



## Developing an NGO corruption risk management system: Considerations for donors

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U4 Issue

September 2011 No 9





# Contents

- Abstract ..... iv**
- 1. Introduction: Framing NGO corruption risk management ..... 1**
  - 1.1 Methodological considerations ..... 1
  - 1.2 Corruption and development ..... 2
  - 1.3 NGO corruption risks ..... 3
  - 1.4 Managing corruption risks ..... 6
- 2. Recommended corruption risk management measures ..... 8**
  - 2.1 Elements of an institutional corruption risk management system ..... 8
  - 2.2 NGO partner standards ..... 19
- 3. Implications and dilemmas in moving forward ..... 24**
  - 3.1 NGO independence ..... 24
  - 3.2 Transferring vs. sharing of responsibility ..... 24
  - 3.3 Accepting corruption risks ..... 25
  - 3.4 Primacy of development objectives ..... 25
  - 3.5 Costs of corruption risk management ..... 25

## Abstract

Non-governmental organisations (NGOs) are often on the front line of aid delivery, managing a significant proportion of aid funds. The risk of corruption in NGO operations is therefore a significant concern. Yet so far, many international donors and the NGOs themselves have not taken a comprehensive approach to managing these corruption risks. Based on an analysis of the systems of four donor agencies and four international NGOs, this report distills good practices for NGO corruption risk management systems.

Important risk assessment considerations include the capacity of the NGO, the type of operation, the operational context, and whether implementation is done by the NGO itself or by a partner NGO. To manage corruption risks, it is therefore recommended to conduct a risk analysis for the specific location, sector and type of programme; strengthen NGOs' internal systems for corruption risk management; have better monitoring and whistle-blowing mechanisms for both NGOs and donors; nuance donors' zero-tolerance policy approach; and establish due diligence measures through NGO selection criteria.

The report also argues that the common classification of corruption risk management tools as "administrative costs" is misguided. Corruption risk management should be promoted as an essential investment in institutional capacity development and therefore a necessary programme cost serving the overall goal of securing positive development outcomes.

# 1. Introduction: Framing NGO corruption risk management

Over the past decade, donors have increasingly recognised the imperative to address corruption in the delivery of development assistance. They do so mainly through interventions at three levels.

One, they encourage programming that aims to strengthen national mechanisms to prevent and sanction corruption in countries where they provide aid. This includes programmes or activities to reduce corruption risks in specific sectors (e.g. in education), and cross-cutting interventions that reduce corruption across the public administration (e.g. by improving public financial management and procurement practices; law enforcement capacities; meritocratic civil service, etc.).

Two, donors support efforts at the international policy level to minimise opportunities to benefit from the proceeds of corruption, in particular grand corruption. The efforts range from enhancing transparency in international financial and economic transactions and related instruments to improving the effectiveness of international cooperation in transnational crime investigations. In certain developing countries where governments are unwilling to fight corruption, and civil society is prevented from doing so, these international efforts may be the only – if indirect – opportunity to counter corruption at all.

Three, donors have also stepped up efforts to tackle corruption within their own development operations, i.e. the programmes and projects they fund, whether these be administered by national governments, national or international NGOs, or private contractors. It is this latter set of interventions – in particular, those implemented by NGOs – that are of interest to the present report.

Development assistance implemented through NGOs is a particular mode of cooperation that constitutes a significant proportion of many donors' portfolios. Working with and through NGOs provides both unique advantages and unique corruption risks. For this reason the report focuses on the question of corruption risks in development assistance to and through NGOs.

## 1.1 Methodological considerations

The research informing this paper was conducted through desk reviews and interviews of four donor agencies – the Australian Agency for International Development (AusAid), the UK Department for International Development (DfID), the Norwegian Agency for Development Cooperation (NORAD), and the Swedish International Development Cooperation Authority (Sida) – and the following well-established national and international NGOs: the Norwegian Refugee Council, Norwegian Church Aid, Save the Children Norway, and Oxfam GB. Some information from the World Bank and the Danish Refugee Council was also considered, but a full analysis was not done. Relevant materials available in the public domain and published research were consulted whenever possible, along with related U4 research.

Beyond the materials received from the partners above, there is very little research available on the issues covered. Empirical evidence is particularly scarce, as both donors and NGOs are reluctant to discuss the effectiveness of their corruption risk management measures, particularly discovered cases of corruption, because these may be misinterpreted as evidence of failure rather than good performance of corruption detection systems. In addition, there are extremely few processes in place, even in-house, to test and analyse the effectiveness of applied risk management measures. Hence, many of the findings are based on practitioners' observations and experiences rather than quantitative data.

In absence of indisputable empirical evidence that certain types of measures are more effective than others, organisations are advised to allow for a testing period of any measures that are selected for implementation before fully integrating them into operational routines. This approach would permit them to collect data and develop an evidence base to evaluate their effectiveness and cost/benefit ratio, although care should be taken to ensure that sufficient time is allowed to properly measure and understand the benefits of a particular approach.

The authors wish to acknowledge extraordinary responsiveness and assistance received from the partners contacted. All errors and omissions are the sole responsibility of the authors.

This paper is organised in three main parts. The first part provides a background discussion of corruption risks in development cooperation as they relate to NGOs as opposed to other development partners, and how these can be managed.

The second part presents a selection of most commonly applied NGO corruption risk management measures along with a discussion of their benefits and drawbacks.

The third part concludes the discussion by addressing the main concerns in applying the recommended measures and developing an NGO corruption risk management system.

## 1.2 Corruption and development

### 1.2.1 How does corruption undermine development?

Corruption has come to be universally recognised as one of the greatest obstacles to development around the world.

Widespread corruption within a country means that funds intended for economic and social development are diverted into private pockets, impeding growth and eroding the quality of basic services (such as education or health care), which in themselves can contribute to positive national development outcomes. Corruption also undermines the development of domestic markets and entrepreneurship, both of which require transparency and confidence that the same rules apply to everyone. In their absence, actors seek to minimise risks by joining the informal rules of the game, making markets ineffective and excluding.

Moreover, corruption destroys societal trust necessary for the development of sectors that depend on confidence and cooperation beyond the family, kinship and clans. Representative democratic institutions and processes often suffer due to such mistrust. Corruption also creates disincentives to participation in formal state structures, including, for instance, paying taxes, which holds further economic consequences: decreased state revenue, fewer funds for essential services and development, and continued poverty – the very reason and main priority of development aid.

More specifically relevant to the present discussion, corruption occurring within a development cooperation programme itself undermines all other programme objectives by diverting funds away from their intended purposes and activities, and reducing their overall impact. Unlike waste, inefficiencies, delays, or other challenges to aid effectiveness, corruption within a programme poses additional dangerous consequences, particularly reputational consequences for the donor agency, and a decline in domestic support for development aid more generally. In addition, a donor agency that is ineffective in curbing corruption within its own programmes will lack the authority to convincingly enter into a partner dialogue (particularly with partner governments) around the adoption of certain anti-corruption norms and mechanisms. It may even be seen as undercutting the increasing donor solidarity in confronting corruption.



## 1.2.2 Responses to corruption in development

In response to the first corruption challenge identified above, donors have been supporting reform programmes and measures to reduce corruption – either as sub-components of broader service-delivery reform initiatives (e.g. health), or focused on so-called “cross-cutting areas” that affect the whole of the public administration (e.g. public financial management and procurement practices or law enforcement capacities, etc.). Many observers agree that the quality of such anti-corruption programming has improved over the past decade, not least because important investments have been made in distilling lessons and producing resources to guide practitioners in understanding the challenges and applying anti-corruption measures.<sup>1</sup>

However, the focus of this paper is on the other corruption challenge identified above – “internal” corruption, or corruption within donor-funded programmes.

The issue of corruption in development aid has begun receiving increasing attention from the donor community in recent years, but the resources in this area remain limited and mostly focused on aid modalities and other partners than civil society organisations. This paper therefore seeks to address a knowledge and resource gap on the underappreciated challenge of addressing NGO corruption, which should be given greater attention considering the relative volume of support which NGOs receive.

## 1.3 NGO corruption risks

### 1.3.1 Why do donors support NGOs?

There are numerous reasons why donors support NGOs. A vibrant civil society is viewed as an indispensable element of democracy, which will hold governments accountable, along with other oversight institutions. During the process of democratic development and consolidation support for nascent organisations is indispensable so that they can begin to play a role, amongst others, in the fight against corruption.

Civil society organisations are also seen as essential in mobilising communities to participate in the development process more generally, especially where formal representation and participatory decision-making mechanisms may be flawed. The engagement of civil society is also increasingly applied by aid implementers as a method to oversee and validate the results of specific development programmes.

Furthermore, northern and international NGOs play a central role in donors’ development efforts as programme implementers. For instance, some NGOs specialising in providing relief in humanitarian

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<sup>1</sup> For instance, the U4 Anti-Corruption Resource Centre ([www.U4.no](http://www.U4.no)) has developed extensive resources on the following themes:

- Anti-Corruption Agencies
- Corruption and Aid
- Donor Coordination of Anti-Corruption Efforts
- Education Sector
- Emergencies
- Ethics
- Fragile States
- Health Sector
- Justice Sector
- Natural Resource Management
- Political Corruption
- Private Sector and Corruption
- Public Financial Management and Procurement
- UNCAC and other conventions

crises have developed impressive operational capacities, and stand as the best implementing partners overall.

But not all NGOs possess equal capacities, including the capacities to prevent and confront corruption in their operations, nor are they all always motivated by the highest moral principles. Hence, the need to understand and tackle the challenge of NGO corruption is great.

### 1.3.2 Why is it important to address NGO corruption?

In addition to reducing the extent or impact of programme benefits noted above, NGO corruption holds additional specific harmful consequences.

Within the broader society corruption undermines citizen trust in the state and its institutions. In the context of NGO operations, corruption can not only destroy the organisation in question, but also undermine the legitimacy of civil society more generally. The damage can be particularly detrimental in contexts where the sector plays a critical/watchdog role vis-à-vis with the state.

Corruption within an NGO can compromise the public perception of universal values that the discredited organisation is promoting, especially potentially unpopular issues such as democratic reforms, or minority rights.

Corruption among NGO grantees can discredit the donor agency as well, and undermine public support for development efforts in the donor country, with tax payers being legitimately concerned that their funds are being stolen rather than helping people in need.

Finally, not confronting corruption with sufficient vigour when it does happen also represents a disservice to those who are not corrupt – and that is the majority of aid recipients. Donors and their partners have a responsibility to express solidarity and support those who are resisting and fighting corruption, which includes preventing and sanctioning corrupt behaviour when it occurs within their own ranks and within the programmes they fund.

### 1.3.3 What are the forms of NGO corruption?

The term corruption refers to a range of illegal or morally objectionable practices that represent – according to the most comprehensive globally recognised definition – *the abuse of entrusted authority for private gain*.<sup>2</sup>

This characterisation contrasts with other well-known definitions, as it represents a shift away from a focus on public officials as a necessary party in a corrupt act. It thereby recognises that corruption can take place within private entities as well. The distinction is relevant for the present discussion, as NGOs are in fact private entities capable of engaging in corruption.

The range of potential corrupt practices committed by NGOs in the development context is extensive. They can be committed within routine institutional operations as well as within programmes and project activities. Some of the most commonly documented forms of NGO corruption include the following:

- “Fictitious” NGOs, established solely to generate income for executives or Board members;
- “Double-dipping”, or seeking or accepting funds from more than one donor for (parts of) the same project;

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<sup>2</sup> This is the definition advanced by Transparency International, [www.transparency.org](http://www.transparency.org).

- Financial irregularities such as inflated, duplicate, or fictional invoices for goods and services procured for a project;
- Kickback arrangements in procurement of goods or services, in hiring of project staff, or in distribution of goods and services;
- Extortion of bribes or other benefits (including sexual favours) from beneficiaries in order to include them on goods/services distribution lists;
- “Ghost” employees, participants or beneficiaries that inflate the costs of project activities.

Other abuses of entrusted authority stem from the influencing or creation of NGOs to represent the agendas of public or private sector interests to gain a perceived societal legitimacy. Such movements sometimes go under the term of “astro turf” (the commercial term for fake lawns) in order to denote the false impression of representing a genuine grassroots movement, rather than a fake, co-opted or coerced one.

What should be noted from the above examples is that many of the corrupt acts perpetrated by NGOs are no different from those in other aid modalities (e.g. kickback arrangements for the procurement of goods or services); others are unique (e.g. NGOs set up solely to generate income for executives of Board members). The distinction raises the issue of NGO specificities, which will be discussed below.

#### 1.3.4 Understanding NGO corruption risks

In project management literature, there are many variants of the definition of “risk,” but one phrasing that is likely to be widely recognised and relevant for the present discussion may be *events or conditions that may occur, and whose occurrence, if it does take place, has a harmful or negative effect*.

The discussion is shifting to the concept of “risk” because the primary interest of this paper is to promote an understanding of the factors that contribute to the possibility that certain corrupt acts will occur, so that appropriate responses can be identified and applied.

The following key factors shaping NGO corruption risks should therefore be kept in mind:

**NGO specificities:** Unlike partner governments, NGO are not subject to legislative norms that apply to state agencies or the same oversight mechanisms. They are private entities not subject to the same checks and balances. Accountability is enforced primarily through their internal rules and procedures, which therefore need to be evaluated for potential and demonstrated effectiveness in curbing potential corruption.

**Differences in capacities:** Not all NGOs have equally strong institutional capacities, yet corruption risk management systems depend to a large extent on such capacities. Lower capacities typically present a greater vulnerability to corruption in NGO operations.

**Partners of partners:** Whilst the majority of donors’ key partner NGOs will have excellent mechanisms in place to prevent corruption in projects that they implement, it must be remembered that they, in turn, often work with in-country partners who do not possess equal capacities or equally robust systems. Operating through national partners can change the risk calculation considerably, inter alia, by introducing distance and additional layers of decision-making and administration that makes the enforcement of standards and oversight more difficult.

**Type of operation:** Organisations acting as donors will have different risks than organisations that implement projects. Similarly, different risks are present with advocacy organisations as opposed to those providing humanitarian assistance or educational services. Risk management measures need to be tailored according to the types of operations an organisation undertakes.

**Specific activities:** At the lowest level, different corruption risks are inherent in different operational activities, for instance personnel recruitment vs. procurement. Prevention and mitigation measures will differ accordingly.

**Operational context:** Programmes in countries with systemic corruption are likely to encounter higher corruption risks than those in countries where corruption is not a major problem. Higher risks have been found to apply with other environmental conditions such as post-conflict or humanitarian emergency contexts.

The above factors are the key sources of corruption risks in development assistance delivered to and through NGOs. Particular combinations of above factors may construct especially high-risk situations. Nevertheless, there may be compelling reasons to provide support through NGOs. Corruption risk management systems need to be sensitive to the specific risks encountered and able to activate mitigation measures that are tailored to the particular challenges.

## 1.4 Managing corruption risks

### 1.4.1 What is corruption risk management?

The concept of risk management is likely to be rather familiar to programme staff in most donor agencies, who probably already apply risk management concepts and practices in designing and reviewing programme and project proposals.

The risk management process arises from the discipline of project management, and broadly consists of the following steps:

- Identifying the risks/threats to realising programme/project objectives;
- Assessing the level of seriousness each risk (*probability* and potential *impact* if realised);
- Identifying and prioritising measures to reduce those risks; and
- Application of measures to minimise the probability or impact of harmful effects.

To fully address corruption risks, however, this approach needs to be understood beyond project management practices as such. The most important finding of the analysis informing this paper is that corruption risks are addressed not only through project management measures, but also through a wider set of mutually-reinforcing institutional mechanisms. The paper will present these mechanisms and discuss how they impact the institutional and programme risk calculation overall.

### 1.4.2 Components of a corruption risk management system

Generally speaking, the fight against corruption – whether within specific projects or institutions, nationally or globally – consists of two broad categories of interventions: preventive mechanisms and sanctions. Prevention is essential, but no system can always prevent corruption, no matter how many safeguards are put in place. Whilst opportunities for corruption (corruption risks) can be greatly reduced, human beings always seem to find a creative way to perpetrate corrupt acts. Hence, mechanisms for dealing with corruption incidents when they do eventually happen must also be in place.

When the notion of a prevention–sanctioning system is expanded and adapted to the development context, the necessary measures – elements of a corruption risk management system – might be grouped as follows:

- Measures that identify corruption risks;
- Measures that reduce the corruption risks (opportunities for corruption);
- Measures to detect corruption;
- Responses: investigative measures and sanctions to address corruption once it is suspected or identified with certainty; and
- Implementation mechanisms for the totality of the measures noted above.

A corruption risk management system, then, encompasses all of these sets of measures and covers multiple levels of institutional operations, both within the project cycle as well as in ongoing institutional policies and processes. This means that managing corruption risks effectively requires the involvement of all levels of an organisation: programme staff, anti-corruption/anti-fraud officers, and administrative and finance staff. Conversely, corruption risk management measures need to be integrated into various levels of institutional operations.

### 1.4.3 Developing and applying a corruption risk management system

This report provides recommendations both on corruption risk management measures at various levels of operations, as well as measures required to implement them effectively. Their totality forms a comprehensive corruption risk management system.

Again, the focus is on NGO corruption risks, particularly issues that concern their internal structure and operations, but many of the recommended measures apply equally to other types of partners and aid modalities.<sup>3</sup>

Furthermore, whilst the main “target audience” for the recommended measures are donor agencies, the vast majority of them can be equally applied by NGOs as well – particularly by the well-established, institutionally mature NGOs that are typically the key implementing partners for donor agencies. In fact, many such NGOs will have more extensive corruption risk management systems than the donors due to their more operational character and thus greater exposure to corruption risks.

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<sup>3</sup> Unfortunately, it is beyond the scope of the present effort to address the risks associated with other implementation partners (e.g. private contractors or state bodies), or risks inherent in specific types of operations or activities. Follow-up efforts in this direction are therefore strongly encouraged. Some operation specific resources already exist: for instance, Transparency International’s 2010 publication *Preventing Corruption in Humanitarian Operations*, but more research and systematisation of existing knowledge are needed.

## 2. Recommended corruption risk management measures

As noted in the introduction, the recommendations contained in this report are based on an analysis of a number of corruption risk management systems in place in donor agencies and large national and international NGOs. These good practices will be presented in two separate sections:

- Section 2.1: Elements of a comprehensive institutional corruption risk management system
- Section 2.2: NGO partner standards

The measures in section 2.1 will be equally applicable to donor organisations and institutionally strong, key partner NGOs (but less so to smaller and less developed NGOs). These measures are also largely applicable for other aid modalities – beyond cooperation with NGOs – at least in terms of identifying corruption risks, if not the remedies.<sup>4</sup>

The measures presented in section 2.2 apply to NGOs specifically and should not be considered as criteria for other types of partners. These criteria have been defined by civil society organisations themselves, for instance, as part of self-regulatory systems developed in setting where NGO corruption has been seen as a threat to the sector.<sup>5</sup> Whilst the majority of the institutionally strong partner NGOs will have little difficulty in meeting the proposed requirements, many less developed partners will struggle to do so. The accompanying discussion will also explore possible responses to the challenges specific to NGOs with less capacity.

### 2.1 Elements of an institutional corruption risk management system

#### 2.1.1 Prevention: measures to identify and mitigate corruption risks

##### *Environmental corruption risk analysis*

Whether at the level of multi-year strategy or specific programme formulation, analyses should be undertaken to assess corruption risks associated with:

- The country, region, or locality where engagement is to take place, and
- The sector (e.g. health) or activity (e.g. food distribution) that is being contemplated.

The depth and extent of risk assessments at preparatory programme phases varies considerably among donors and implementers. Most agencies conduct some form of mandatory risk appraisal as part of the overall situation analysis, but often there is insufficient guidance on how to conduct a corruption risk assessment: what are the relevant key questions, where to seek reliable information, and how to interpret it.

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<sup>4</sup> Their relevance for other aid modalities and partners will decline in line with restrictions inherent in relationships with other partners, for instance other donors or partner governments. In those cases, the recommended partner selection criteria are largely irrelevant – as these are specifically tailored to NGO partners; the contracting or monitoring and evaluation options might likewise be quite limited.

<sup>5</sup> See, for instance, the Philippine Council for NGO Certification (PCNC) Guidebook on the Basics of NGO Governance available at <http://www.pcnc.com.ph>.

Individuals performing such assessments can access numerous external resources in order to begin building a corruption risk profile that could inform a range of in-country activities. Well known global resources such as the Transparency International Corruption Perception Index (CPI) or the World Bank Worldwide Governance Indicators are often used for this purpose, but they represent, at best, only the first step in understanding the context: these sources provide very little insight as to the key corruption threats in the country, sectors affected, existing anti-corruption mechanisms, or the main drivers of corruption in the country.

*A thorough qualitative analysis of the specific corruption situation is necessary, particularly if a donor contemplates a longer-term engagement.* Such assessments are rarely undertaken, however, and programmes and projects are often initiated without a proper understanding of the corruption risks being confronted.

It is therefore *strongly recommended that donors institute a practice of performing an in-depth country/sector analysis of the corruption situation as part of preliminary programme and project assessments.* The necessary background information may already exist in the public domain in the form of analytical reports by national or international organisations. Where such assessments are not publicly available, it is a worthwhile investment to conduct such analyses either in-house, in cooperation with other donors or NGO partners, or even to outsource them altogether.

In cases where the analysis is done internally, donors are further advised to provide the responsible staff with guidance on how to perform such assessments.<sup>6</sup>

If performed diligently, this initial investment would provide donors and their partners with an initial corruption risk assessment (more specifically, different assessments depending on the sector of engagement) that would inform all subsequent steps of programme implementation, so that appropriate mitigation measures and safeguards could be considered and integrated into specific programmes. The assessment should also provide an insight into the extent of corruption afflicting civil society organisations.

This measure is a general good practice, recommended for all types of organisations contemplating initiating development cooperation, and for all aid modalities, regardless of the implementation partner(s).

#### *Partner selection criteria/due-diligence measures*

The selection of reliable and reputable partners is recognised as one of the most important processes in limiting opportunities for corruption and achieving programme impact. In contrast to corruption risk assessments of the broader national or sector contexts, donors typically have more detailed guidelines for reviewing potential NGO partners, including the following criteria:

- Compliance with national NGO laws and regulations (e.g. concerning registration and financial reporting);

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<sup>6</sup> At a minimum, the responsible staff should be supplied with a checklist of specific questions to be considered (e.g. what are the main forms of corruption and sectors affected), and guidelines on resources such as:

- Transparency International Global Corruption Barometer (GCB) data
- Global Integrity Report (score card and narrative data, where available)
- Other donors national/sectoral assessments
- National NGOs assessments (e.g. Transparency International chapters' National Integrity System surveys)
- State institutions' assessment (e.g. national Anti-Corruption Agency reports, service delivery reports, sectoral assessments).

- Legal representatives of the NGO;
- NGO's managing and accounting system, including routines for audit;
- NGO's past performance;
- NGO's institutional capacity for financial management and corruption prevention.

For many donors initial in-house assessments are complemented by more in-depth evaluations of financial management capacities and practices, particularly when long-term cooperation or high-value grants are being considered. DFID, for instance, has moved toward outsourcing such due diligence measures to private contractors.

Inevitably, not all NGOs seeking support have equal capacities and donors have been responding to the distinctions (i.e., the perceived differences in corruption risk levels) quite differently. For instance, NORAD currently manages the disparities by varying the duration and form of support (one-year or three-year project agreements for new organisations and small organisations, and longer-term cooperation or core support agreements for medium-sized and large organisations with long experience in development assistance). DFID, by contrast, has developed different grant programmes altogether for NGOs of differing capacities, and part of the variation lies in the caps for funding for which they are eligible to apply.

Whilst evaluating an NGO's past performance can be a relatively simple yet effective indicator of corruption risks of an NGO, donor agencies have traditionally placed more emphasis on financial management capacities. By contrast, in their self-regulatory efforts, civil society organisations have themselves emphasised criteria such as organisational management and governance standards for NGOs. These include institutional oversight mechanisms and other management processes that impact on a wider array of corrupt practices beyond fraud and embezzlement. In that respect, *NGO self-regulatory standards represent a significant advancement from most existing donor selection criteria and deserve serious consideration for integrating into the donors' existing corruption risk management systems.*

Due to their high level of detail, NGO selection criteria and standards will be elaborated separately in section 2.2, organised in the following categories:

- Governance structure and standards;
- Integrity policies/codes of conduct;
- Transparency standards;
- Human resources management policies;
- Financial management standards; and,
- Downward accountability measures.

The final issue to review among partner selection criteria is whether the partner applying for support will be implementing the proposed programmes directly or whether the implementation will be carried out by national partners, who are unlikely to have the same capacities and the same corruption risk rating as the main implementing partner. *This circumstance may alter the risk calculation considerably, thus partner selection criteria should also be applied to all the partners in the implementation chain.*



### *Programme operations and activities*

Once the corruption risk level has been established for the overall programming context, along with that of the potential local partners, risks inherent in a particular programme or project should also be evaluated to the extent possible.

This is arguably the most difficult aspect of corruption risk assessments, as the risks will closely relate to the type of operations and activities being undertaken. As noted in the introduction, NGOs acting as donors (e.g. re-granting operations) will have entirely different risks than those implementing projects.

Different project activities will also involve different risk levels: distributing food and supplies to earthquake survivors amid general chaos arguably holds more risks for corruption than selecting a service provider for a conference.

Unfortunately, there is no consolidated guidance for identifying and mitigating corruption risks in all operational contexts and all types of activities, but some of the most challenging ones have been codified.<sup>7</sup> Many such instruments also exist as internal materials among implementing agencies – particularly among the high-capacity NGOs with extensive operational experience. Even where the materials have not been codified, important knowledge often resides with individuals within organisations, including with local partners with otherwise limited institutional capacities.

*Whether or not published resources exist, donors are advised to evaluate to the extent possible specific operational corruption risks and potential responses in close consultation with the partners.* The same advice holds for high-capacity NGOs with regard to their national implementation partners. In the longer term, donors are also advised to support their partners in codifying and sharing the experience gained, as well as other efforts to develop guidelines on tackling activity-related corruption risks.

#### 2.1.2 Measures to detect corruption

##### *Implementation monitoring*

Regular programme monitoring is widely considered the most effective corruption risk mitigation measure during the implementation phase. *Written activity- and/or financial reporting is a minimum measure, but on-site monitoring visits are pivotal to discovering corrupt activities.* It is also commonly held that just the *expectation* of being observed and examined serves as a compelling deterrent for individuals who may otherwise consider engaging in corruption.

There are a myriad of ways to conduct monitoring visits and inspections. Whilst the most important challenge is actually finding the resources and the time to conduct them altogether, experience suggests that visits are most effective if they are done with mixed teams of finance specialists and programme staff, and if they are not always announced in advance.

Commonly recommended elements of visits or inspections include the following:

- Review of relevant documentation held by the NGO;
- Examination of the NGO financial accounting management systems and relevant documentation associated with the preparation and management of project funds in question;

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<sup>7</sup> See for instance, Transparency International's 2010 publication *Preventing Corruption in Humanitarian Operations*, available at: [http://www.transparency.org/publications/publications/humanitarian\\_handbook\\_feb\\_2010](http://www.transparency.org/publications/publications/humanitarian_handbook_feb_2010).

- Review of relevant project files and claims paid by the donor;
- Discussions with appropriate NGO personnel; and
- Written documentation of the findings;
- Control, when possible, of the planned deliveries and their specified standards;
- Discussion with stakeholders/intended beneficiaries.

*Donors are advised to secure more resources for conducting field visits and inspections, particularly of in-country implementing operations and local partners.* Such visits could also be undertaken jointly with the lead implementing partner NGO that is contractually responsible for the programme delivery, or, where donor capacities are limited, only by the partner. What is essential is that sufficient monitoring is planned and financially supported within the project or programme.

Donors are also encouraged to support knowledge sharing on useful corruption risk management tools such as guidelines for conducting monitoring visits.

#### *Evaluations and audits*

Evaluations and audits are the most common forms of *ex post* risk management tools. Neither tool is used for all projects, however. Whilst audits are frequently compulsory, external independent evaluations are typically planned only for projects over a certain monetary value due to their high costs. Existing research, including feedback received from organisations surveyed for this report, suggests that the effectiveness of audits may be overestimated.<sup>8</sup> Evaluations, too, have a mixed track record of effectiveness in revealing corruption.

Despite their lack of demonstrable effectiveness in terms of detecting corruption, donors might be able to enhance the effectiveness of audits by:

- Screening and identifying quality auditors to be engaged by NGOs; and
- Requiring a comprehensive audit of an organisation's finances, rather than a project audit, to increase the likelihood of identifying double-billing or other irregularities.

As concerns evaluations, it seems advisable to consider enhancing their potential as learning instruments, rather than tools to detect corruption. Internal evaluations are particularly valuable in this respect: whilst they may lack in objectivity, they may also yield surprisingly frank appraisals by staff who are intimately familiar with all the challenges encountered during implementation.

*The key is to ensure that the findings are used for institutional learning purposes and improving work processes and procedures (particularly corruption-risk mitigation measures), rather than as a basis for sanctions for errors and omissions.* Ideally, evaluation findings would also be shared more broadly among partners within the wider development community, but reluctance remains despite the near universal recognition of the benefits of learning from past experiences.

There is no ready-made solution to overcoming the reluctance to share past lessons, particularly those where corruption was involved. Donors and NGO partners of all capacities are encouraged to openly discuss the perceived risks of public access to evaluation findings and how these may be addressed.

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<sup>8</sup> See U4 Issue paper *Countering NGO corruption: Rethinking the conventional approaches*, March 2011, No 3, available at <http://www.u4.no/document/publication.cfm?3969=countering-ngo-corruption>.

### *Reporting and whistle-blowing mechanisms*

All organisations should have mechanisms in place to receive reports of suspicions of corruption and other misconduct, whether from within the organisation or outside it. This holds true even for NGOs with the lowest levels of capacity, although their systems are unlikely to be particularly well developed. Donors' and more advanced NGOs' *whistle-blowing systems* should have the following main characteristics:

- For staff, the *obligation* to report suspected corruption;
- Well-publicised procedures and a clearly communicated commitment to pursue administrative and criminal sanctions against wrongdoers;
- Points of confidential contact;
- For staff, the option to bypass immediate superiors, even go outside their local unit, directly to headquarters;
- Mechanisms to deal appropriately with unfounded or malicious allegations of corruption;
- Procedures to protect whistle-blowers from retribution; and
- Staff trained to deal with corruption allegations.

An organisation's internal *incident reporting procedures* need to be distinguished from whistle-blowing mechanisms. An incident reporting system aims to track a wider range of incidents that a staff member may experience, such as assault, theft, or being asked to pay a bribe, which do not necessarily require employee protection or confidentiality. *Recording of all incidents is important for an organisation, as it serves not only to account for potential financial losses, but also to learn and improve existing prevention and risk mitigation measures – and not only in regard to corruption.* It thereby represents one mechanism of many to protect the legitimacy of development aid. A corruption reporting/whistle-blowing system is different from an incident reporting system because it allows for confidential reporting of suspected or identified corrupt actions (as well as other offenses) from both inside and outside the organisation, and affords the person making the report protection from reprisals.

Most major donors and many large, high-capacity NGOs have whistle-blowing systems in place. The distinctions in practices mostly involve the extent to which supporting materials and procedures are developed. For instance, whilst most organisations will have step-by-step guidelines for reporting suspicions of corruption, including names and contact information of responsible individuals/units, they do not all provide extensive definitions of concepts such as confidentiality or defamation, or of forms of corruption (e.g. conflict of interest vs. financial irregularities), or explain in full how whistleblowers will be protected (although this may be a particular concern for overseas local staff). At the other end of the spectrum are organisations that go as far as providing very explicit guidelines on conduct upon detecting corruption – specific DOs and DON'Ts such as “Don't confront the suspected individual(s) yourself.”

Specific guidelines and training should also be in place for staff responsible for undertaking an initial investigation of a report in order to assess whether there is sufficient basis to proceed more seriously (after all, not all reports will be *bona fide*). *There is a need to identify and protect any evidence that may exist, as well as to protect both the whistle blower and the suspect(s) until some clarity about the case can emerge, and it should not be assumed that staff automatically know how to do so.*

Many NGOs surveyed found whistle-blowing systems to be an area where they could improve their work. Furthermore, in instances where both the donor and the NGO partner have developed whistle-blowing systems, the challenge will be one of coordination: agreeing on which set of guidelines will be publicised in project activities, identifying the point at which the other party is to be informed

should a report be found worthy of investigation, potentially dividing the responsibilities (and costs) of the preliminary and advanced investigations, prosecutions, and sanctions, etc.

Both donors and leading NGOs are advised to review their whistle-blowing system for comprehensiveness and effectiveness, and engage in dialogue about coordination with partners who have their own systems. When working with partners who do not have their own systems, it is essential to clearly state expectations about how the more developed party's mechanism is to be used and to clarify any questions that may exist about the concepts or actual procedures. In the unlikely case that neither the donor nor partners have established mechanisms, it is strongly recommended that a basic mechanism be established as part of programme or project activities.

In addition, *donors are advised to support NGOs in developing and strengthening their own corruption reporting systems as needed.*

### 2.1.3 Responses to corruption: investigative measures and sanctions

#### *Corruption investigations*

Distinct from initial investigations that can be considered part of a whistle-blowing mechanism, specialised corruption investigations – typically in-depth financial investigations – require extensive expertise and resources. Unsurprisingly, few donors or advanced NGOs have internal units specialising in such work. Investigations of suspicions of fraud and corruption are instead usually delegated to internal audit departments, yet in most cases, these departments lack the internal capacity to conduct proper corruption investigations themselves. In most cases of financial misconduct, external assistance is needed, as well as the funds to support it.

However, not all corrupt acts will involve project financial irregularities as such – for instance cases of kickback arrangements or extortions of payments from beneficiaries for goods or services they are supposed to receive free of charge, not to mention nepotism in hiring practices or mismanaged conflicts of interest. Unless the matter is serious enough to turn over to the national police, some protocols would need to be in place and guidance available on investigating the matter internally.

Donors and NGO partners are therefore advised to define arrangements for dealing with corruption investigations. Among other steps, this would include:

- Agreement on when – at what stage – to notify each other about corruption incidents or suspicions;
- Protocols for such communication;
- Agreement on the investigation protocols and division of responsibilities;
- Contractual obligation to provide access to all internal documents and archives (in case the partner is uncooperative) – such agreements should extend to all the partners in the implementation chain; and
- Funds to support the costs of the investigation.

The most important consideration of all is that founded suspicions of corruption are adequately investigated and, if sufficient evidence exists, sanctioned. The quality of the investigative process – both competence/rigour and the perceived fairness – determines the applicability of appropriate sanctions, which in turn impacts the credibility and the deterrent effect of the entire sanctioning system.

### *Sanctions*

If corruption is indeed uncovered, sanctions proportional to the scope and seriousness of the offence need to be applied, and many donors have adopted a differentiated penalty system to reflect the circumstances of an offence. While the monetary value of the breach is one of the variables to be considered, there are other equally, if not more important, ones. For instance, some donors, such as DfID, apply stricter sanctions in cases where it has been determined that a *deliberate* effort to defraud had been made (as opposed to, for example, a single opportunistic act made possible by some flaw in the control systems).

At the other end of the spectrum are rigid systems that respond to all incidents of corruption in the same manner – for instance, by freezing programme funding and requiring repayment of the unaccounted for funds, regardless of the circumstances.

*A warning against such unsophisticated policies is in order, as they may generate serious negative consequences, precisely contrary to intended objectives.* The following considerations should be borne in mind when designing a sanctions strategy:

- Proportionality of sanctions is a core principle of justice (and justice systems in democracies). The same principle should equally apply in non-criminal, institutional sanctions strategies, with a range of reactions and penalties defined to reflect the circumstances and severity of each particular offence.
- Criminological studies repeatedly confirm that the *likelihood* of punishment is far more effective deterrent than their severity. In other words, it is more important to always punish wrongdoing with appropriate (proportional) sanctions than to apply tough penalties inconsistently or occasionally.
- Insufficiently differentiated sanctions strategies often lead to situations where the decision-maker is presented with two equally problematic options: applying a disproportionately harsh penalty or dismissing the case and not applying one at all. In view of the deeply engrained sense of injustice inherent in the former, most enforcers opt for the latter. A lack of an adequate range of available sanctions therefore actually undermines sanctioning altogether, and any deterrent effect it may hold: the non-application of sanctions increases the risk that corrupt acts will be perpetrated.
- Disproportionate sanctions and sanctioning systems perceived as unfair or unjust can also have a negative effect on the *reporting* of wrongdoing. In effect, an unfair system undermines cooperation and compliance, again, increasing the risk that corruption will go undetected or unreported.
- An important factor contributing to the perceived fairness of a sanctioning system is the transparency and predictability of the decision-making process – clarity as to what steps would be taken, how the “suspect” can respond, what evidence and contextual factors would be considered, and who would be involved in the process, including who makes the final sanctioning decision.

To deter future wrongdoing, a sanctioning policy needs to:

- Promote a clear understanding of what practices are considered corrupt by the donor and in the project being supported;
- Encourage detection and reporting of all corrupt practices through a variety of mechanisms;
- Define a range of sanctions that are broadly perceived as fair and proportional to the offences;
- Ensure that such differentiated sanctions are applied consistently, for all identified breaches;

- Verify that the entire sanctioning system is clearly defined, transparent, sensitive to the context, and perceived as fair by partners who are subject to it.

A sanctioning policy should also reflect on the circumstances under which criminal sanctions or a civil case would be pursued. There are sometimes legitimate reasons to refrain from seeking a judicial outcome, for instance, if the offence occurs in a national context with weak rule of law or poor law enforcement capacities. Many corruption offences are notoriously difficult to prove even in well-resourced and effective criminal justice systems. *The decision to pursue particular cases should be made in close consultation with partners to ensure that the full range of relevant issues is considered before a decision is reached.*

Furthermore, a sanctioning policy should include considerations of information-sharing and public disclosure of detected wrongdoing. Information-sharing may include, for instance, passing on to partners (other donors, implementers, NGOs) information about organisations that have been sanctioned for corruption or blacklisted from further cooperation. Public disclosure of incidents – often a legal obligation for donors under national access to information laws as well as a good practice – could be misused by opponents of development efforts or particular organisations, and hence needs to be executed with some care. The needs of NGO partners and presentation strategies should be carefully considered while remembering that having a corruption case independently “discovered” by the media creates the impression of concealment and dishonesty, which ultimately causes far more harm in the long term.

Many of the shortcomings of existing donor sanctioning policies reflect a need to present a tough stance against corruption in development aid for domestic purposes, originally in response to increased awareness of corruption challenges in development (and numerous scandals) over the past couple of decades, and more recently in the wake of the global economic crisis that has necessitated painful budget cuts and dampened popular support for development aid in many countries. Some of this posturing has led to the adoption of ill-conceived “zero tolerance” slogans (slogans rather than fully fledged anti-corruption policies), which appear equally popular among donors and some of the world’s most corrupt regimes.

*A zero-tolerance policy could be elaborated so as to be perfectly consistent with the considerations outlined above – at least in the context of NGO partners – for instance, in the insistence that even the smallest corruption manifestation receive a response proportional to its severity.* In practice, however, this tends not to be the case, as zero-tolerance positions are not intended to describe a policy but rather to signal toughness. As a result, they typically emphasise severity rather than the likelihood of sanctions – practices contrary to core principles of effective deterrence noted above.

The limitations of a poorly nuanced zero-tolerance slogan as a policy principle is further exposed when one considers the disincentives they create for other corruption risk management practices such as openly discussing corruption risks and corruption challenges, or for reporting incidents of corruption.

Zero-tolerance positions also ignore broader development objectives, and particular challenges associated with them – for instance, in humanitarian relief operations. Few people would advocate a strict zero-tolerance response in a situation where a small bribe to an armed militia leader is the price of delivering food, water, and medical assistance to thousands of refugees fleeing armed conflict. In such a setting, saying no to corruption needs to be weighed against the potential loss of countless lives. Even beyond this extreme example, *sanctions and all other corruption responses must be sophisticated and flexible enough to respond to very different circumstances so to function in service of, rather than contrary to, primary development objectives.*

## 2.1.4 Implementation instruments

### *Project documents and contracting*

Forms such as programme formulation templates, project proposal forms, proposal evaluation checklists, etc. should all serve as mechanisms to reflect on corruption risks identified in the overall context, prospective partner(s) and the activities being contemplated. They also present an opportunity to discuss with partners potential response measures, and to agree on the acceptable *residual risk*.

Residual risk is the risk that remains after mitigation measures have been taken. Again, no prevention system can be 100% effective, and in certain high-risk environments, possible mitigations measures will be limited, while the development imperative (typically a humanitarian imperative) will remain high. In such situations, it is important to agree on an acceptable level of risk mitigation that is balanced against the development objective. Arriving at that acceptable level will require difficult trade-offs.

The contracting stage provides the opportunity to formalise these agreements and mutual expectations between partners regarding corruption risk mitigation measures and systems to detect, investigate, and sanction corruption. *All corruption risk mitigation measures and other obligations should be clearly specified in the contract in order to establish a legal requirement to observe them. This also allows for a clear basis to react to eventual breaches.*

Few donor contract templates address corruption risk management measures in any great detail, apart from some basic financial management, procurement, or audit requirements. Much more detail could be developed in the form of annexes, which would not require major changes to the contract templates themselves.

*Donors are advised to review their current contract templates to ensure that all recommended and adopted corruption risk management measures can be incorporated and thus formally agreed with partners.* High-capacity NGOs who are sub-contracting other partners, particularly local partners with less capacity, are also urged to undertake the same measures.

### *Operational manuals and guidelines*

These types of documents typically elaborate in more operational detail the various corruption management mechanisms, for instance how to carry out a wider national assessment of corruption for the purposes of strategy or programme formulation, how to assess what corruption risks exist in procurements, or how the organisational whistle-blowing system works. Existing practices with regard to operational manuals vary, but may be divided into two broad categories: those that focus only on corruption and fraud-related mechanisms, and those that “mainstream” corruption-related measures together with other routine operations.

The first category – explicit corruption- and fraud-related procedures includes, but is not limited to the following kinds of guidance:

- Whistle-blowing procedures;
- Incident reporting procedures;
- Procurement procedures;
- Gift declaration procedures;
- Declarations of interests;
- Vehicle and inventory monitoring forms; or,
- Financial review checklists.

The second category – mainstreamed corruption risk management measures – typically includes the following types of instructions:

- Project/programme risk assessment guidelines;
- Partner/implementer assessment checklists;
- Checklist for project monitoring visits; or,
- Minimum standards for operating in emergencies.

They can exist as stand-alone documents, or be integrated into larger operating manuals covering all phases of project implementation. Often, they are referenced or linked to stand-alone anti-corruption policy documents that will be discussed in the next section.

Whatever operational guidelines may be in place, it is nearly always possible to supplement or expand them with additional guidance on managing particular corruption risks identified by staff. One of the NGOs surveyed had developed a paper for staff entitled “How to deal with requests for a bribe...” to assist them in confronting an apparently common operational challenge encountered in programme implementation.

Both donors and NGOs at all capacity levels are advised to survey their staff to identify the most common corruption risks and dilemmas encountered in their work, and strive to develop guidelines to meet those needs. Donors should support the efforts of partners to formalise and share their experiences and operational lessons.

#### *Policy documents*

In addition to operational guidelines, many organisations choose to elaborate a specific, stand-alone policy document addressing the threat of corruption and fraud, and outlining the totality of the mechanisms in place to combat it. The length and level of detail of these documents vary, but typically they include key definitions (e.g. various corrupt practices), the obligations of the organisation’s employees with regard to corruption, and a description of the preventive and reactive mechanisms in place to address corruption risks and incidents of corruption – the organisational corruption risk management system – and how to use it.

Other organisations have separate policy documents describing different components of the overall system. For instance, an explanation of preventive measures and their application within the project cycle may exist as one policy document, and the whistle-blowing system may be described in another. Whilst each of these individual policy documents are useful *a stand-alone document that presents the entire institutional corruption risk management system is important in promoting its recognition and acceptance*. The development of such an instrument is recommended *in addition to* – rather than *instead of* – these additional materials.

This recommendation applies equally to donors and NGO partners regardless of their institutional capacity. The main objective of a comprehensive anti-corruption policy document is to present a clear overview of the institutional corruption risk management system – no matter how sophisticated it is – and to signal a commitment to confronting corruption. Where local partners with less capacity may have difficulty in elaborating such an instrument, supporting them in this effort could form part of the partnership agreement and constitute a portion of project activities, alongside other essential corruption risk mitigation measures.

#### *Communicating the importance of fighting corruption*

The most developed corruption risk management systems continually reiterate the message of intolerance toward corruption and fraud through a number of means:



- Customary distribution and wide availability of corruption-related materials (e.g. code of conduct, complaints mechanism, whistle-blowing procedures, etc.);
- Regular discussion of corruption challenges, both internally and with external partners (e.g. at employee induction, during performance reviews of staff and external partners, during organisational “corruption awareness days”, etc.);
- Periodic training on corruption issues (e.g. a course like the existing U4 “Essentials of Anti-Corruption” module could be made mandatory for all staff, and additional trainings on specific topics could be further arranged for both staff and partners).

A commitment to the fight against corruption would be further communicated through the establishment or expansion of existing policy units charged with anti-corruption policies. Such units could, among other activities, undertake regular reviews of existing instruments and tools; track staff and partner corruption related concerns or challenges and explore remedies; manage knowledge on the topic; and develop additional assistance/guidance materials as necessary.

Donors and high-capacity NGOs are strongly advised to invest in both communication and policy development. NGOs with less capacity should be supported in at least developing the necessary materials and procedures to communicate their anti-corruption policy and mechanisms (the sustainability of such practices is a much less cost-intensive proposition and depends primarily on the organisational commitment).

## 2.2 NGO partner standards

The issue of due diligence and establishing partner selection criteria plays an important role for risk assessment and risk management. Of the donors surveyed, AusAid stands out in emphasising this approach, by having Australian NGOs pass through their established NGO accreditation system in order to access funding.

### 2.2.1 NGO institutional standards

As noted earlier, the measures recommended above for donor agencies are also widely applicable for partner NGOs – in fact, many of them have been identified among NGO rather than donor good practices.

By contrast, the majority of the criteria below concern governance and organisational structures specific to NGOs. As such, they constitute potential partner NGO selection criteria discussed in section 2.1.1 above.

Ideally, all NGOs receiving support would comply with these standards, but that is not a realistic prospect in context of at least two common development objectives. One, in certain settings – particularly emergencies – the range of local NGO partners may not be particularly extensive, and the choice comes down to working with a partner that does not meet the criteria below or not implementing a relief programme at all. Two, if the objective is to promote the development of civil society, then donors will aim to support precisely the new and less institutionally developed NGOs that do not meet the defined criteria.

Why, then, define such criteria at all? There are at least two reasons. One, it is useful to have benchmarks that emerging NGOs should strive to attain to become stable, institutionally developed, and sustainable organisations. Two, donors (and NGOs acting as donors) should be aware that partner weaknesses on the identified standards represent a corruption risk that needs to be addressed during cooperation through measures such as more intensive monitoring of activities, or institutional capacity building.

The criteria below might also be reviewed to arrive at additional corruption risk management tools. For instance, the standards might be prioritised to reflect differing levels of risk, according to which NGOs can be rated (e.g. grade A, B, C, D, etc.) and cooperation mechanisms be determined accordingly. It may also be possible to define a set of *minimum standards* for NGOs with low capacity, beyond which neither donors nor their key NGO partners would engage, even in emergencies.

#### *Governance structure and standards*

NGOs are private entities with a special status that distinguishes them from firms and other profit-making entities. An essential NGO accountability mechanism is its governance structure. The following standards are widely accepted as essential in this regard:

- Voluntary, not-for-profit and non-government character;
- Governing Body (Board), membership, and staff that do not profit from the NGO's assets;
- Legal entity, with identified office holders, with a documented structure of responsibilities and appropriate systems to ensure accountability, including to its supporters;
- Clearly defined governance structure, particularly role of the Governing Body in governing documents;
- Clearly noted separation of Board functions from management (if the CEO is member of the Board it should be in a non-voting role only);
- Public list of current Board members;
- Conflict of interest provisions for Board members;
- Membership rules (including eligibility, suspension, and expulsion);
- Clear election procedure;
- Defined terms of office (length of terms, limits on re-election);
- Minimum number of board meetings defined;
- Method of convening meetings defined (who initiates, how to set dates, who decides agenda, etc.);
- Decision-making procedures defined (number needed for quorum, how to vote and record decisions) and explicit indications that decisions are to be taken collectively;
- Records of Board meeting minutes on file;
- Rules on Board member remuneration (Board Members should not receive compensation beyond reimbursement of expenses); and,
- Mechanisms for members to raise issues at governing body level and evidence that the NGO has made those mechanisms known.

For larger NGOs, additional standards may be considered, for instance, on fundraising and income generation practices.

#### *Integrity policies: codes of conduct*

Donor organisations typically have codes of conduct and other ethics rules as part of the regulatory framework that governs their work overall. This is not the case for NGOs. NGOs are private entities that are not bound by national civil service regulations, and hence, codes of conduct should be viewed as essential instruments for NGOs to promote ethical behaviour.

Codes of conduct typically address, at a minimum, conflicts of interest and gift policies, but also often deal with favouritism, bribery, discretionary authority and abuse of power, confidentiality, etc. They typically also emphasise other organisational values such as non-discrimination and respect for human dignity.

An indispensable feature of these policies is that they must apply to staff and members of the governing body, as well as volunteers. The most important elements of these policies include the following requirements:

- That members of the governing body, paid staff, and volunteers disclose any real or perceived conflict of interest or any affiliation they have with an actual or potential suppliers of goods and services, recipients of grant funds, or organisations with competing or conflicting objectives;
- That members of the governing body, paid staff, and volunteers excuse themselves from decision-making processes in which they have a conflict of interest; and
- That members of the governing body, paid staff, and volunteers report any material gifts or offers of gifts for their personal use, and are prohibited from accepting valuable or otherwise inappropriate gifts, favours, or preferential treatment.

Definitions of what constitutes a “valuable gift” vary considerably from society to society, and hence it may be difficult to produce a single definition applicable to all organisations in all countries. Nevertheless, some general benchmarks may be possible (e.g. proportion of an average monthly salary, a formula that is often used in determining similar threshold values in national legislation).

In-depth definitions of what constitutes conflicts of interest have also proven useful, as have definitions of concepts such as nepotism and favouritism, or good practices such as removing oneself from decisions where one’s impartiality may be compromised. Such *definitions offer a platform for discussion between donors and potential partners with different attitudes so to agree on the rules for conduct, align expectations, and avoid future misunderstandings. As such, it can be seen as a risk management approach.*

Finally, codes of conduct should explicitly note the employees’ obligation to report corruption or any illegal or unethical behaviour.

#### *Transparency standards*

NGOs, as private entities, are not subject to the same information disclosure laws that would apply to donors. It is therefore essential that they voluntarily set high standards of transparency. Typically, NGOs at a minimum publish annual reports that include financial statements, but more proactive information-sharing should be recognised as a good practice. Additional transparency criteria, e.g. publication of the list of donors, could be agreed in consultation with NGOs partners. Many such requirements already exist in national legislation on NGOs.

#### *Human resources management policies*

NGO human resources policies should include the following elements:

- Merit-based recruitment practices, which include the requirement for job descriptions outlining candidate qualifications and responsibilities, advertisement of vacancies, multi-person hiring committees and interview panels with representatives from both the human resources department and relevant operational departments, scoring/ranking criteria, etc.;
- Transparent salary and benefits structures, including e.g. per diem policies;

- Transparent policies and criteria for regular staff appraisal;
- Transparent disciplinary measures and procedures; and,
- Objective complaint mechanisms, including an appeals procedure.

Most smaller, newer, and otherwise less well-established organisations will fail to meet these standards, mostly due to a lack the capacity (and dedicated staff). In such cases, donors and/or leading NGO partners may consider short-term alternatives (e.g. participating in selection or employee grievance committees) while supporting the weaker partner in developing permanent capacities.

#### *Financial management standards*

Many donors will have financial management criteria for NGO partners, and civil society organisations themselves have developed quite extensive standards for effective financial management.<sup>9</sup>

As with many other issues already discussed, the challenge lies not with the well-established NGOs' compliance with the established standards, but rather in the practicality of imposing *minimum standards* for entering into a partnership with lower capacity partners. Donors are advised to review this possibility in dialogue with key partner NGOs who have extensive experience in forming partnerships with weaker local organisations.

As a starting point for discussion, the following minimum requirements are proposed for consideration:

- Existence of basic accounting tools (e.g. books of accounts, general ledger, general journal, cash receipts book, cash disbursements book, bank account records);
- Separation of key functions (e.g. division of approving officer, book keeper, and cash custodian);
- Annual financial statements of income and expenditure; and,
- Exercise of annual audits.

Minimum procurement requirements should be based on:

- Competitive procedures for purchases above a certain threshold; and,
- Other documented procedures below threshold (e.g. best value for money among three possible suppliers).

Whilst in the medium term, support for financial management capacity development for weaker organisations is encouraged, a short-term corruption risk mitigation measure may be more extensive oversight arrangements. *Donors are also advised to consider adopting a comprehensive list of desirable financial management criteria based on the above-noted standards promoted by civil society organisations themselves.*

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<sup>9</sup> See, for instance, standards and support resources developed by organisations like Mango, whose mission is to assist civil society with, *inter alia*, improving its financial management capacities (see *Guide to Financial Management for NGOs*, [www.mango.org.uk/Guide](http://www.mango.org.uk/Guide)). Many NGO associations (e.g. Norwegian NGO Development Network) and self-regulatory bodies (e.g. Philippine Council for NGO Certification) also address the issue. .

*Downward accountability measures*

Whilst this extensive and under-explored topic is beyond the scope of the present research, it is worth noting that the global civil society community has been engaged in a debate for the past decade about promoting *downward accountability*.<sup>10</sup> The discourse extends far beyond corruption risk management; in fact, the primary interest is in improving development outcomes. It identifies as a key problem the fact that NGOs historically have been more accountable to donors (upward accountability) than their beneficiaries (downward accountability).

The notion of downward accountability involves the elaboration and implementation of mechanisms that would increase the role of programme beneficiaries at all levels of operations, from organisational planning to oversight. *In terms of corruption risk management potential, downward accountability measures could extend the range of interested parties (watchdogs) and provide them with the means to react if they detect a problem.*

Many NGOs – particularly those working on service delivery at the community level – already employ practices that promote downward accountability, for instance, the following:

- Open house policies where programme beneficiaries are invited to attend any meeting of the organisation;
- Community town hall meetings/public hearings where the beneficiaries can comment on the project;
- Participatory evaluations of programmes with beneficiaries; or
- Social audits.

A great deal more remains to be done on this front but transforming organisational practices, or instituting sophisticated new ones, is neither simple nor cost free. The potential to increase downward accountability deserves further consideration and support from donors and consultation with NGO partners. *It is recommended that investments be made in assessing these promising practices, including their corruption risk mitigation potential, for possible inclusion in future corruption risk management systems.* At the same time, the effort and costs involved in implementing downward accountability measures should not be overlooked.

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<sup>10</sup> For an introduction to the issue and recommendations for further reading, see U4 Issue paper *Countering NGO corruption: Rethinking the conventional approaches*, March 2011, No 3, available at <http://www.u4.no/document/publication.cfm?3969=countering-ngo-corruption>.

### 3. Implications and dilemmas in moving forward

This report has attempted to promote an understanding of corruption risks in development cooperation through NGOs by highlighting NGO specificities and corruption risks that they commonly encounter, along with the criteria for NGO operations and governance that are commonly viewed as essential benchmarks of corruption prevention capacity.

It has also presented the elements comprising a comprehensive corruption risk management system for development agencies or other institutionally advanced organisations. It has highlighted the equal importance of preventive measures and responses to detected corruption incidents, as well as instruments for their implementation.

This final section reflects on the implications of recommended measures and dilemmas in their implementation, with the aim of pointing the way forward.

#### 3.1 NGO independence

Some donors – and certainly some NGOs – may be quite sensitive to the proposition of this paper that donors may interfere in the operations of independent organisations by imposing conditions or criteria. This is a valid concern in principle, but arguably the issue at hand is one of degree: donors already have requirements for cooperation; certain criteria are already in place. In addition, the majority of NGOs certainly recognise that donors do have a responsibility towards their funders – the tax payers – to protect and maximise the development investments. Further, the majority of measures and standards advocated in this paper – particularly those concerning NGO operations and governance – have been compiled on the basis of standards developed by individual NGOs and civil society groups concerned with NGO governance.

This paper equally advocates consultations with NGO partners, particularly on measures that would impact them directly. In sum, the advocated approach arises from a notion of common purpose and partnership between donor agencies and NGOs, including in developing more robust approaches in tackling corruption in their joint work.

#### 3.2 Transferring vs. sharing of responsibility

Donors typically have limited operational capabilities, including limited capacities to monitor programme implementation. These limitations are often compounded by a distance from field operations where programme activities are taking place. As a result, the primary responsibility for direct monitoring of programme activities is with the main implementing partner. In the present discussion, this would typically be the well-established, high-capacity NGO. Practical considerations inevitably require a certain division of responsibilities for programme implementation, rather than a *transfer* of responsibilities altogether.

In fact, the notion of partnership on which this entire discussion is based suggests that the responsibility for a programme's success (and also failure) should be conceptualised as *shared* between the donor and the NGO partner(s). The concept acquires a practical dimension when considering, for instance, the consequences arising from corruption when it does take place within a project. A position of shared responsibility would suggest that if the principal implementing NGO is unable to recover lost funding (despite applying all reasonable measures) the burden of the financial loss would not fall on the NGO alone. The notion of shared responsibility should be applied not only in reviewing the donor's sanctioning policy, but also to all other measures noted in this paper.

### 3.3 Accepting corruption risks

In the discussion of sanctions in section 2.1.3 above, humanitarian disaster and other emergency contexts were evoked to illustrate the perils of applying so-called “tough”, or rather, simplistic responses.

The fact is that emergency settings pose specific challenges at all levels of operations, including in applying corruption risk management measures. For instance, in such contexts, there is insufficient time to conduct in-depth corruption risk assessments, or insufficient capacity to apply all the desirable mitigation measures. This is precisely why they are considered high corruption risk environments. Nevertheless, the imperative to save human lives and provide relief makes the risk *acceptable*.

Other development policy objectives – beyond the humanitarian imperative – also dictate that certain corruption risks are accepted, even in less dramatic circumstances. The only way that corruption risks can be eliminated altogether is by not engaging in development activities at all. The choice, therefore, is not between accepting and not accepting corruption risks, but rather, how much risk is acceptable and how much investment (in particular, financial investment) should be made in risk mitigation measures, in proportion to the broader development objectives of a given project or programme.

### 3.4 Primacy of development objectives

Development objectives should not only dictate the acceptance of certain (levels of) corruption risks; they should also influence the choice of the mitigation measures applied. By way of example, when confronted with the prospect of working with an NGO with poor financial management capacities, the possible mitigation measures will include, one, increased oversight and two, capacity development. As promoting civil society participation is very likely to be among the objectives of the programme in question, an investment in capacity development of the NGO should be seen as essential, even if increased oversight alone would have been far less costly.

Cynics may be tempted to construe this proposition to imply that corruption should be ignored. This is not the case. On the contrary, reducing corruption in both aid-recipient countries and in aid programmes is in itself a development objective. *The point is to consider the range of available corruption risk responses together with the range of development objectives being pursued, and invest in options that will maximise those objectives.*

### 3.5 Costs of corruption risk management

Finally, the most important challenge for many organisations will be the administrative and/or financial burden inherent in many corruption risk management measures recommended in this paper. Whether the burden is expressed in numbers of staff or the cost of services (e.g. independent audits or evaluations), the measures are at some point expressed in financial terms, and typically as *administrative costs*.

Administrative costs are never a cherished budget line item, and with development aid in particular, individual donors and tax payers alike want to see the bulk of their support to go to programming – feeding the hungry or vaccinating children – rather than to “inefficient bureaucracy.” This is of course an incomplete and superficial view of aid operations, but one that is persistent and difficult to counter in public discourse: this paper would be difficult to reduce to a populist campaign slogan, and the value of funds *not* stolen is not easy to quantify and use as a counterargument.

The lack of figures on the value of corruption prevention measures is a particular challenge for advocates of their more extensive application. Whilst it may be possible to generate some estimates – for instance, by calculating average annual amounts of “leakage” several years before a new

corruption risk management system was implemented compared to several years afterwards – a more effective short-term strategy may be to redefine the terms used, starting by insisting that corruption risk management costs are *not* administrative costs, but rather essential institutional and programme investments.



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Indexing terms:

Non-governmental organisation  
Corruption risk management system  
Risk assessment      NGO  
Risk management      Aid  
Risk analysis      Due dilligence  
Corruption      Zero-tolerance  
Policy

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## Abstract

Non-governmental many organisations (NGOs) are often on the front line of aid delivery, managing a significant proportion of aid funds. The risk of corruption in NGO operations is therefore a significant concern. Yet so far, international donors and the NGOs themselves have not taken a comprehensive approach to managing these corruption risks. Based on an analysis of the systems of four donor agencies and four international NGOs, this report distills good practices for NGO corruption risk management systems.

Important risk assessment considerations include the capacity of the NGO, the type of operation, the operational context, and whether implementation is done by the NGO itself or by a partner NGO. To manage corruption risks, it is therefore recommended to conduct a risk analysis for the specific location, sector and type of programme; strengthen NGOs' internal systems for corruption risk management; have better monitoring and whistle-blowing mechanisms for both NGOs and donors; nuance donors' zero-tolerance policy approach; and establish due diligence measures through NGO selection criteria.

The report also argues that the common classification of corruption risk management tools as "administrative costs" is misguided. Corruption risk management should be promoted as an essential investment in institutional capacity development and therefore a necessary programme cost serving the overall goal of securing positive development outcomes.