



Independent
Commission
for Aid Impact

DFID's Approach to Anti-Corruption

Terms of Reference

1. Introduction

1.1 The Independent Commission for Aid Impact (ICAI) is the independent body responsible for scrutinising UK aid. We focus on maximising the effectiveness of the UK aid budget for intended beneficiaries and on delivering value for money for UK taxpayers. We carry out independent reviews of aid programmes and of issues affecting the delivery of UK aid. We publish transparent, impartial and objective reports to provide evidence and clear recommendations to support UK Government decision-making and to strengthen the accountability of the aid programme. Our reports are written to be accessible to a general readership and we use a simple 'traffic light' system to report our judgement on each programme or topic we review.

1.2 We have decided to conduct a review of DFID's approach to protecting UK funds against the risk of corruption. We will assess whether UK funds spent in systematically corrupt contexts serve to consolidate trends with regard to corruption that are detrimental to the values which underlie the UK's work to improve governance generally and fight corruption specifically. These Terms of Reference outline the purpose and nature of the review and identify the main issues that it will investigate. A detailed methodology for the evaluation will be developed during an inception phase.

2. Background

2.1 The issue of corruption is often raised by the UK Parliament and the public regarding the UK aid programme. It was raised consistently as a concern by respondents to our public consultation. The UK public has a right to know that taxpayers' funds are being spent effectively for the purposes for which they are given and not wasted through embezzlement or misdirection. DFID must be accountable for the integrity of the aid programme. DFID is now also operating in a new environment of laws designed to tackle corruption and money-laundering.

2.2 Corruption is a central issue in assessing the effectiveness and value for money of UK development aid. Corruption can undermine the impact of aid programmes and cause their benefits to be unequally distributed. Aid programmes affected by corruption represent poor value for money. They can even be harmful if they help sustain corrupt political elites.

2.3 Many of the world's poorest people live in countries where corruption is endemic. Furthermore, the UK is committed to scaling up its assistance to fragile and conflict-affected countries where country systems for financial accountability are likely to be particularly weak. The UK therefore cannot avoid engaging with countries where the corruption risk is high. Hence it is imperative that DFID finds ways to deliver aid in high-risk environments so that the funding still achieves its intended goals and that its assistance includes long-term integrated strategies for reducing corruption.

2.4 We recognise that there may be trade-offs between protecting aid funds against the risk of corruption and maximising development impact. Some donors prefer to provide their assistance in the form of projects, implemented by international contractors with the funds ring-fenced from access by local authorities. Some thinking on aid effectiveness argues that this represents a missed opportunity to strengthen the national authorities, who should be the 'owners' of the development process. Commentators have also noted that a balance needs to be struck between minimising fiduciary risk and maximising aid effectiveness, including by investing in building the capacity of local actors fighting against corruption. DFID's business model has changed dramatically over the past decade, away from traditional projects administered by UK civil servants and contractors, towards directing aid through international partners, recipient governments and non-state actors. This is perceived to change the nature of the corruption risk facing the UK aid programme.

2.5 DFID has a number of corruption-related policies and guidelines but no holistic or over-arching anti-corruption strategy.¹ Its *Counter-Fraud and Anti-Corruption Policy*, produced by the Internal Audit Department and Counter-Fraud Unit, outlines the responsibilities of DFID employees, consultants and contractors when encountering corruption within aid projects.² The *Essential Guide to Rule and Tools* – known informally as the *Blue Book*³ – sets out detailed rules on financial management, accountability and audit. For each country where financial aid is being provided or considered, DFID carries out a Fiduciary Risk Assessment evaluating the quality of the country's public financial management systems. There is also guidance material for staff on more specific corruption issues, such as how to deal with corruption in the health sector.⁴

3. Purpose of this evaluation

3.1 To assess whether DFID's strategies and approaches for dealing with corruption (particularly in fragile states) are appropriate and sufficient, having regard to the requirements of maximising development impact and ensuring accountability to the UK taxpayer; and to make constructive recommendations on how improvements could be made.

4. Relationships to other evaluations/studies

4.1 In 2011 the National Audit Office (NAO) issued a report on DFID's financial management.⁵ This is a high-level report looking right across DFID's financial management systems. The report notes that DFID's programme budget will grow by

¹ The Governance Department produced a paper in 2002 on the possibility of developing a holistic anti-corruption strategy, but this appears not to have been pursued.

² *Counter-Fraud and Anti-Corruption Policy*, DFID, www.dfid.gov.uk/aboutDFID/anti-fraud-corruption-policy.pdf.

³ *The Essential Guide to Rules and Tools*, DFID, 2011, www.dfid.gov.uk/about-us/our-organisation/blue-book/.

⁴ *How to note: Addressing corruption in the health sector*, DFID, November 2010, www.dfid.gov.uk/Documents/publications1/How-to-Note-corruption-health.pdf.

⁵ *Department for International Development: Financial Management Report*, National Audit Office, April 2011, www.nao.org.uk/idoc.ashx?docId=8184a4cd-c1d9-4c5e-9e88-4d7e4cbe32e7&version=-1.

£3.3 billion between 2010-11 and 2014-15, an increase of more than a third. Much of this increase will be in fragile states. At the same time, its administration budget will reduce by a third. This will give rise to significant financial and operational challenges, making sound financial management essential. The report notes, however, that DFID has a comparative lack of qualified finance staff.

4.2 The NAO notes that the value of fraud and corruption reported in DFID's accounts is low (£459,000 for 2009-10 or 0.01% of expenditure of which £199,000 has so far been recovered). Where aid is channelled through country systems, however, corruption is likely to be hidden and DFID's purely reactive approach to control of corruption may fail to detect it. Like other donors, DFID has no systematic or comprehensive approach to quantifying the extent of corruption within the UK aid programme. The NAO report states that:

'The Department is too reactive and cannot provide Parliament and the taxpayer with a clear picture of the extent, nature and impact of leakage. The risk of leakage will potentially increase as the spending increases for those countries with less developed controls and capability.'

4.3 The Committee of Public Accounts has also commented on DFID's management of corruption risk. In a recent report on UK support for primary education, it noted that DFID had assessed the risks in the Kenya programme as 'manageable' but that serious fraud had nonetheless arisen⁶ and recommended a general reassessment of how DFID assesses and manages fraud risk.

4.4 The International Development Committee in a 2010-11 report on DFID's corporate performance stated that:

'We are concerned that DFID may not yet be taking the threat of fraud as seriously as it should. Indeed, there seems to be an over-reliance on staff reporting cases of fraud rather than DFID taking action to mitigate such risks before they arise. We recommend that, in response to this Report, DFID provide us with more information on the steps it is taking to ensure that it has a robust, consistent and strategic approach to fraud in all its country programmes and in all sectors in which it works.'⁷

4.5 In the light of these concerns, ICAI wishes to examine how effectively DFID has responded.

⁶ *The Department for International Development's bilateral support to primary education*, House of Commons Committee of Public Accounts, Thirteenth Report of Session 2010-11, HC 594, December 2010, www.publications.parliament.uk/pa/cm201011/cmselect/cmpublicacc/594/594.pdf. See also *Department for International Development: Providing budget support for developing countries*, House of Commons Committee of Public Accounts, Twenty-seventh Report of Session 2007-08, HC 395, June 2008, www.publications.parliament.uk/pa/cm200708/cmselect/cmpublicacc/395/395.pdf.

⁷ *DFID's Performance in 2008-09 and the 2009 White Paper*, International Development Committee, HC 48-I, March 2010, www.publications.parliament.uk/pa/cm200910/cmselect/cmintdev/48/48i.pdf.

5. Analytical approach

5.1 This is an evaluation of how DFID provides aid in environments with high corruption risk. It will assess whether DFID's corruption strategies are effective in addressing the risk of corruption while maximising development impact. It will also assess whether DFID is complying with its policies.

5.2 This review will address three elements of DFID's approach to working in environments with high corruption risk:

- i) Does DFID have a credible approach to combating systemic corruption through its planning and programming choices?
- ii) Does DFID make appropriate choices as to aid modalities and safeguards within its programmes, so as to minimise corruption risk and maximise development impact?
- iii) Does DFID respond effectively when it encounters incidents of corruption? How does this response affect the overall country programme?

6. Indicative questions

6.1 The review methodology will be developed during the inception phase, setting out detailed questions and the methods to be used for answering them. Possible review questions include:

- Does DFID have a coherent overall policy framework for responding to corruption risk? Are its policies consistent with UK Government rules and guidance? Are they well understood by DFID staff?
- How effective are DFID country and sectoral programmes at addressing the systemic causes of corruption? Is DFID investing enough in anti-corruption measures (e.g. in budget processes, public financial management, procurement, national accountability institutions, external scrutiny of government processes and non-state actor demand-side accountability mechanisms)?
- How effective is DFID's analysis of the level of corruption risk and how effectively is this analysis built into decision-making?
- Has DFID been effective in minimising corruption in its programmes? Does it effectively monitor the types and extent of corruption that occur within its programmes? Does it provide opportunities for intended beneficiaries and other national stakeholders to participate in monitoring and reporting incidents of corruption? How much leakage has in fact been detected? Does DFID make appropriate choices as to aid modality in high-risk environments? Does it build appropriate safeguards into the design of its programmes?
- Is the risk that UK aid to corrupt regimes may do harm identified and mitigated in DFID programming?
- Do DFID staff in high-risk environments face pressures to spend, irrespective of concerns about corruption?
- Does DFID respond effectively to corruption incidents? Does it make efforts to recover the funds? Does it pursue sanctions against perpetrators? Does it diagnose what went wrong and adjust its programmes accordingly?

- Is DFID transparent enough in its policies and funding decisions to enable external scrutiny of its spending decisions/risk profile?

7. Outline methodology

7.1 The methodology for the review will have three main components:

- i) Analysis of DFID's policy on corruption and fraud:
 - assembly of the different policies, strategies and guidance;
 - interviews with DFID senior management;
 - interviews with FCO senior in-country officials present and past (where possible);
 - consultations with other UK stakeholders, including anti-corruption NGOs, on DFID's approach to engaging with corrupt regimes;
 - analysis of the policy framework, by reference to HM Treasury guidance on use of public funds and the practice of other donors, such as the World Bank (in particular the INT department) and the United States Millennium Challenge Account; and
 - an assessment of whether DFID provides sufficient training to staff on counter-fraud and anti-corruption.

- ii) Case studies of DFID programmes in high-risk environments:
 - select four cases of DFID programmes in countries in the bottom third of Transparency International's Corruption Perceptions Index where DFID Fiduciary Risk Assessments have identified the corruption risk as high;
 - assess whether choices of funding modalities and programme safeguards are appropriate, given the level and types of risk identified in the Fiduciary Risk Assessment;
 - identify whether the design of the programmes includes proactive anti-corruption measures (e.g. investments in improving country systems, measures to increase transparency of development expenditure, intended beneficiary and civil society monitoring) and consultation with civil society and/or intended beneficiary groups on whether they view DFID's anti-corruption approach as appropriate; and
 - identify whether DFID has responded appropriately to incidents or allegations of corruption in relation to the programme, either from evaluations or raised by external stakeholders and whether a top-down as well as a bottom-up approach has been taken to identify corruption.

- iii) Case studies of DFID's response to incidents of fraud:
 - find out from DFID how many cases have been cancelled, delayed or scaled back due to corruption-related concerns. Analyse according to country, sector, aid modality and other relevant categories to identify what patterns emerge. This could include looking at World Bank Integrity Department investigations relating to UK aid funds;
 - select a sample of two cases where DFID has scaled back or halted programmes due to concerns about corruption;

- assess whether they were properly investigated, reconstruct the decision-making processes and assess whether the follow-up actions were adequate; and
- assess whether there is a mechanism for lessons learnt from corruption incidents to be fed back into policies and guidance for staff.

8. Timing and Deliverables

8.1 The review will be overseen by Commissioners and implemented by a small team from ICAI's consortium. The review will take place during the third to fourth quarter of 2011, with a final report available by the end of November 2011.