bolivia, as no strategy was developed to manage the oppositions aroused by the re-engineering programme, it was easy for opposing interests to make the reform fail. The difficulty of complying with the IDB's condition to recruit 120 civil servants, within 10 months, could have been a strong alarm signal.

The case studies confirm, with little surprise, that political will is key. Political will for reform was found in the three countries, but the Philippines benefited from a strong personal commitment of the President and the team in the Ministry of Finance. Another crucial point in this country was the tight connivance between the President and the customs commissioner, who himself, was fully dedicated to the reform process.

The case studies also brought out a number of recommendations for the effective use of re-engineering to combat corruption.

- A Transparent Design and Implementation Process

In Pakistan, the lack of transparency in the design of the project (particularly as no diagnostic report was made public) and the lack of participation by supporting interests, clearly contributed to the project's failure. Given its secrecy and exclusion of stakeholders from the planning process, it was easy for detractors to cite the lack of preliminary analysis, or present the project as one imposed by the IMF. The design process necessarily influenced the contents of the project, which was much criticised by customs specialists. It also weakened public support for reform, as the reasons for an extensive restructuring were never disclosed and this led to suspicions that the objective was to reshuffle rent-seeking beneficiaries in relation to tax collection posts. Finally, it weakened the government in negotiating with opposition interests. In total, the way in which the design and presentation of the programme were handled effectively reduced the chances of its success.

In the Philippines, much importance was attached to communication, not only at the design stage but also at all points during the reform itself.

- The Support of the Private Sector

The close involvement and support of business associations proved to be crucial and more important than civil society, represented by NGOs advocating democratic and civic values. The Bolivian and Pakistani programmes failed to associate the private sector, even when this was most clearly desirable, in the design and then, later, the implementation of reforms. In the Philippines, the participation of various private interests, at the design stage, underwrote the reform programme and assured its legitimacy. Such participation was a key, underlying, principle of the strategy. Objectives of increasing revenue, and curbing corruption were linked to those of easing and facilitating trade, to capture private sector support for the entire

reform process. Businesses supported implementation, as their interest had been solicited and taken into account from the beginning. They also played a key role in its sustainability by standing firm against threats of reversal.

With hindsight, in the Philippines, the customs-private sector partnership should have been vested with legal personality by the highest authority, as is done in many other countries, so they could not be ignored by a new administration. Given the right responsibilities, such an organisation could have monitored and resisted any efforts to re-establish opportunities for corruption that had been removed or to create new ones.

- **Make Progressive Steps**

Another reason which might have led the Pakistani government to finally abandon the reform project is the fear, in the end, that a complete restructuring was too risky as it could disrupt the functioning of the customs administration, or that the autonomous PRS would escape from existing control frameworks. The radical change implicit in creating a new institution, with new status and important changes in personnel, was too much for a too weak leadership. Moreover as its scope was broad, the programme attacked too many fronts at the same time, thus arousing different sources of opposition which converged to make the project fail before its enactment.

On the contrary, in the Philippines, reforms were implemented progressively. Favourable expectations for forthcoming reforms were created, dramatically, by renovating offices and buildings. Non-controversial software components were introduced first, leaving more sensitive elements for installation much later, after staff had accepted the first steps.

- **Combine Re-engineering with Changes in the Management**

Purges or measures of staff selection, as envisaged in Pakistan, have proved difficult to handle: targeted individuals can bring forward to defend their interests the discretionary or illegal character of the measures taken against them. Yet the high level management of an organisation is crucial for its functioning: it is not possible to have a high integrity customs if it is run by corrupt managers. The Philippines reform programme used an astute solution to this problem: the redesign of the customs chain weakened some posts of responsibilities and created new ones, to which were assigned reliable agents.

- **Monitor the Effective Implementation of Re-engineering Measures**

If nothing is done to monitor and secure the effective implementation of the re-engineering process, reformers may as well save their money. In Bolivia, the monitoring process came only at the end of the reform effort. Set up earlier, it would have revealed potential sources of resistance. In the Philippines, the customs commissioner set up indicators that permitted him personally to monitor the reform process.

- **Secure Computer Systems**

The introduction of software and computer systems should be a key element in the reform process, as this permits the reduction of the discretionary interface extensively, but if re-engineering can transform control by making it less discretionary, there is no way of doing without controls. Computer systems need to be secured through specific measures (see Box 2), otherwise they can open the way for even wider frauds.

**Box 2. How Can Computer Systems Be Made Secure?**

The following measures could be introduced to secure a computer system:

*Prevention measures:*

- Restrict access to the computer system by introducing passwords for authorised users. Different types should be introduced, which reflect the following compartmentalisation of tasks. The idea is that each actor has access only to the information he needs for his assigned job.
- Separate the tasks:
  - Programmers should not have access to the databases of the daily operations. This is to make sure that they cannot introduce changes difficult to detect in the data.
  - Programmers should be the only ones to be able to make changes in the programmes used.
  - Users, who test the programmes and the changes introduced, should not have access to the library of the results of the tests.
  - Programme librarians (i.e. librarians of the source code) should be the only ones to be able to change the content of the source code.
- Other preventive systems:
  - Block the closing of books if some transactions are detected to be missing; when systems have been forced; etc.

*Detection measures:*

- Identify the techniques of fraud which can be expected and establish audit guides accordingly.
- Detect when data has not been entered in the computer system by comparing with previous recordings or with recordings from similar posts.
- Control the frequency of system interruptions and the turnover in the material. Indeed, interrupting or putting the system out of order voluntarily allows fraudulent operations that would be risky normally.

*Source:* inspired from Pons (2000).

### **V.3. The Broader Conditions which Facilitated the Philippines Success**

Even if trade liberalisation was at work in all three countries, the fact that it had reached a more advanced stage in the Philippines facilitated successful reform there. It had brought a transformation of the corruption problem. Classical smuggling procedures through manipulation of the formal entry declaration were used less frequently. In Bolivia, customs also collect internal taxes on imported goods, including VAT. As these exceed import duties, incentives to bypass the regular customs procedures did not disappear with on going trade liberalisation. In Pakistan, customs reform is very dependent on success in overcoming the influence on government of opposition groups, benefiting from import duty exemptions, as this is a necessary condition for reducing the general level of import duties. The readiness of an important part of the private sector in the Philippines to comply with the rules and to pay taxes was crucial for the success of a reform strategy linking trade facilitation to a fight against corruption, in order to increase public revenue.

As mentioned above, political will for reform existed in all three countries but another distinctive feature of the Philippine case was that the administration was not as captive to political groups as in Bolivia and Pakistan. In these two countries, the case studies revealed the influence of various groups on the governments and the customs administration. The existence of a huge informal sector in Pakistan also contributed to creating difficult conditions for reform. This is important for two reasons. First, it has a certain political weight (it represents up to 41 per cent of the GDP according to certain estimations), which probably has some influence on policy making. Second, by its nature, this sector makes it difficult to develop a broader base for internal taxes that could allow the government to lower import duties.

Finally, economic conditions in the Philippines probably favoured stronger support from the private sector than in the two other countries. Philippine private sector support, from exporters and the formal trade sector, depended on a local exporting community, exposed to competition, an important non-exempted trade sector, afraid of competition from smuggled goods, and a developed social capital in the shape of business associations.

These conditions clearly reflect and necessitate a genuine economic take-off from a condition of under-development. They tend to show that a certain level of development of a formal private sector is essential before business can be expected to press for and support an efficient and corruption-less customs administration.



## VI. CONCLUSION

Comparative analysis of the reform efforts undertaken in Pakistan, Bolivia and the Philippines documents the difficulties met in the reform of customs administrations and enriches the understanding of what can be done to fight corruption. The past attempts in Pakistan and Bolivia failed, while the Philippines made important progress. Although these countries are very different, we drew a number of conclusions on what does not work in a context of widespread corruption and on what could be more effective.

Strategies based on repression and positive incentives are effective in regulating a situation of low corruption and preventing its further development but experience shows that these tools cannot correct a situation of widespread corruption. A re-engineering of procedures that leads to an important reduction of the opportunities of corruption should be at the core of the strategy.

Reformers should be aware that while re-engineering provides an indirect way of tackling opposing interests, measures should also be taken to confront them. This means maintaining a high degree of transparency in design and implementation, obtaining the active support of groups benefiting from reform, proceeding step by step, combining re-engineering with changes in management, monitoring implementation and securing computer systems. Political will remains key for a successful implementation. The case studies showed that it is crucial to have strong commitments on the part of both political leaders and the customs director.

It would appear, from analysis of the conditions which favoured successful reform in the Philippines, that these recommendations for implementation could be either impracticable or inadequate in certain other contexts. The Philippine reform was facilitated by a supporting environment, characterised by a strong political will, with sufficient autonomy to resist influential pressures, a well-engaged trend to liberalisation and strong support from various business associations, demanding action against routine or fraudulent corruption. These conditions, especially a supportive private sector, are not found in every country.

In other terms, this leads to the intuition of a link existing between three data: *i)* the tax and trade policies, which shape the customs mandate; *ii)* the state of development of the private sector and its relation to the State authorities (formal or informal sector, dependent from the state or relatively independent); and *iii)* the way customs operations can be organised. The Philippines were able to move towards a model of customs administration which is less prone to corruption, *because* its economy had evolved on the two other dimensions: there had been important shifts in the trade and fiscal policy, and a maturity of a private sector.

This paper made an opening reference to the importance of combating corruption in customs administration because, among other reasons, of its adverse effects on economic development. The paragraphs, immediately above, tend to show that the conditions which favoured successful reform in the Philippines were very

much linked to a relatively advanced level of economic development. It appears, from the case studies, therefore, that even if many lessons learned from the Philippines experience could be drawn on, with advantage, in other contexts, not all countries can replicate the Philippines strategy right away. The question remains “What can be done in a less advanced context to break out of existing vicious circles linking corruption and under-development?”

The case studies suggest that reforms should be adapted to their political and economic context. The idea that a reform programme should be adapted to the technical level of a country is generally well accepted: progress should be made step by step, with, for instance, a need to strengthen basic telecommunication and electricity infrastructures before installing large computer systems. Such is not the case regarding the political and economic context. Too often still, policy makers seem to follow the *linear implementation model*. In the terms of Grindle and Thomas (1991, p. 122): “a proposed reform gets on the agenda for government action, a decision is made on the proposal, and the new policy or institutional arrangement is implemented, either successfully or unsuccessfully”. The authors, continue, criticising this approach: “If implementation is unsuccessful, the usual remedy is to call for greater efforts to strengthen institutional capacity or to blame failure on lack of political will, an explanation often propounded by external analysts and donors who see countries not carrying out reforms they consider desirable. In the absence of detailed knowledge about what goes on within another government and a capacity to analyse the decision process, lack of political will becomes a catch-all culprit, even though the term has little analytical content and its very vagueness expresses the lack of knowledge of specific detail”.

In the specific context of customs reform, one way to adapt the guiding strategy to the local political and economic environment would be to operate, in the short term, within existing limits, while working towards longer-term action by moving back these constraints. For this purpose, it will be useful to distinguish between different corrupt practices. Attacking corruption “head on” may turn to be ineffective. It might be useful to differentiate the different corruption practices in the strategy design and attack them separately (this implies not to explicit the fight against corruption as the objective of the reform, as this rhetoric does not permit to distinguish corruption problems). The case studies show that such different corruption practices depend on and affect different groups, with different logics of action. For a particular practice, the balance of forces between those opposing reform and those supporting it might be favourable for reform. That practice could be targeted in priority.

Differentiating between practices could also enable the policy maker to assess the social costs of each and to design appropriate responses. It might be that, for some corruption practices, the policy maker will base action, to use Reisman’s terms, on changing the mythical system rather than trying to repress the practical code.

Some corruption practices may seem minor whereas others will be perceived as highly harmful to society. In other words, reforms should be designed to fit as closely as possible to the political and economic profile of the corruption problem, and based on a judgement of where oppositions can best be confronted, when they

cannot be met by earlier changes in the balance of power. This approach would have

the merit of adjusting the reform programme to local possibilities and would, at least, save public funds from large, costly and unadapted reform programmes.

In the long term, reform measures should purposely develop these power balances. Strengthening democratisation is one important supporting trend. Facilitating access for direct foreign investors, now under pressure from the OECD Convention, to observe sound integrity standards, could also reinforce the weight of private sector claims for efficient, corruption-free customs administrations. Grindle and Thomas stress that policy elites, in most developing countries, play a role within governments, even more important than in western industrialised nations. This suggests, in practical terms, that reformers need to be centrally concerned with the attitudes, perceptions, and actions of these elites, as they will be fundamental to any efforts to initiate and sustain reform. Another long-term measure would hence be to provide high quality training to higher customs officers to develop management capacities and to sensitise them to the importance of the customs service for the functioning of the entire economy.

## NOTES

1. See website [www.wcoomd.org](http://www.wcoomd.org). In practice, it works as a forum where representatives of its 151 Members countries can tackle customs-related issues. It establishes and promotes international instruments for the harmonisation and the modernisation of customs systems.
2. See Lambsdorff (1999) for a survey of econometric studies on the causes and consequences of corruption.
3. This is in sharp contrast with developed economies for which trade taxes represent a negligible fraction of total tax revenues, and have been declining steadily over the past two decades. See reports of the WCO Harmonised System Committee.
4. Drafted by John Crotty, Chief of the Tax Administration Division at the IMF. The paper draws upon the experiences of the Tax Administration Division of the Fiscal Affairs Department.
5. This working group includes the following countries: Albania, Bulgaria, Czech republic, Hungary, F.Y.R. Macedonia, Romania, Slovak Republic and Slovenia. The document mentioned was drafted in July 2000.
6. This present work is part of a broader research project, conducted jointly with UNDP. These countries have been chosen because they had expressed a demand for co-operation to our partner UNDP on corruption problems.
7. Survey conducted in May 1998 by the Bolivian government and survey conducted in 1997 by CIET-International on 1599 private firms. See Arduz (2000).
8. Survey conducted by the Social Weather Station on the perceived extent of corruption in a number of government agencies. See Parayno (1999).
9. Other surveys tend to show that this is a feature common to transition countries. In Georgia for instance, customs administration is the administration receiving the largest share of side payments, after the tax and financial inspections service. See World Bank PREM (1998).
10. This research has been conducted in collaboration with local experts, familiar with their national customs: Mario Arduz for Bolivia, Malik Younas for Pakistan and Guillermo Parayno for the Philippines. The description of corruption characteristics is based on their testimonies. It reflects the situation in these countries until the late 1990s. Other reform efforts, not reported in the present work, have been conducted since that time.
11. This description is inspired from *École Nationale des Douanes de Neuilly*, 1995.
12. The cargo manifest is the transport document of the merchandise that has been loaded in a port or in an airport at destination of another port or airport.
13. Let us note also that passing through the customs administration implies physical movements of goods, which can also be sources of fraud and corruption. Merchandises in transit move from a frontier post to another frontier post. When, for instance, the operator is not sure of the regime under which he wishes to register his merchandise for instance, the merchandise will move from a frontier post to a warehouse for temporary stocking. If some frontier posts are overloaded with work, or if some posts are specialised in the treatment of certain types of goods, goods will have to move from a frontier post to an inland post.

14. In fact, brokers, broker's representatives and the personnel of traffic departments of businesses took advantage of this perception by asking for exaggerated facilitation budgets (more popularly called "overtime"), the main part of which they would keep to themselves.
15. Some authors have observed that customs officers actors will modify the customs setting on purpose, in order to permit the further development of corruption practices. For instance, Cunningham (1996), quoted by Finger and Schuler p. 515, "in an assessment of several least developed countries considering customs reforms, observed that systems and procedures appeared to have evolved to maximise the number of steps and approvals — to create as many opportunities as possible for negotiation between traders and customs officials".
16. This exercise was undertaken in 1993 when Nawaz Sharif, then Prime Minister, visited the Central Board of Revenue (CBR). Many officers held to be corrupt were made OSDs. But no charges were framed, no sanctions were implemented. With the dismissal of the Sharif government in July 1993, officers on OSD manoeuvred their rehabilitation to regular assignments. Similarly, the chairman of CBR appointed in January 1998 made frequent postings and transfers of officers. But again no charges were framed and no proceedings initiated; the affected officers were subsequently posted to regular assignments.
17. The ley SAFCO (*Ley de Administración y Control Gubernamental*) set the framework for the modernisation of public administrations.
18. See Tilman, 1968.
19. See Lahiri, Nasim and Ghani, 1998.
20. *Source*: Direccion General de Aduanas.
21. Out of 109 officers of that category at that time.
22. Since 1999, these firms no longer undertake control of exports.
23. Without mentioning cases where control mechanisms such as purges or investigation units were planned or used to pursue political objectives. For instance, in December 1971, Zulfikar Ali Bhutto assumed power as Chief Martial Law Administrator and President. In 1972, under the Removal from Service Regulation, 1303 public servants, including 9 senior customs officers, were dismissed. This purge was undertaken under the influence of the employees affiliated with the party in power. The message that was received by the bureaucracy as a result of the purge was clear and straightforward: support the policies of the party or look for another job. This message was reinforced the day before the formal announcement of the administrative reforms, when 18 additional senior officers were compulsorily retired with no benefit of extraordinary martial law provisions. According to Younas, Bhutto had a vested interest in gaining some measure of control over the selection process to the bureaucracy. This motive provides a cogent explanation for the introduction of wide-scale lateral recruitment and horizontal movement under the terms of the reform.
24. See Project description, October 1999, World Bank website [www.worldbank.org/pics/pid](http://www.worldbank.org/pics/pid).
25. One should be cautious about how to interpret shortfalls between targets and tax actually collected. Shahid Sheikh (former Pakistani customs officer, now WCO officer), indicates that Pakistani customs authorities did not participate in the assignment of targets, established by the Ministry of Finance. Moreover, a target met at 100 per cent or beyond does not mean that there is no corruption. Is reported here the interpretation that was given at that time, in this particular context.

26. We refer here to the draft that was introduced in the National Assembly on December 1998 (which was then sent back to the National Assembly Committee on Finance).
27. PPP government in August 1990, PML government in July 1993 and PPP government in November 1996.
28. The E&D Rules of 1973 propose a framework to penalise improper conduct, dereliction of duty and corruption. The provisions of the Government Servants Conduct Rules of 1964 propose a code of conduct for civil servants more detailed than the PRA Bill in some respects, including the obligation to declare assets regularly and when leaving service: “i) gifts which create official obligation to the donor not to be accepted; ii) lending and borrowing with those having official dealings not to be done; iii) buying and selling of moveable and immoveable property to be done after government approval; iv) construction of building to be done after government approval; v) assets to be declared at entry, thereafter at end of year and also whenever required by government; vi) no indulging in speculative investment; vii) no living beyond means and no indulging in ostentation on occasions of marriage and other ceremonies; viii) habitual insolvency and indebtedness to be avoided; ix) no unauthorised communication of official documents or information; x) no approach to members of National Assembly or Provincial Assembly or any other non-official person to intervene in any matter; xi) no propagation of sectarian creeds; xii) no nepotism, favouritism and victimisation; xiii) no publication of information and public speech capable of embarrassing government; and xiv) no use of political or outside influence, directly or indirectly, in support of any claim arising in connection with employment”.
29. Agreement ATN/Sf-3421-BO.
30. Agreement 895 – SF-BO.
31. La Paz, Cochamba, Santa Cruz
32. The development of adequate legal bases to build on reforms is often overlooked. In the Bolivian case, these legal bases were established through a series of decrees and ministerial and administrative resolutions (Supreme Decree No. 23098 which established the legal bases of the reform programme for instance).
33. The land acquisition process for the post was problematic.
34. Among the actions the two biggest employees association undertook were the following, they:
  - filed a class suit against the commissioner of customs with the civil court. They asked for the issuance of a temporary restraining order against the implementation of the Selectivity System on the ground that it prevented them from performing the functions given to them under the Tariff and Customs Code;
  - caused both houses of Congress to conduct separate investigations supposedly in aid of legislation on the reform programme components that are viewed to be anti-personnel and could weaken the anti-smuggling defences of the Bureau;
  - conducted noontime protest rallies and marches to protest at what they perceived as privatisation of customs and the subservience to the dictates of World Bank and IMF;
  - convinced the government union “Courage” to undertake teach-ins in the Bureau on the evils of privatisation and “reforms” that actually clip the prerogatives of government officials or threatens their continued stay and importance in government;
  - put up their own newspaper *Budjong* as a vehicle to communicate their opposition to the reform;
  - conducted information campaign in provincial customs stations on the threats to them of the reform;
  - undertook media campaigns in regular newspapers against the reform.

35. The blue copy of the Single Administrative Document, which the customs broker needs to effect delivery of the goods from the cargo handler, was detained by customs and only issued to the broker *after* the completion of the processes at the collection division, including the completion of manifest clearance (manual posting of the entry declaration reference number and date to the manifest and the manual comparison of the entry details to the manifest details). Green lane entries were all required to go through the Import Specialist Team Office, after the completion of the computerised process, before the release instructions could be transmitted to the cargo handler allegedly for review.



## **ANNEX 1. EXAMPLES OF CORRUPTION CASES OBSERVED IN BOLIVIA, PAKISTAN AND THE PHILIPPINES**

In order to concretise the problem of corruption in customs, let us give a few examples of *techniques* observed in the three countries studied.

### **Routine Corruption**

Information from the Philippines enables us to detail a number of practices that fall under the category of routine corruption. For instance, the initiation or completion of actions by officials will be delayed until a favour is given or promised. Officers use different “techniques” to create these delays: the files of those who have given bribes are attended first; officers turn out being absent or elsewhere when the requested action is much needed; the hearing of seizure cases is prolonged; etc. Another situation of routine corruption is when officers create or threaten to create excessive difficulties in the customs clearance process. Those will conduct examinations in excessive detail, ask for documents difficult to produce, threaten to stop the operations or to send the merchandise for further controls, etc. Situations in which officers threaten to submit exaggerated assessments or audit findings coupled with recommendation for punitive measures to extort certain sums have also been observed.

### **Fraudulent Corruption**

Information from Pakistan enables us to expose a number of typical smuggling techniques (see Box 3 for illustrations). The most frequent technique is misdeclaration: importers provide erroneous information on their customs declaration regarding the nature of the merchandise, its quantity, its origin or its value. Operators also try to obtain abusively concessionary or exemptions notifications. As these are much lighter than for commercial operators, smugglers abuse customs procedures for passengers to pass in important quantities of merchandise. Goods are taken out of warehouses without the due accomplishment of customs procedures. Goods meant for transit are dropped in the country, etc.

### Box 3. Examples of Fraudulent and Criminal Corruption Practices Observed in Pakistan

- Misdeclaration:

Second-hand machinery has been concealed in iron and steel scrap consignments and declared as scrap; auto-parts have been concealed in iron and steel scrap consignments; tyres in rubber scrap consignments and declared as rubber scarp.

- Misuse of exemptions and concessionary notifications:

Operators have obtained abusively concessionary notifications for substantial gain. One such case involved the import of equipment and materials that were cleared on concessionary rates of duty, on the basis of a provisional certificate. The authorisation to import the goods with concession was issued by the Central Board of Revenue despite the fact that the contract of the importer required the full payment of customs duty. This case represented a loss of customs duty of Rs 67 million (\$2.6 million<sup>1</sup>).

- Misuse of baggage facility:

Customs procedures for passengers are much lighter than for commercial operators. A large number of carriers called *khepias* import clandestinely huge quantities of commercial merchandise under the garb of passenger baggage. The smuggled goods are then sold in posh markets in towns. These *khepias* function in collusion with customs and other officials posted at airports. They enjoy clout and in case of need, powerful persons come to their support and ensure that their activities and flow of smuggled goods is not interrupted.

- Undue removal of goods from warehouses, fraudulent release of shipments:

Bonded warehouses permit the storage of imported goods within the customs perimeter with no payment of customs duties and taxes. But diplomatic bonded warehouses have become conduits for the supply of smuggled goods to posh markets in Islamabad, Lahore and Karachi. Huge stocks of foreign goods, which have no common measure to the registered annual sales, are accumulated. Cases involving clandestine removal of huge quantities of goods, notably against forged documents, have been detected. In one case, a diplomatic bonded warehouse cleared 24 342 bottles of liquor, 97 104 cans of beer, 92 units of electronic items and 271 packages of foodstuff against 215 fake exemption certificates. In another case, electronic goods involving customs duty and taxes of Rs 610 000 (\$23 000<sup>2</sup>) were cleared against bogus exemption certificates.

- Smuggling over the Pakistan-Afghan border:

Pakistan has an agreement with Afghanistan (The Afghan Transit Trade Agreement, 1965) under which goods meant for Afghanistan are imported at Karachi port and thereafter sent by sealed railway wagons to border towns, Chaman and Peshawar. From there, goods are sent to the Pakistan-Afghan border by trucks. In practice, the Afghan transit trade is one of the main sources of smuggling of goods in Pakistan. Goods meant for transit to Afghanistan are dropped in Pakistan. Goods that have passed the Afghan border are also brought back clandestinely in Pakistan and sold in numerous foreign goods markets. Allegations of import of Afghan transit trade goods, against forged Letters of Credit, have also been made.

### Box 3 (contd.)

- Export rebate fraud:

An important case of export rebate fraud was detected in Karachi. The exported consignments were declared to contain embroidered saris and men's shirts when it consisted in fact wholly of second-hand clothing. This misdeclaration led to an undue payment of Rs 49 million (\$2.4 million<sup>3</sup>) as export rebate.

Detected in 1989, the investigation of this case revealed the existence of an elaborate international network that operated in different countries. Customs officials up to the level of the collector in charge of the customs post of Karachi were held as involved. This indicates that the mechanism in place of posting and transfer did not prevent collusion between customs officers engaged in illegal activities, as well as the inefficiency of the supervisory control.

The State Bank of Pakistan never recovered the amounts paid as export rebate nor the fines due. In the end, criminal cases were registered but no conviction was secured. This case manifests the ineffectiveness against powerful groups who perpetrate such frauds.

- Export rebate fraud:

Another similar case at Quetta collectorate was detected in 1991, which involved the fraudulent export of fabrics and pieces of glass marbles from Gwadur to Dubai. Investigations revealed that the documents showing export had been manipulated. The launches said to have transported the goods to Dubai did not have the capacity to transport such heavy consignments; nor were the means available at Gwadur port to load them. Moreover, the goods mentioned never reached destination. This scheme was drawn up in collusion with top customs officials who abetted and facilitated the fraudulent export and rebate payments. The rebate paid amounted Rs 131 million (\$5.6 million<sup>4</sup>). It has not been recovered.

## Criminal Corruption

Corruption also accompanies other illegal activities, such as money laundering. A classic scheme, for instance, when making declarations is to overestimate the value of imported goods that are not subject to any import duty. This enables the unlawful transfer abroad of foreign exchange. Huge funds generated illegally have been moved outside from Pakistan using this technique<sup>5</sup>.

Misdeclaration is also used to abuse export promotion schemes. Rebate payments against fraudulent exports are made with collusion of customs officials. In Pakistan, such frauds generate big money and the operators have organised themselves into powerful mafias (see Box 1).

## **NOTES TO ANNEX 1**

1. Based on an average of the official exchange rates between 1990 and 1995 (local currency units relative to US dollars).
2. Idem note 1.
3. Based on the official exchange rate in 1989.
4. Based on the official exchange rate in 1991.
5. A parallel illegal banking system for transfer of amounts, from and to Pakistan, called Black Hawala has been operating in Pakistan. See Younas, 2000.

## ANNEX 2. COMPARING THREE POLICY PAPERS

The following table compares the policy recommendations proposed by three documents in order to curb corruption in customs administrations. When a cell appears empty, it means that this policy paper did not consider the policy recommendation.

Policy Recommendations	WCO — Arusha Declaration (1993)	IMF Integrity Paper (1997)	Working Group Budapest July 2000
<b>General Organisation</b>			
Position among State institutions		Financial and administrative independence, independence from general civil service requirements, with appropriate checks and balances	
Scope of responsibilities		Separate the setting of policy from its administration	
<b>Organisation of Work</b>			
Define targets for the administration and performance standards		Clear statement of objectives: revenue targets, service standards	
Strategic segregation of functions	Yes	Yes	
Clear job description and definition of roles and responsibilities to enhance internal control			Yes
<b>Customs Procedures</b>			
In general	Simple, consistent, with minimum discretion	Simple, transparent	Clear, precise and easier to control customs regulations
General organisational principles	See revised Kyoto Convention	Self-declaration system, one step process	
Access to customs procedures	Easy	Easy	
General principle		Standardisation of procedures	
Information to be given by importers and exporters		Minimise the information and documentation requirements	
Computerisation	Should be a priority	Yes: control of rates, allocation of exemptions, proper documentation, payment deadlines, follow-up action; management of time, officers' activities.	Use of information technology to computerise procedures, for control purposes, to apply risk analysis, for payment of duties and taxes, for internal and external communication

<b>Staff Rules</b>			
Legal definition of active and passive corruption crime, definition of sanctions (fines, jail penalty)			
Code of conduct (or ethics)	Implications of which should be explained to customs officers	Integrity, confidentiality of information, conflict of interest, disclosure of assets, appearance and conduct	Yes
Definition of disciplinary measures and penalties for cases of misconduct and corruption	Including possibility of dismissal	Including possibility of dismissal	Yes
Penalty system for minor offences		Yes	
<b>Internal Culture</b>			
Organisational culture	Promote sense of loyalty and pride in the service, "esprit de corps" and a desire to reduce their exposure to the possibility of corruption	Build "esprit de corps", emphasise responsibility and loyalty	
Public image			Promote the importance of customs service so as to increase public image
<b>Information Production and Investigation</b>			
General principle	Random allocation of examinations		
Day-to-day controls	Line managers: prime responsibility to identify weaknesses in working methods and integrity of their staff and take steps to rectify such weaknesses	Supervision of day-to-day activities, regular review of the outputs of employees	Yes
Internal audit: compliance with procedures, expenditure of funds, procedures appropriate	Yes	Yes	
Specialised internal affairs unit: investigation of cases of suspected malpractice	Yes		Yes
External audit	Yes		By independent organisations or other governmental bodies
Feedback from external actors and clients (importers and exporters) on customs work and monitoring of complaints	Letter boxes, Hot lines	Special unit for the receipt of complaints on the performance of officials	
Disclosure of employees' assets		Can be included in code of conduct	

<b>Human Resource Management</b>			
Recruitment process	Objective and immune from interference	Clear definitions of requirements for recruitment	Based on knowledge
Recruitment process	Identify applicants with high standard of personal ethics		Clean criminal records; filter through psychological tests
Advancement process	Objective and immune from interference	Merit-based promotions, jeopardised by inappropriate behaviour, with regular review of outputs of employees	Clear and transparent promotion system, with clear criteria and regular evaluations
Advancement process			Publish internally results of promotion exercises
Redeployment system			Transparent and with clear criteria
Rotation of staff assignments	Yes	Yes	
Regular relocation of staff	Yes		
Continuous training	Yes, including on ethics issues	On appropriate technical skills and to build "esprit de corps" and promote integrity	Yes, including on ethics issues, at all levels of the administration
<b>Remuneration</b>			
General	Sufficient to afford a decent standard of living	Sufficient to provide a good standard of living	Decent basic salary
Incentive payments	Yes	Yes	Reward and bonus schemes, with clear criteria for their allocation
Incentive payments			Clear criteria for receipt of bonuses
Other benefits	In certain circumstances health care and housing facilities		Job satisfaction, long term stability, pension prospects
<b>Working Conditions</b>			
General		Appropriate: proper office space, equipment and supplies	Good working conditions
Security			Yes
Relations within the services			Good
<b>Relations with Other Actors</b>			
With customs brokers	Open and transparent, through liaison committees		Good relations with the other agencies
With the business community	Open and transparent, through liaison committees	Have the possibility for importers and exporters to discuss decisions made	
Procedure for appealing against customs decisions	Yes, with possibility of recourse to independent adjudication in the final instance	Within customs and outside (Courts)	
<b>Trade Policy</b>			
Level of import tariffs	As low as possible	Perceived as fair, low	
Number of rates	Limited	Minimum	
Administrative regulation of trade (non-tariff barriers)	Reduced to the minimum	Minimum	
Exemptions to standard rules	As few as possible	Minimum and clearly specified	

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