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## **BOLIVIAN CUSTOMS REFORM: A CASE STUDY OF CONSOLIDATING DEMOCRATIC INSTITUTIONS**

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## Table of Contents

<b>EXECUTIVE SUMMARY</b>	<b>1</b>
<b>I INTRODUCTION</b>	<b>3</b>
<b>II TAXONOMY AND BACKGROUND OF CORRUPTION IN THE BOLIVIAN CUSTOMS</b>	<b>5</b>
1. The Taxonomy of Corruption in the Customs	5
2. Geographic and Economic Fundamentals	8
3. Modern Political Evolution	9
4. Social Attitudes	11
<b>III THE CUSTOMS REFORM INITIATIVE</b>	<b>14</b>
1. Reform Antecedents	14
2. Progress to Date	15
3. Current Situation and Prospects	25
<b>IV ANALYSIS</b>	<b>32</b>
1. Overview	32
2. Why Now? The Role of International Organizations	33
3. Why Now? The Role of Domestic Political Support	34
4. Why Now? The Role of Media and Public Attitudes	36
5. Feasible Goals for Customs Reform	39
6. Design of the Reform Strategy	39
7. Obstacles to Reform	43
8. Economic Effects of a Successful Reform	45
9. Political Effects of A Successful Reform	47
<b>V LESSONS</b>	<b>51</b>
<b>APPENDICES</b>	
Appendix 1. List of Persons Interviewed	55
Appendix 2. Current Forms of Contraband and Related Corruption	57
<b>BIBLIOGRAPHY</b>	<b>61</b>

## **Boxes**

<b>Box 1. Simplified Tax Regime and the Secondary Zone</b>	<b>6</b>
<b>Box 2. Aerosur Scandal</b>	<b>27</b>
<b>Box 3. RENASA Scandal</b>	<b>28</b>
<b>Box 4. New Customs Courts</b>	<b>29</b>
<b>Box 5. Two Customs Directors Resign Under Media Pressure</b>	<b>35</b>

## **Tables**

<b>Table 1. Reform Strategy</b>	<b>18</b>
<b>Table 2. The New Structure of Customs</b>	<b>21</b>
<b>Table 3. Winners and Losers from the Customs Reform</b>	<b>48</b>

## List of Abbreviations

AN	Aduana Nacional de Bolivia
ADN	Acción Democrática Nacionalista
CA	Customs Administration of Bolivia
CNDA	Cámara Nacional de Despachantes de Aduana
COA	Control Operativo Aduanero
CSAR	Civil Service and Administration Reform Project
CIF	Convenio Interinstitucional de Financiamiento
DS	Decreto Supremo
ESAF	Extended Structural Adjustment Facility
GNF	Gerencia Nacional de Fiscalización
HIPC	Highly Indebted Poor Countries
ICM	International Cargo Manifest
IDB	Inter-American Development Bank
IMF	International Monetary Fund
IRP	Institutional Reform Project
IRS	Bolivian Internal Revenue Service
MIR	Movimiento de la Izquierda Revolucionaria
MNR	Movimiento Nacionalista Revolucionario
MOF	Ministry of Finance of Bolivia
NFR	Nueva Fuerza Republicana
NIP	National Integrity Plan
PNI	Plan Nacional de Integridad
PRGF	Poverty Reduction and Growth Facility
PRI	Programa de Reforma Institucional
PRISMA	Proyecto de Reforma a la Implantación de Sistemas Informáticos Aduaneros
PROMA	Programa de Reforma y Modernización de la Administración Aduanera
PSM	Public Sector Modernization Program
SAFCO	Financial Administration and Control Systems Law
SIDUNEA++	Sistema Aduanero Automatizado version 3
SNA	Servicio Nacional de Aduanas (former name of Aduana Nacional)
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Program
UTISA	Unidad Técnica de Intervención a los Servicios Aduaneros
VMPT	Viceministerio de Política Tributaria
WB	World Bank

### List of Translations

Aduana Nacional	Customs
Comité de Seguimiento	Monitoring Committee
Convenio	refers to the agreement between Customs and the Ministry of Finance setting out collection goals and budget for Customs
Fiscal	Prosecutor
Fiscalía	Prosecutor's Office or Attorney General's Office
Fiscalía del Distrito	District Attorney's Office
Fiscalía General de la República	Attorney General's Office
Gremialistas	merchants in the informal sector dealing largely in smuggled goods
Fiscalización	in the context of the Customs, means bringing the customs operations, or more broadly foreign trade transactions, under monitoring or "control"
Supernumerarios	unofficial ad honorem staff that carried out various customs functions in order to keep a part of the proceeds

## Executive Summary

The corruption endemic in the Bolivian Customs over the past several decades is closely tied to two basic features of the country: the prevalence of contraband trade—encouraged by long, remote borders and the poverty of the mass of the population—and the siphoning of public funds from state agencies for use by the political parties. Corruption has been further supported by social attitudes which, until recently, took a tolerant view of such behavior, and favored interests of particular groups rather than a broader national interest. Corruption principally takes the form of bribes to officials to allow transport vehicles through without documents, with false documents, or with undervalued merchandise, though there are more elaborate forms of fraud as well. This corruption has helped foster large-scale contraband trade, some of it financed by drug money. Rake-offs to political parties were a well-established practice since the 1950s; party-appointed individuals served as unofficial Customs agents, collecting both taxes and bribes.

Since 1982, Bolivia has been ruled by a constitutionally elected executive and legislature, and since that time has undergone a series of economic and political reforms. Until recently, however, nothing has been done to eradicate the institution of using corruption in public agencies as a source of political funding. A refocus of the IMF, World Bank and other international agencies on this problem, and growing public pressures on the administration of President Hugo Banzer (whose five-year term started in August 1997) to take an anti-corruption stance, produced a political consensus, including the main opposition party, to depoliticize and clean up the Customs. This initiative was regarded by reformers as a pilot project for a broader National Integrity Plan, which envisions reform of the entire civil service, focusing on those government agencies especially notorious for party patronage and fund-siphoning.

A decision to reform Customs was by no means to be taken for granted. Despite some antecedent attempts to reform government corruption generally and the Customs in particular, there were strong forces against this change—both those engaged in illegal trade, and party officials benefiting from the funding—and the Customs was still a deeply corrupt institution well into 1999. The decision to undertake serious reform was initially triggered by the insistence of the IMF and World Bank, on whose financial assistance (including possible debt-relief program) the government depends; it was also pushed by a formal private sector eager to become more competitive in regional and global markets; and finally, it was supported by a President under criticism for corrupt associates, eager to make his mark in the anti-corruption area, and backed by a younger, ambitious Vice President who made the National Integrity Plan his special project. The President persuaded his coalition; the Vice President approached the main opposition party, whose reform-minded leader then helped draft the new Customs Law.

The Customs reform, although already in planning stages by 1998, began to take serious hold in mid-1999 with the passing of the Customs Law, and the appointment, in early August, of a new Executive President, Amparo Ballivián, widely recognized for her outstanding qualifications and character, and a non-partisan Customs Board, whose members, all coming from private sector business or law practice, were nominated by the

major parties; the 5 members of the Board, including its Chair, the Director, were not appointed by the President but proposed by a two-thirds majority of the legislature and then chosen by the President. As their terms do not coincide with that of the presidency, the Board and the Director are assured political independence. Ballivián's first acts in office were to remove the informal, party-appointed Customs agents, and to enforce the nepotism provisions of the new law. Progress, although slow, has been made to replace the entire executive and technical ranks of the Customs with carefully-vetted individuals applying for positions through competitive procedures; to install computer systems into the whole range of Customs operations; to strengthen the Customs police, as well as create internal investigation and ethics units, and a controller's department carrying out follow-up checks of enterprise accounts; and to establish an effective public relations function.

Major obstacles to the reform have arisen in part from lack of support from other government agencies. Aside from coordination problems with the Ministry of Finance, which appear to have been largely overcome, there is unreliable support from a still unreformed and corrupt judicial system, which now has the task of prosecuting and convicting those breaking the Customs Law, which criminalizes certain contraband and corruption actions. The eventual creation of the Customs Courts specified in the new Law, as well as special training for selected prosecutors and judges, may lead to improvements in this area. Stronger support of the police, possibly even the army, to deal with armed *contrabandistas*, is also required, but this too requires a more energetic impetus from the political authority. While this support is still there, it has been threatened by the weakness of the government itself, confronted in September/October 2000 with nationwide strikes and road blockades. The impending Presidential election in 2002 will make further reform more difficult to carry out from mid-2001 onwards.

To the extent that the reform has been successful, it shows the importance of top-level political support at the outset, backed by public opinion informed by a free press; of the potentially catalytic role of pressure and support from international donors; of creating a strong and independent leadership for a reforming government agency; and of appointing a high-quality, properly motivated head of the agency. The obstacles mentioned above, however, show the problems of carrying through a pilot project in an otherwise unreformed and corrupt state system. The recent riots show the problems of carrying through a reform, strongly pushed and supported from outside the country, without taking fully into account the likely economic and political consequences. A successful reform will be a first step toward a reformed state and political system; but it may also provoke a powerful counter-reaction from those with a strong stake in the status quo.

# I

## Introduction

Corruption takes many forms, and so does the reform of corrupt activity. For example, to reduce corruption of officials in a government agency, where (for instance) bribes are being taken for prompter completion of a service provided by that agency, there are several alternative or complementary approaches to reform. These include deregulation or liberalization of the transactions associated with bribery, increased penalties for giving and receiving bribes, strengthened internal policing of the agency, and personnel policy reform. Normally, such reforms can be carried out within an agency without too much attention to other parts of the political system: classic examples of such reforms are given by Klitgaard (1988). In some cases, however, corruption within a government agency is so closely intertwined with the workings of the political system that the decision to reform the agency is tantamount to at least a partial reform of the political system itself. Such an instance is the subject of this study of Bolivian customs reform.

This is one of four case studies commissioned by the Global Democracy and Governance Center of the U.S. Agency for International Development. The objective of this project is to create analytical and training materials appropriate for use by policymakers, donor representatives, and activists who are trying to address systematic corruption in developing and transition countries. These case studies thus aim to provide useful models, lessons and analytical tools in support of such efforts.

The ongoing effort to reform the Customs (Aduana Nacional) in Bolivia was chosen as one of these cases for several reasons. First, it seems likely to be one of the modest number of successful anti-corruption initiatives on the South American continent in recent years. Second, as suggested above, it is an especially interesting case because the corruption that existed in the Customs Administration was not simply normal predation by underpaid and poorly managed civil servants seeking to augment their incomes, but rather the systematic theft of the public purse for the purpose of financing political parties. Therefore, to understand how this reform got underway, it is important to examine not only the techniques of reform but also the political bases of the reform decision itself. Finally, Bolivia is a very poor and throughout most of its history has been a very badly governed country, run largely by military dictatorships. The last 18 years, however, have seen the encouraging emergence of a modern democratic system, with major reforms, first, to establish an honest electoral system, and second, to devolve a major degree political power and funding to elected municipal<sup>1</sup> governments where popular participation is encouraged through certain institutional arrangements. As will be described below, increased urbanization and literacy, combined with free media, have led to de facto increases in transparency and accountability in a political system that in some respects is still a carry-over from the days, within living memory of many, when Bolivia

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<sup>1</sup>Since the approval of the Popular Participation Law in April 1994, the term “Municipal” refers to 314 territorial districts into which the entire country has been divided, and which include rural as well as urban areas.

was run by a tiny elite. This struggle between past and future is reflected in both the achievements and remaining obstacles experienced by the Customs reform initiative.

The study is divided into four remaining sections. In Section II, some background information is presented that in the authors' view is crucial for understanding the challenges faced by the Customs reformers: the corrupt state of the Aduana at the outset of the reform in a country where the past still weighs heavily on current political reality, and where economic and geographic circumstances condition every aspect of social and political life. Section III presents the antecedents to reform, the steps that have been taken thus far, and the current juncture of the reform initiative. Section IV then analyzes key aspects of the reform: the question of why such an initiative finally got underway, after so many years of blatant and crippling corruption; a critique of the technical aspects of the reform; and the broader economic and political implications of a successful reform. The final section summarizes the lessons of the Customs reform experience for Bolivia and the global community.

This study is based on both written documents and interviews conducted by the authors in La Paz and Washington. The written documents are listed in the bibliography, and the list of interviewees in Appendix I. Because of the politically sensitive nature of some of the information provided by interviewees, it was agreed that the source of such information (if reported in the study) would be kept anonymous. As a general rule, information based solely on interviews is not reported in the study unless confirmed by more than one interviewee, or unless the authors were convinced of the unimpeachability of their source.

## II

### Taxonomy and Background of Corruption in the Bolivian Customs

Corruption in the Bolivian Customs is closely intertwined with the fundamentals of the economic and political life of the country: the prevalence of contraband trade, which is rooted in geographic and economic givens, and the longstanding use of state agencies for the financing of the political parties. In this section, the major types of corruption in the Bolivian Customs (and closely related features of contraband trade) are described, followed by brief reviews of the geographic and economic background, relevant political evolution over the past half-century, and social attitudes.

#### 1. The Taxonomy of Corruption in the Customs<sup>2</sup>

The prototypical story of corruption in customs is the case of Singapore as described by Klitgaard (1988). In this story, poorly paid civil servants, at both low and high levels, and with at least implicit collusion among themselves, seek to bolster their salaries through some well-known practices:

- **Tipping, or speed money**, to get goods through customs. Goods may be subject to substantial delays, either because the customs is inefficient and/or understaffed, or because delays are created intentionally to elicit bribery.
- Bribes to officials to overlook **undervaluation** or **false descriptions** of merchandise.
- Bribes to allow merchandise to pass through transit points and warehouses without registration, inspection or payment: essentially, bribery to allow **contraband imports**.

While all these practices have been prevalent in Bolivia, it has added at least one of its own practices to this mix. This practice—which flourished until its abolition in 1999 as an early step of the customs reform initiative—consisted of allowing a large number of unofficial customs staff, known as “*supernumerarios*” or “ad honorem” staff, to carry out various customs functions, such as stamping documents, clearing merchandise, and submitting a part of the duties they collected to the government. In a typical transaction, involving severe undervaluation of imports, the prevailing principle was the “*regla de tres*” (rule of three), under which the merchandise was valued at a third of its market cost, but the importer paid two-thirds the actual duties due: in effect, the importer gained one-third the actual duty (by not paying it); one-third was transmitted to the government; and one-third was shared by the customs official and his political party bosses (see below for more on the political dimension of customs corruption).<sup>3</sup> The notebooks of a corrupt Customs Director, General Monje (see Box 5), gave evidence of the party rake-off being passed up through the ranks. At a number of customs posts, *supernumerarios* outnumbered *bona fide* customs officials.

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<sup>2</sup> For a more detailed description of some of these practices, see Appendix II.

<sup>3</sup> Manuel Castilla, IDB expert, has found this practice in several other Latin American countries.

In practice, there are interesting differences in the forms taken by smuggling and related corruption, arising from geographical and economic characteristics of different regions. In the Western highlands, a typical pattern is a La Paz informal merchant who puts together capital, hires a trucker, and crosses the Chilean border, bringing smuggled merchandise back to warehouses in La Paz or Cochabamba. These warehouses are protected from customs inspections as part of the “secondary zone,” that encompasses small tax contributors under the so-called “Simplified Regime” (see Box 1). From these warehouses, smuggled goods are distributed to well-known informal outlets by large networks of family relations and associates. Some merchants, selling electric appliances, computers, bicycles, and other household goods, will even give receipts and warranties. Trucks are not properly registered, drivers usually come from Oruro Department, and may use a network of dirt roads that cross the Chilean border without Customs inspection. Another technique is to import merchandise legally into Chile, receiving an International Cargo Manifest (ICM), but then, after leaving the free zone of Iquique, either disappear over the Bolivian border or are passed through Customs with false documents or without inspection.

### **Box 1. Simplified Tax Regime and the Secondary Zone**

According to Article 4 of the Customs Law, primary zones consist of border customs posts, airports and customs warehouses. This is where the Customs has direct jurisdiction. The rest of the country is a secondary zone, where the Customs does not operate directly, but where it can perform “customs monitoring and control regarding persons, establishments, and wholesale warehouses.”

Under Bolivian tax laws, small contributors may report their income under a special regime, known as the “Simplified Regime.” The intent of the Simplified Regime is to allow small informal retail merchants and tradesmen to pay taxes without filling forms that may appear forbidding to some of them. Until now administrative expenses in collecting this tax outweigh the amounts collected. A second problem is that, in the words of former Finance Minister Herbert Müller, “elephants disguised as ants” manage to evade taxes under the Simplified Regime, meaning that large merchants and tradesmen report ridiculously small incomes through the provision of this Regime.

A third problem, directly related to customs, is that many informal but large merchants bring smuggled goods into wholesale warehouses at major cities, and they want these warehouses to be exempt from customs inspection. By relentless lobbying, these merchants, associated under a “gremialista” union, have forced the government to include a provision in the Regulations to the Customs Law that declares their warehouses off limits to customs inspectors. As this report was being written, the government, at the suggestion of the Customs, was negotiating access to gremialista warehouses by Customs inspectors, at least for wholesale merchants. Retailers, under Article 3 of the Customs Law Regulations, are defined as those who file taxes under the Simplified Regime. Gremialistas managed to become a part of the negotiations to lift the roadblocks that were part of the September 2000 protests, and imposed as a condition that all their warehouses remain off limits to Customs inspection. Thus, smugglers may continue to stock kitchen appliances, computers and computer parts, software and electronic games, all kinds of radios, stereo systems, and TV sets at wholesale warehouses, from where these goods are distributed to nearby retail outlets.

In Cochabamba, another type of fraud, operating with legally imported merchandise with ICMs, is carried out through private customs warehouses, involving undervaluation and false reporting of merchandise leaving the warehouse. White-collar fraud of this sort was exposed in the RENASA case (see Section III.3, Box 3), which is presently under prosecution in the courts. For example, merchandise is registered as having partly left the warehouse, but in fact all has left (thus, duties and other taxes were paid on only the part that had left). This type of fraud, inter alia, is an example of the possibility of changing and falsifying computer records.

One region that still appears far from under control by the central Customs administration is the southeastern part of Santa Cruz Department, where criminal rings operate large-scale smuggling operations on the Brazilian border, in collaboration with local merchants, customs authorities and the police. There is also considerable “ant” smuggling small-scale smuggling on foot over the Brazilian border. Another source of smuggling in this region is alleged to be Santa Cruz airport, where the Customs office has traditionally been paid to allow through containers with luxury imports and computer parts.

Corruption in the customs has not only been carried out by and for civil servants. As described further below (Section II.3), the Customs has served, for many years, as one of the government agencies subject to systematic efforts by high-level party officials to siphon off funds for party use. Even during the democratic period since 1982, there has been an implicit understanding that the government parties divided up various public services that could be used as cash cows for the parties—the Highway Service, the Internal Revenue Service, the Social Development Funds, and, of course, the Customs Service. Within the Customs, different posts were assigned to different local party organizations, with some spreading around among different government parties.

Even those party leaders who were not directly involved in these siphoning operations tended to look the other way because of the direct or indirect economic and political benefits to them. Prior to 1999, occasional lip service to Customs reform seems to have served as a smoke screen while corruption continued. Certainly, there seemed until the past year to be no change in the accepted use of customs positions as political plums awarded by party officials to those who had performed various services for the party (the bigger the service, the bigger the job).

Of course, the details of this political involvement in the Customs tend by their very nature to be undocumented, but accumulated anecdotal evidence, including testimony of interviewees for this study, suggest a number of features of the system. The local party boss—or sometimes a special appointee of the national government—would take charge of overseeing division of the spoils, in particular, appointing (or selling to) another party member the position of director of a customs post, and other officials would gain their jobs through some combination of personal connection and purchase. Before the reforms of 1999, party bosses would also appoint the *supernumerarios*. Informal rules—like the *regla de tres* described earlier—would dictate the division of bribes between officials and

parties. Such rules were presumably also influenced by whether a customs official had bought his post—i.e., already transferred funds to the party—or not. There seems to have been frequent collusion between party officials and the private sector, as well as between Customs officials and private individuals, to rob the public purse. While positions in the Customs tended to be subject to patronage, some staff survived by peddling their support to new parties in power. Seasoned Customs staff are known to have requested open bribes soon after changes in government with the explanation that this was done to satisfy newly appointed supervisors from the new governing parties.

## **2. Geographic and Economic Fundamentals**

One cannot understand the problem of establishing an effective customs service in Bolivia, and the underlying problem of large-scale contraband trade, without considering Bolivia's fundamental geographic situation and economic history.

### *a. Geography.*

Bolivia is a large, land-locked, relatively thinly populated country (8.1 million in 1998).<sup>4</sup> The total length of its borders with its five neighboring countries—Argentina, Brazil, Chile, Paraguay, and Peru—is about 3700 miles, and most of the border country is remote, with little or no population. There are numerous places on the border where it is possible to cross and where there is no Customs post nearby. It is simply far beyond the resources of the Aduana Nacional, police, or even army to patrol anything beyond the main roads, railroads, and airports that represent the principal means of transit into the countries; but beyond this are a large number of minor roads, trails, river crossings, landing strips and salt flats that can be reached by land vehicles, airplanes, or back-packing individuals. It is not surprising, therefore, that contraband has long been an established means of livelihood in Bolivia.

### *b. Economic history.*

Bolivia is one of the poorest countries in the Western Hemisphere, with a per capita income similar to that of India and only 40% that of Peru.<sup>5</sup> Although the population has become predominantly urbanized since the early 1970s, an impoverished and isolated peasantry still represents a large group of the population. Both the urban and rural poor, facing weak demand for labor in manufacturing and mining, have strong incentives to become involved in illegal activities. And low-price (because untaxed) goods face ready markets among all segments of society. Moreover, since the 1970s, the cocaine sector (both production and trade) has been attractive for these groups, as have other forms of contraband smuggling. At the same time, until the Customs Law was passed last year, there were no legal penalties for smuggling, which has historically been considered a legitimate enterprise among the poor, and apparently also among the wealthier participants in this activity. (There is, for instance, a long tradition of “ant” smugglers,

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<sup>4</sup> 424,152 square miles (1,092,581 square kilometers), about twice the size of France (or Texas).

<sup>5</sup> These comparisons are based on the purchasing-power-parity estimates of GDP given in Table 1, pp. 247-275, in World Bank (2000).

who backpack merchandise on foot or beasts of burden, evading Customs supervision by using remote trails and roads.)

Corruption in the old Bolivian customs service was not an isolated phenomenon of government officials adding to their income: it was thus part of the entire network of the informal economy, which some observers believe ranges from 50% to 100% of formally recorded national income. Smuggling has been the main economic activity of border areas since a customs office was established. In more recent years, the drug trade has expanded the volume and value of smuggling, both directly—smuggling out cocaine base—and indirectly, through financing a variety of illegal activities, including the contraband importation of automobiles, appliances, electronic equipment, and other high-value items. Smuggled goods evade not only customs duties but also the 13% value-added tax, and for certain goods excise taxes as well. To take an important example, smuggled cigarettes are freed from a total of 78% taxation (excise, VAT, and transactions taxes combined). Small and not-so-small merchants in the informal sector deal largely in smuggled goods, and are so powerful and recognized a group that they are formally recognized as the association of “*gremialistas*”; and associated with them are the thousands of street vendors that are a characteristic feature of Bolivian cities.

Estimates of the economic importance of contraband trade are hard to come by, but one estimate is that collections on contraband trade might exceed current collections of about \$100 million a year (compared with an overall government budget of some \$1 billion). These estimates suggest how important collections in customs are for the fiscal situation as a whole. It should also be noted that they form a serious impediment to legitimate business, as those dealing in smuggled goods have up till now openly sold their wares, even in large stores. Such openness is not surprising, when it is remembered that until the Customs Law was passed in July 1999, there was no law on the books against contraband trade, and neither a single smuggler nor a single corrupt customs official had ever been prosecuted for his activities.

As noted in sub-section II.4, corruption of government officials has, until quite recently, been considered, if not exactly legitimate, at least a normal state of affairs by the mass of the Bolivian population. An important economic result of this state of affairs is the anemic state of the Bolivian private sector, with the exception of mineral and certain lowland agricultural activities. The attraction of drug-related and contraband activities to both capital and entrepreneurship has drained these key factors of production from the private non-traditional sector, especially manufacturing. It is significant in this context that one of the few robust manufacturing activities is the “informal” small-scale manufacture of counterfeit clothing and leather products, which are either sold illegally (i.e., without domestic taxation ) within the country or smuggled abroad.

### **3. Modern Political Evolution**

As recently as 1952, Bolivia was a quasi-feudal state, run by a small class of landowners and tin mine owners, with an electorate restricted to property-owning males literate in Spanish, perhaps 5% of the population. The representatives of this elite group,

sometimes elected through “liberal democratic” means, were frequently displaced from government by military leaders, who sometimes emerged from the lower strata of society, and usually ruled by brutal means. The resulting political system was unstable: on average there has been a change of government every 2.22 years.<sup>6</sup>

On April 9, 1952, a reformist (but not socialist) party, the *Movimiento Nacionalista Revolucionario* (MNR), in alliance with more left-wing elements, took power on the strength of a popular insurrection that defeated the army. Quickly, the MNR government, led by President Victor Paz Estenssoro, carried out major social, economic and political reforms that included abolition of feudal obligations; a wide-ranging land reform; nationalization of the tin mines; and universal suffrage. The MNR top leadership, while not personally corrupt, sought to create groups of support through titles of land to peasants—not in itself an economically perverse mechanism—but also through patronage exercised through nationalized corporations, cheap foreign exchange at the official exchange rate (which could be resold at large profits in the black market), and a political spoils system operating within certain government agencies, among which was the Customs.

Despite scanty documentation, there is little doubt that since the first MNR Presidency of 1952-56, through subsequent democratic and military regimes, this spoils system has persisted. Since 1982, Bolivian Presidents have been chosen by constitutional means. Under the prevailing Bolivian constitution, if no presidential candidate achieves more than 50% of the vote, the elected Congress chooses among the top 2 candidates.<sup>7</sup> As no such candidate has achieved 50% of the vote since 1980, the president has been chosen in every instance by a process of coalition creation, involving detailed negotiations, and these negotiations have, of course, included the assignment of political plums, such as the Customs and other agencies subject to predation, like the Internal Revenue Service, the Highway Service, and the development funds.

Alleged vote rigging in the 1989 elections led to public pressures for electoral reform. Four partisan members of the national election board, before it was reformed and turned non-partisan in 1991, were given one-year turns as Customs Directors, under the presidency of Jaime Paz Zamora (1989-93).<sup>8</sup> The opposition accused these individuals of rigging 1989 election results in crucial districts. Once in power, MIR party members and their coalition partners supported electoral reform. Due to these reforms, political parties have since been receiving moderate financing from the central government, making them publicly accountable to the non-partisan national election board for use of these funds as well as for use of private campaign contributions.

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<sup>6</sup> During 175 years of Republican history, Bolivia has had 79 different governments. Of these, 41 have been constitutional, 37 de facto, and 1 the product of the first constituent assembly, which elected Simon Bolivar as the first president of Bolivia. To date, 61 different individuals have been presidents of Bolivia. For a complete listing of these governments and their respective dates in office, see de Mesa, Gisbert and de Mesa Gisbert (1999).

<sup>7</sup> The 1967 Constitution was amended in 1994 so that only the top two winners of the popular vote run against each other in Congress (Article 90); before, it was the top three vote-getters.

<sup>8</sup> Still the current leader of the third major Bolivian party, the *Movimiento de la Izquierda Revolucionaria* (MIR).

Despite public financing of parties, there remained various sources of unaccountable funding and patronage: the government agencies referred to earlier, as well as urban municipalities and regional prefectures. In fact, Customs and the other government agencies were probably less important components of the spoils system than were the major state enterprises, until they were privatized (see below). Party hacks and relatives of leading politicians, rather than major power brokers, were awarded positions in the Customs in exchange for generating political support and producing campaign funds, or in payment for political contributions of other sorts. A part of these spoils, of course, went into the private hands of party and government officials at all levels.

Under President Gonzalo Sánchez de Lozada (1993-1997), the current MNR leader, a major program of privatizing state-owned enterprises was carried out, and it is widely believed that support for divesting the government of this major source of patronage was obtained in part through giving control of Customs to MNR officials. Thus, by the time Hugo Banzer Suarez, head of the ADN (Acción Democrática Nacionalista) Party, became President in 1997, the major state enterprises were now out of the reach of the parties, and the importance of Customs for party financing increased, even as the decision was being taken to reform it. Indeed, payment of political and campaign debts depended increasingly on Customs and other unaccountable funding, and the Customs was controlled by close allies of President Banzer, while other coalition members were given pieces of the Customs pie. The embarrassing revelations with regard to the last corrupt Customs Director, General Juan Carlos Monje, in the spring of 1999, explained in further detail in Box 5, show that even while reform plans were being drawn up, and the Customs Law was in the process of being debated by Congress, the Customs administration remained in the hands of a group of the government's political allies who continued established mechanisms of siphoning off funds to feed the spoils system.

#### **4. Social Attitudes**

A recent survey completed through a representative sample of Bolivians<sup>9</sup> asked people to evaluate a list of public services with regard to several variables, including frequency of contact with a given public service by the respondent and degree of corruption registered in that particular service by the respondent in terms of bribe requests and bribe payments. The Customs was identified by most respondents as a highly corrupt, but infrequently approached service.<sup>10</sup> (Customs users in Bolivia are formal importers and exporters as well as travelers who use a passport; most Bolivians do not travel with papers or engage in formal trade across borders.) Most people said they sought public health and public education services, which they perceived as less corrupt than the customs and other services.<sup>11</sup> Frequently contacted public services, which were perceived as highly corrupt

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<sup>9</sup> "Estudio sobre Corrupción, Informe Preliminar," Encuestas y Estudios, conducted January- March, 2000, under contract for National Integrity Plan, Office of the Vice President, La Paz, Bolivia.

<sup>10</sup> *Op.cit.*, Chapter 7, "Attitude and Behavior towards Corruption," p 67. Only 4% said they had contacted the customs, of which 54% said they were asked for a bribe and 48% actually paid the bribe.

<sup>11</sup> *Ibid.*, p. 67, table shows 33% had contacts with education services, 15% were asked for a bribe, and 11% paid the bribe. Table shows 26% had contacts with health services, 12% were asked for a bribe, and 10% paid the bribe.

by survey respondents, included the police and municipal governments.<sup>12</sup> Political parties and politicians, including elective officials, were also perceived as corrupt.<sup>13</sup>

For most survey respondents, corruption was an important or very important problem.<sup>14</sup> The survey showed that people from all walks of life in every region of Bolivia are able to tell right from wrong in the performance of the duties of a public official in a formal sense.<sup>15</sup> Respondents showed a great deal of flexibility in tolerating non-compliance with laws and norms when personal interest was at stake.<sup>16</sup> Many people in Bolivia will admit in private that legal formalities should be ignored when economic conditions and group loyalties argue for an alternative path.

According to the Year 2000 UNDP Human Development Report:

When one speaks about social networks, a first level of analysis is that of family and friendship relations which generate ties that allow a person access to certain opportunities and information, or that materialize into effective support when emergency situations come up.

In Bolivia, these relations are well developed under the shape of informal institutions such as “godchilding” (“padrinazgo”). Often such ties are the base of economic and commercial activities, the opening up of job opportunities or migratory trends. In the political area, these kinds of ties are very often at the center of clientelistic and sinecure producing practices closely linked with elections and to the persistence of institutional mechanisms within the state.<sup>17</sup>

Under this logic the political spoils system is accepted in practice, even as it is verbally condemned. There is an expectation that rotation among political parties in power will eventually place members of one’s group in a position from which they will be able to help other members of the group. When this happens, group members in power are routinely approached for favors with the matter-of-fact expectation that they will place their group loyalties above other duties they may have as public officials.

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<sup>12</sup> Ibid., pp. 67-68.

<sup>13</sup> Ibid., “Top of Mind,” table on p. 55 shows 10% of respondents freely associated the word corruption with political parties. The highest association of the word corruption was with “theft and cheating,” 48%.

<sup>14</sup> Ibid., Chart on p. 56 shows 88% responded that corruption is a very serious problem in Bolivia, 11% said it is more or less serious, and 1% said it is not serious at all. In response to the question How much corruption affects the country, 94% said a lot, 5% a little, and 1% said not at all (p. 57).

<sup>15</sup> 80% responded that laws should be obeyed even if we do not like them (p. 79).

<sup>16</sup> For instance, 21% said they would pay speed money. This low response may reflect how a portion of the remaining 79% of respondents who said they would not pay speed money want to be perceived rather than what many would do in actual situations (p. 81).

<sup>17</sup> UNDP (2000), p. 101.

Small, yet stable groups form as the result of personal acquaintance that bonds people through shared experience, joint undertakings, or personal preference. A high proportion of Bolivians is godfather to more than one child.<sup>18</sup> Informal bonds bridge these social divisions with a strength that outweighs poorly inculcated public duties, carried out by a civil service already undermined by extensive patronage. These bonds of loyalty produced by face-to-face relations across status lines form despite the highly stratified nature of Bolivian society, where people of lower status are discriminated against by those with superior command of Spanish language and customs or higher income. Many people recognize informal relations established by personal acquaintance as more important than relations established by the formal duties of a public official.

Whom you know matters a great deal. The same public official can be rigid with unknown members of the public and highly cooperative and ready to bend rules with people of his or her informal acquaintance. Those who live by corrupt practice are likely to waive public duties and bribes for people they know.

In addition, lack of a strong private sector turns government into the main source of jobs and wealth. This leads in turn to the reinforcement of a parasitical attitude regarding opportunities for rent seeking within the state. Most people will express support for customs and other reforms in theory, but are likely to take advantage of rent seeking opportunities in the Customs, as in other public services, as long as such opportunities are available to them. Few will condemn such practices when given excuses such as personal need, the pull of personal acquaintances, or the falling into socially accepted practices like those sanctioned under the traditional political spoils system.

All reform efforts, starting with the adoption of democracy, depend on a gradual shift of clientelistic and authoritarian habits inherited from the days of de facto regimes into habits of tolerance and public accountability that are required of citizens in a modern democratic state. The role of political, economic and social elites in this effort is critical, both those in government and those in civil society. Often members of these elites have split personalities: as an example, they may obey traffic laws rigorously while in the United States or Europe, but when they return to Bolivia, they ease back into traditional elite behavior, which tends to be paternalistic and discriminatory. It would be a big help if there were a handful of individuals from all regions of Bolivia who, with the prestige of belonging to the elite, set the tone about obeying the rules of the democratic system. In sum, the challenge is educating the role models. Of course, Amparo Ballivián and her new Customs staff are an excellent beginning.

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<sup>18</sup> “The national average is 2.9 godchildren per person.,” *ibid.*, p. 102.

### III

## The Customs Reform Initiative: Antecedents, Progress to Date and Prospects

#### 1. Reform Antecedents

Over the course of the past fifteen years, there have been many attempts in Bolivia at institutional reforms with the broader goal of reducing corruption. To a large extent, the reforms that are currently underway build upon the substantial reforms, including privatization and decentralization initiatives, that have been made by various Bolivian Administrations since 1985. These early reforms sought to eliminate corruption through the establishment of daily public auctions of foreign exchange along with the termination of price, trade, and other controls. The number of taxes was reduced from almost 200 to under a dozen and inspection companies were contracted to verify declared values of imports and exports.<sup>19</sup>

These efforts alone were insufficient to significantly reduce corruption and more focused attempts were subsequently made. Perhaps the most important of these attempts, and a crucial precursor to civil service reform in Bolivia, was the Financial Administration and Control System Law 1178 of July 1990, known as the SAFCO Law, which made all public servants fully accountable for the resources under their control. It implied that public servants could be prosecuted for wrongdoings as well as for errors in judgment. In 1995 it was remarked in a World Bank publication referring to the SAFCO law that, “the law has not prevented the petty corruption of low-level employees, but it is feared by high-level officials, and consequently has the potential to stop the most harmful cases of abuse of public resources.”<sup>20</sup> While this may or may not have been the case, the SAFCO law was certainly seen as a step in the right direction. Unfortunately, at least as recently as 1999, the broader management and planning systems and regulatory framework outlined in the law had yet to be applied.<sup>21</sup>

Two and a half years after the SAFCO Law was promulgated, the Public Prosecution Law was enacted establishing the prosecutorial function as independent of the executive branch of government. Both of these laws were characterized as anticorruption measures and can also be seen as laying the groundwork for more recent reform attempts aimed specifically at the Customs Administration (CA).

A failed reform attempt that took place in the mid-1990s was the Civil Service and Administration Reform (CSAR) Project. Supported by the World Bank and several other donors working with Bolivia, its objective was to fund the salaries of competitively recruited civil servants placed in key positions throughout the central government on a declining basis. Some 260 recruits were hired for positions in several agencies. However, in 1997 the Government requested that the CSAR project be suspended, in order to undertake a more fundamental reform of human resource management within a broader public sector modernization effort.<sup>22</sup>

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<sup>19</sup> Sánchez de Lozada, (1999) in Staphenurst and Kpundeh, (eds.).

<sup>20</sup> Morales, (1995).

<sup>21</sup> World Bank, (1999).

<sup>22</sup> World Bank, (1999).

In 1992 and 1993 there were reform attempts, supported by the IDB and the UNDP, aimed specifically at modernizing the Customs. The primary goals of these programs were to: transfer certain functions to the private sector; simplify operating procedures and reduce the number of physical inspections; reduce the number of customs officials from 1300 to less than 600; and support the development of computer systems.<sup>23</sup> In 1994, as part of the first goal, warehouses were privatized, while Customs remained responsible for the overall supervision of the private firms and would perform its inspections of these firms on private property. The role of customs valuation was also transferred to private firms. Nevertheless, the excessive politicization of the Customs impeded the program's ability to successfully carry out the other components of the program.

In short, up until very recently, previous attempts at reform programs and legislation had been piecemeal, and reforms had not been able to significantly improve the Customs Administration as a whole. As a result, collections remained low and the Customs was still a notoriously corrupt organization. From 1993 to 1997 under the administration of President Gonzalo Sánchez de Lozada there was little progress on customs reform, although this topic was discussed with the IMF and it was formally on the reform agenda. However, other reforms—a privatization program, reform of the pension system, and the devolution of public expenditures—were given higher priority.

None of the previous reform attempts faced up to the fact that the Customs was an important element of the political spoils system. For this reason, previous reform efforts were for the most part formal gestures. As such, previous reform efforts unwittingly helped camouflage continuing political party assault on customs revenues. If previous reform attempts proved anything, it was that until and unless the main political parties agreed in earnest to let go of the Customs, all reform efforts would lack a sound basis and be only nominal.

## **2. Progress to Date**

After August, 1997, the new administration of President Banzer, with the support of the IMF, made institutional reform a priority, customs reform in particular. In 1997 Bolivia launched a first “national dialogue” between the government and opposition leaders, business groups and labor unions with the idea of sounding out opinions and broadening the base of support for government policies and programs. The National Dialogue recommended that the government carry out an effective anti-corruption campaign. The resulting National Integrity Plan is aimed at changing the ‘culture of corruption’ in Bolivia.<sup>24</sup> Vice President Jorge ‘Tuto’ Quiroga has been a key leader of this effort.

Further impetus for fighting corruption in the public sector also came from the Catholic Church as part of the Jubilee 2000 Consultation Forum and more importantly, from the international donor agencies, which made a second National Dialogue conducted during the year 2000 into a requirement for receiving assistance under the IMF-World Bank

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<sup>23</sup> Aduana Nacional, (July 2000).

<sup>24</sup> “Bolivia Paves the Anti-Corruption Road” *The Miami Herald*, September 28, 1998.

program for debt relief for low-income countries.<sup>25</sup> These pressures for reform are discussed in further detail in Section IV.

The IMF began its first technical assistance mission in late 1997. By the middle of 1998 a reform program had been developed—in collaboration with the Fund, World Bank, and other donors—that was known as the Public Sector Modernization Program (PSM). The PSM seeks to improve the effectiveness, efficiency, and transparency of the Bolivian public administration. This larger effort is to be phased in three operations over a ten-year period. The first operation, Phase I, the Institutional Reform Project (IRP), is to extend from 2000 to 2005. The largest of its components (\$59.3 million of a total \$72 million) is on Organizational Reform. This program would reform the basic institutional framework for the public sector and combine these institutional reforms with organizational strengthening in several key agencies. The pilot agencies chosen, the IRS and Customs Service, were to be models for a more widespread civil service and government reform. Customs and IRS were chosen as pilots in large part because the business community and general public often accused them of being rife with corruption, but also because their reform was expected to augment government revenues. Reform of these agencies was thus expected to improve investor confidence, fiscal performance and macroeconomic stability. Many different donors and countries are supporting the PSM program. Customs reform is being financed and managed by the World Bank, IMF, IDB, Japan and Sweden.

In 1998, as part of the IRP, the IMF, with the support of customs experts, began to elaborate a strategy and action and form a team of qualified and motivated professionals to push the reform ahead. The IMF identified as initial conditions a demonstration of political will on the part of the authorities, a project team, and enough resources to assure that the project could be carried out effectively.<sup>26</sup> The reform had begun to take shape and a new director of customs, General Monje, was appointed in mid-1998.

Concurrent with the efforts of the IMF, the private sector became more deeply involved in pushing customs reform ahead, specifically the approval of a new customs law. After President Banzer took office in 1997, the business associations set up three ad hoc committees: an anti-smuggling committee, a follow-up committee, and a committee on customs results. A joint committee and common fund were established by the Chamber of Commerce, Chamber of Industry and the Chamber of Customs Dispatchers with the idea of hiring appropriate technical staff to help draft the law. In October of 1997 the political counterpart to this joint technical committee of the chambers had been established, a National Council on Customs comprised of the Minister of Finance, the Vice Minister of Taxation Policy, a representative of the President and, eventually, the Director of Customs.<sup>27</sup>

By the end of January 1999, by means of *Decreto Supremo 25279*, the Programa de Reforma y Modernización de la Administración Aduanera de Boliviana (PROMA) or, Reform and Modernization Program of the Bolivian Customs Administration, was approved on the basis of the IMF recommendations. PROMA's three main objectives (as

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<sup>25</sup> This is the so-called HIPC (Highly Indebted Poor Countries) Program.

<sup>26</sup> Aduana Nacional (July 2000).

<sup>27</sup> The role of the private sector in promoting reform is discussed at greater length in Section IV.3.

revised in the August 2000 Customs Evaluation Seminar) are: (i) to increase collections; (ii) to facilitate trade, and (iii) to reduce corruption. In January of 1999 the IMF contracted a French expert, Yves Soler, to be the international coordinator of the program and work on the technical reform measures. The international coordinator contracted a team of 11 Bolivian advisors from February to August of 1999, the majority of whom eventually went on to form part of the hierarchy of Customs. This team produced a significant quantity of documents in order to implement the program and obtain international resources. With the eventual passage of a new Customs Law and the credibility that was generated by the commitment of all major political parties to customs reform, the international community committed the necessary resources and the World Bank pledged to help support the personnel component of the reform.

While the political underpinnings of customs reform fell into place, the PROMA agenda continued to be developed and a description of its components can be found in Table 1. The six prongs of the long-term strategy to strengthen the Customs are:

- Strengthening the organization itself by a complete overhaul of the executive and technical/professional levels of the staff;
- Modernizing regulations and procedures, according to the best international standards;
- Strengthening the *fiscalización* (ex-post control) function;
- Computerizing all the customs functions, including a computer-based system of controlling vehicles passing through borders;
- Strengthening the judicial system's ability to deal with criminal cases arising from contravention of the Customs Law, through creation of special judicial tribunals; and
- Creating public relations and communications program.

The short-term action plan, '*Plan de Contingencia*', has been the origin of most of the reforms that have been accomplished thus far. It has the objectives of repairing the image of the institution, conducting random checks against those suspected of contraband and institutional corruption, and improving collections. It also includes plans to restructure the customs police and increase their budget, remove unauthorized persons from customs posts, establish a plan for rotation of personnel and initiate construction of customs warehouses in Puerto Suárez and Oruro. In practice, the Contingency Plan was not implemented in the way originally conceived and its recommendations were not executed until the passage of the Customs Law. (The intention was that it would be initiated by December 1998 but implementation instead began in September of 1999). This was due to the lack of resources and the limited coordination between customs authorities and program personnel. The lack of finances for the Contingency Plan was eventually resolved through an agreement between the Republic of Bolivia and the UNDP. In these recent reforms the respective roles of the IMF, World Bank, and IDB are as follows: the World Bank plays the leading role in managing and financing the institutional change; the IDB supports specific technical activities (training, evaluation, computerization); and the Fund leads in the "technical aspects" of the reform and overall coordination.

**Table 1. Reform Strategy**

<i>Component Description</i>	<i>Results</i>
<b>Contingency Plan</b>	
<b>Objective:</b> Strengthen the capacity of the National Customs Administration in the short-term.	
<p><b>Control Operativo Aduanero (COA):</b> The role of the COA is to control, prevent and penalize contraband and customs fraud and to execute methods and systems of investigation, inspection and punishment of contraband.</p>	<p>Selected personnel have been trained and equipment has been acquired. Beginning its activities in October of 1999, the COA has completed a variety of very successful operations that have ended with confiscation and conviction resulting in prison sentences.</p>
<p><b>Unidad Técnica de Intervención a los Servicios Aduaneros (UTISA):</b> Essentially a mobile audit unit that carries out surprise audits at suspected customs offices, UTISA implements controls for replacing customs administrators and sub-administrators, in effect correcting irregularities and achieving efficiency in customs operations and procedures, reestablishing suitable collections and ensuring the application of the relevant customs rules and regulations.</p>	<p>Hiring and training of personnel has been accomplished and equipment has been acquired. The unit began its operations in August of 1999. Its successful operations include the replacement of customs officials suspected to be involved in illicit activities. This was determined by the detection of multiple irregularities.</p>
<p><b>Transit System and Support to the Reform:</b> establishes efficient controls over international commerce operating by means of ground transportation.</p>	<p>The computer system proposed is based on the registration of commercial vehicles with a computer chip card containing information on the vehicle and its cargo. Pilots have been tested and the implementation of the cards at a national level was expected to begin soon after. Advisors were hired to carry out the initial stage of selection and training of non-management personnel, and revise their responsibilities. Accomplishments include: a Manual of Communication; a short-term communication strategy; and a monthly Internal bulletin of communication. Support was also given to the process of selecting a firm to carry out the medium and long-term communication strategy.</p>
<p><b>Viceministry of Taxation Policy (VMPT) Responsibilities:</b> To continue the process of transferring areas to the private sector and to complement the tax regulations by modernizing the customs administration.</p>	
<b>PROMA</b>	
<b>Objectives:</b> (a) reduce corruption in the CA; (b) increase collections; (c) facilitate foreign trade	
<p><b>Institutional Organization:</b> 1) <i>Civil Service Reform</i> includes the financing of customs salaries on a declining basis; (2) <i>Analysis and Strategy Advising</i> supports efforts of the CA to improve its institutional management capacity, especially with regard to the framework of administrative procedures of the SAFCO law; and (3) <i>Create an Ethics Office</i> – to provide the CA with an added mechanism to reduce internal corruption</p>	<p>The CA is now a separate, autonomous entity. The National Congress proposed Customs Board members from shortlists of three candidates for each of the five positions. The President and Vice-president of the Board have been selected. The Customs Board is set with positions to be periodically renewed on a staggered basis. Funds have been secured for PROMA. Other accomplishments: (1) (a) ‘Ad honorem’ staff (<i>supernumerarios</i>) have been removed; (b) the list of customs staff that signed affidavits that they were of no relation to the President, VP, senior and deputy staff was published; (c) General Manager and Regional Manger posts have been created as the first step to decentralization; (d) competitive salaries have been fixed in order to attract prestigious professionals. (2) Recruitment for Ethics Office Staff has begun and it was anticipated that the office would begin its activities in August 2000.</p>
<p><b>Regulations:</b> (1) <i>Strengthening the Department of Valuation</i> to provide the CA with sufficient capacity to make customs valuation comply with the framework of</p>	<p>A Regulations Decree of the Customs Law was created. There has been support for a Board of Statutes of the CA. Simplified operating procedures have been introduced. A</p>

<p>Bolivia's agreements with the WTO, the 1999 Customs Law, and its rules. (2) <i>Development of Standard Operating Procedures</i> to support the CA in the development of specific standards relative to the various customs procedures, as well as the formulation and compliance of a policy of concessions to the private sector</p>	<p>document was created to establish the strategy of transition to the WTO valuation system. New procedures were to be applied in September, 2000, as agreed by the Bolivian government.</p>
<p><b>Fiscalización and Controls:</b> <i>Strengthening Methods of Ex Post Controls</i> –to strengthen the CA's capacity to carry out ex post inspections of customs declarations</p>	<p>In the beginning of June, 2000 advisors elaborated the functions and procedures of the National Manager of Fiscalización (GNF). In August of 2000, international consultants with experience in ex post valuation were brought in to support this aspect of the reform.</p>
<p><b>Computerized Systems:</b> The subcomponents are (1) <i>Development of SIDUNEA++</i> (2) <i>Communication System</i> to integrate the computer system and create an internal communication network between the various customs offices (3) <i>Electronic Security System</i> to guarantee reliable sources of electricity for the functioning of SIDUNEA++, especially in the border areas and (4) <i>Computer Equipment</i> to provide customs with the necessary equipment to keep SIDUNEA++ functioning properly.</p>	<p>A set of minimum requirements for the operating system was established and an evaluation of the cost effectiveness and risks of each system was conducted. On the basis of this information, SIDUNEA++ was selected. The Customs Board proceeded to negotiate an agreement with the United Nations Conference for Trade and Development (UNCTAD). Technical training was conducted and the program is in the final stages of acquiring equipment and software. The remaining tasks are: (i) development of prototypes; (ii) testing of the pilots</p>
<p><b>Judicial Management:</b> The subcomponents are: (1) <i>Training</i> judges, public prosecutors and lawyers in customs legislation by means of carrying out workshops, seminars and by observing countries using legislation similar to that of Bolivia (2) <i>System of Monitoring the Process</i> to provide the CA with a mechanism of monitoring the judicial process and (3) <i>Regulation Compendium</i> to provide the CA with an instrument that permits it to elaborate its operating regulations in a manner consistent with national legislation and accounting for information on similar legislation.</p>	<p>The selection of the company in charge of carrying out training was to be finalized in mid August, 2000.</p>
<p><b>Marketing and Institutional Image:</b> to reinforce the image of the CA and of the reform.</p>	<p>After receiving expressions of interest from only five firms in response to a first solicitation of expressions of interest, it was decided that a second notice would be released. After the final selection was made in July 2000, the contracted firm began its activities of restoring the image of the CA.</p>

Source: Aduana Nacional, Programa de Reforma y Modernización de la Aduana Nacional, Informe de Avance, La Paz, 28 de Julio de 2000

In the spring of 1999 after the initial enthusiasm from the approval of PROMA had receded, reform efforts again began to slow down, in large part because of public disturbances that diverted the attention of the government in March and April of that year.<sup>28</sup> The Customs was subject to a series of publicly reported scandals, the worst of which was provided by journalists obtaining a copy of a notebook General Monje, the Customs Director, had left on his desk, which documented the diversion of funds from various Customs posts to officials of the government party (see Box 5). As a result of these revelations, General Monje was forced to resign in April, and public pressure was increased on the government to reform Customs.

The tide turned in the summer of 1999 when a series of crucial measures were taken at last. The first important such measure was the passing of the General Customs Law (Law

<sup>28</sup> David Atkinson, representative of the IDB in Bolivia stated that the reform and modernization of the customs service had hardly advanced. He also claimed that the Bolivian government did not concern itself with the subject of customs, which led to a total paralysis of the reforms. Bolivian Times, Bolivian News Briefs, April 29, 1999

No. 1990) in July of 1999 and along with it the establishment of the Customs Board as the highest authority of the institution. The passage of the law and the appointment of a competent Board through transparent means are considered to be the turning points in this reform.

Up until the time when the bill came into Congress, the government had worked on the law with the private sector. At that point it became clear that the opposition had to be included to ensure the credibility and sustainability of customs reform. In order to lay the groundwork for sustainable reform, Vice President Quiroga made important moves toward building a consensus for reform by discussing the draft Customs Law with the opposition party and succeeded in receiving their support. The creation of the Customs Board was an important step in doing so. Appointments to the Board were to be non-partisan in the performance of their functions, but each appointee was to be nominated by each of the five main political parties with the understanding that each party would nominate people of high integrity and proven professional capacity.<sup>29</sup> The law provides that the Customs Board will be made up of 5 members designated by the President of the Republic on the basis of a short list of 3 candidates for each position presented before the Legislature and elected by a two-thirds majority. The President of the Customs Board (i.e., Director of Customs), like the Board itself, is now elected by Congress instead of being appointed by the President of the Republic. In order to maintain some continuity of the Board, members are rotated so that the term of only one member expires each year. The President of the Customs Board remains in office for five years that overlap with the presidential term: this is to maintain continuity of Customs Board leadership and also to depoliticize the office to the extent possible, i.e., to ensure that reform will continue even after the presidential elections that will occur in 2002. Table 2 describes the new structure of Customs.

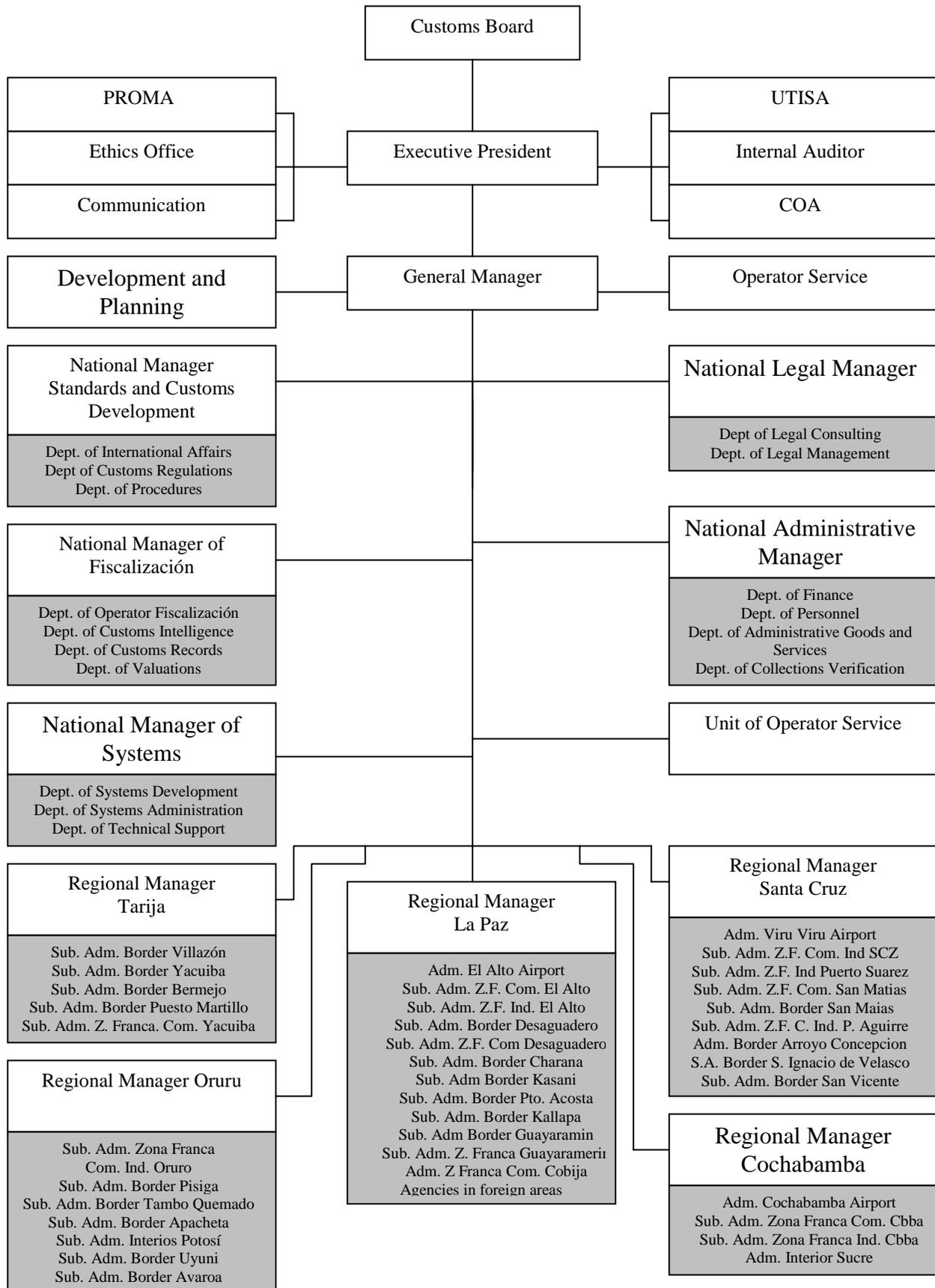
Further innovations of the Customs law were that, for the first time, customs related offenses were criminalized and Customs was given the power to imprison offenders. The law allows for the establishment of special courts for customs purposes. However, for the Special Customs Courts to be created, the Law of the Organization of the Judicial Branch must first be passed. Then, the judicial branch itself will organize these tribunals.

Another result of the law is that the administration of Customs is now centralized, with La Paz having responsibility for the whole administration. Regional offices will have budgetary autonomy but for the first time they are accountable to the national office. Under the previous system, local political interference with the Customs administration escaped possible monitoring by the central government. One Gerencia Nacional de Fiscalización official will be placed in each of the 5 regional administrations in order to establish audits of exports, create an intelligence department and develop records. These officials are in the process of being competitively selected. Also elaborated under the new law was the system of *fiscalización*, under which only 20% of merchandise is physically inspected and the remaining 80% subject to ex post evaluation through random checks of the financial statements of firms.

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<sup>29</sup> The ADN candidate was the Director; the other 4 members were appointed by the 4 largest other parties: MNR, MIR, UCS, and NFR.

**Table 2. The New Structure of Customs**



After Law 1990 was passed in July 1999, a new Director, Amparo Ballivián was installed. Although a member of the ADN, holding a ministerial post under Banzer, her international experience (working at the World Bank), training, and character were perceived by all parties as making her capable of directing the Customs service in an independent, non-political manner. Her conduct in office thus far has made her widely admired by all interviewees, although not necessarily popular with groups adversely affected by the reforms.

At the time Ballivián became Director, the main elements of the project were first, creating an elite, armed anti-smuggling unit of 55-60 known as the Control Operativo Aduanero (COA)—also referred to as Customs Police—which replaced a corrupt unit. There was intended to be a transparent selection process carried out by the UNDP with competitive bidding for the jobs; this process, which had been well underway before mid-1999, was completed in August of 1999 and has been considered a success. Also, by the end of 1999, another elite group on internal affairs, la Unidad Technica Investigativa (UTISA) was created to investigate allegations of corrupt actions. This group was also to have the power to “relieve” staff for up to 3 days and to carry out “control by transposition.” Other accomplishments include the selection of new Directors at the national and regional levels and the selection of software to be used in the computerized system.

Upon becoming Customs Director, Ballivián immediately implemented two important measures to advance the reform and give it an increased level of credibility. The first of these was eliminating the *supernumerarios* from customs posts. Despite considerable resistance in some posts, *supernumerarios* have now been successfully removed from all 41 customs offices. For instance, in the southern border town of Yacuiba, there were 160 *supernumerarios* (compared to 20 officials on the government payroll); when the 160 were dismissed, 30 refused to go. The head of the local police declared himself unable to handle the problem (the local police force was very small). In the end, the crisis was handled by sending in the head of the customs police, who identified the leaders of the resistance and threatened them with convictions on other grounds, such as drug trafficking, unless they and their followers left the office.

The second immediate step taken by Ballivián was the implementation of anti-nepotism rules contained in the new Customs Law. All Customs officials were made to sign sworn affidavits that they were not related to the President, cabinet ministers or members of Congress to the fourth degree or closer. As a result of this, some officials (who were so related) resigned, while the names of those who signed were made public, creating the possibility (which materialized in some instances) that those who signed falsely would be denounced by people who knew their relationship to the designated public officials.

The process of professionalizing the customs staff was further advanced with the identification of unqualified or corrupted employees, firing them and replacing them. The World Bank will supplement the salaries of these replacements, on a declining basis with gradual reduction of such supplements over the five-year period of the first phase of the program, until salaries are entirely financed by the Bolivian government.

In October of 1999, following guidelines of the World Bank, which is financing the human resources module of the reform, a private firm was hired to fill 74 executive positions.<sup>30</sup> The firm recruited and selected new employees through advertisements and a competitive process. 1000 applications were received. 30 of these positions were initially filled through this process, while others were filled through pro-active search by Customs Board members and Customs top management, but these additional candidates were also required to take the same exams as the initial recruits. Subsequently, performance of all 74 has been carefully monitored, and some have already been relieved of their positions, necessitating a further round of advertisement and selection.

A similar process of recruitment, involving the same private firm, was repeated for 380 technical positions in April of 2000. 4000 applications were received for these positions, but there were not a sufficient number of qualified applicants among these, and only 190 of these positions have so far been filled. This process has been slow and not particularly successful. A second phase of recruitment began in September of this year and attempts will be made to correct the problems that arose in the first phase. One of these problems (for both executive and professional/technical positions) was that the headhunter firm in charge of the process was not required by its scope of work to be proactive in the search for candidates and therefore limited the search process to placing advertisements and processing candidates on the basis of application forms, interviews and tests. This was a problem because first, there is very little tradition of applicants submitting applications in response to media ads, and second, efforts were not made to find candidates that were not already interested in a customs position or those that may have had a negative image of customs work. In the second phase of the process to recruit executive positions, a new scope of work will be drafted to attempt to resolve this problem and different firms will be asked to present letters of interest.

One unforeseen result of the reform has been the lack of qualified staff for the once lucrative border posts. This difficulty is in fact a positive sign that the candidates selected are not motivated by expectations of illicit earnings. Hence, the poor school and other infrastructure in border towns—perhaps necessitating leaving families behind, maintaining a separate home, and traveling long distances—will require Customs to offer special incentives to those accepting border positions, as well as establishing procedures for rotation of staff.

Training programs are now underway for both executive and technical personnel. These programs include a management course from the headhunter firm and an in-house course on customs procedures as well as courses on foreign trade and other customs related topics, but more training programs will have to be developed as computerization and procedural reforms are implemented.

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<sup>30</sup> It was pointed out in interviews that the firm hired was a Bolivian firm with no experience in so large an operation; it was chosen over a well-known international firm, with superior experience but much higher costs.

After Directors of the Board were successfully nominated and chosen, they decided to focus their own long-term reform agenda on 4 areas: personnel and human resources; facilitating customs procedures; ex post controls; and the relationship with Chile. The reasoning behind this last area is that 70% of smuggling comes through the Iquique Free Trade Zone and mechanisms must be created jointly with Chilean customs to reduce this problem. Finally, by means of DS 25587, on November 11, 1999, the Aduana Nacional officially replaced the Ministerio de Hacienda as the organization designated as being responsible for the implementation of PROMA, giving the Customs a high degree of autonomy in carrying out the reform.

There has also been some progress in the implementation of the computer system. During the planning stage of the Customs reform, in 1998 and early 1999, a French system had been chosen on the understanding that the French government would extend a credit to Bolivia for purchase of the system; but this initial offer was subsequently withdrawn. Thus, after Ballivián became Director, in August 1999, there was a review of alternative systems available, taking into account available finance. The loan from the IDB for this aspect of the program was signed in May of 2000 and congressional approval is expected by the end of the year. As for the system itself, a team of technical experts evaluated the options and decided upon the UNCTAD system in May of the same year. Its implementation is now underway and computers will be put in all posts. For border towns this means having to install communication systems and in some cases even electricity, which will be another source of delays.

Information systems are expected to provide powerful tools for customs management and control. IT creates the physical separation of the customs user from the customs employee. Once the UNCTAD system is fully operational, customs declarations will be completed on the screen by importers and exporters. The system will compute duties owed and keep a record of the amounts and types of declared merchandise. Thus a major source of corruption, which is the informal agreement (accompanied by bribing) between the customs user and the customs employee to undervalue goods or let shipments pass through unregistered, will be greatly reduced. The problem will shift to customs inspectors who, on the basis of the declaration made on the screen, will carry out spot checks of merchandise.

Another major innovation planned is the container tracking system. Each transport vehicle will be obliged to carry a “smart card” that will record in magnetic form data about its origin, destination, contents, value, and estimated duties. Transporters will be obliged to stop at electronic checkpoints along the way, which will verify the contents of each smart card. The data from the check points will be centralized by the new information system, which will be able to detect inconsistencies, particularly containers that never arrive at the declared customs destination point (“tránsitos no arribados”). While delays have taken place, in part because of discussions with the government about financing by the private sector (which has committed itself in principle to such financing), fear has also been expressed that implementation of the new system will incite strong opposition from truckers. Smart Cards were supposed to be implemented in

December of 1999 but this was pushed back to April 2000 and eventually to the end of the year.

Since Santa Cruz accounted for a large part of customs collections in past years, the 30% drop in that district has offset the remarkable increase in collections at other points, such as those with the Chilean border. The Santa Cruz airport, in particular, was a major source of collections in the past. Though in principle easier to control than distant posts at the Brazilian border, the Santa Cruz airport accounts for a large part in the drop of Santa Cruz customs collections under the new customs administration. The only plausible explanation for the fall in Santa Cruz collections is that corruption has not been totally eliminated there.

Customs President Ballivián fired the Santa Cruz customs manager and sent a UTISA team as temporary managers and auditors until a competition was held for this post. Santa Cruz businessmen and politicians opposed the removal of the former Santa Cruz customs manager, who belongs to the Santa Cruz business community and social elite, claiming that his removal was due to discriminatory hiring practices against lowlanders on the part of national customs management. While there is a strong clientelistic culture in Bolivia as a whole, this phenomenon is probably more openly admitted and practiced in Santa Cruz than in the highlands. Thus, the selection and performance of the next customs manager in Santa Cruz will be an important indicator of the progress of the current customs reform on a particularly difficult front.

Despite such problems, there is a huge nationwide potential for collections to increase, especially when the fact is considered that Customs also collects several other types of taxes. There has been some debate about the targets that have been set for collections and whether they are too low. The general sentiment, legitimate or not, is that only when the computer systems are implemented will the true potential for collections increases be realized.

### **3. Current Situation and Prospects**

One of the chief sources of delay in carrying out the reform during 2000 has been the lack of an IMF-appointed customs advisor. Bolivia is committed to adopting new standards and procedures of customs inspection and valuation. Moreover, since the 1980s, valuation has been carried out by two private firms, whose performance is regarded as having been both costly and of dubious honesty, and one aim of the reform is to bring the valuation operation back within the Customs itself. Although there are a number of competent professionals in the Customs, these reforms require the international expertise that an outside advisor can bring.

The last such advisor, Yves Soler, departed in January 2000, and the IMF took the hard line that they would not bring in a replacement until the government followed through with two commitments: first, to form a Monitoring Committee (*Comité de Seguimiento*), and second, an Agreement (*Convenio*) between the Customs and the Ministry of Finance setting out collection goals and budget of the Customs. There were delays in both these

areas, but particularly the second; at time of writing, the Customs-Ministry Agreement had just been signed. The difficulty arises, in part, from ambiguities surrounding the relationship between the Customs and the Ministry. The Customs, under the Law, is defined as an entity of “autarkic character,” yet under the guidance (“*tuición*”—an oddly chosen word in Spanish as it would be in English) of the Ministry of Finance. These difficulties in language underline the inherent tension of creating an agency independent of the political process, yet necessarily part of the coordinated revenue-collecting and budget-making duties of the politically run central government. The same Article 29 of the Customs Law that describes both the autarkic character of the Customs and the “*tuición*” of the Ministry of Finance also specifies that

The annual operational and investment budget, assigned by the General Treasury of the Nation to the National Customs, will not exceed 10% of collections of import duties. This amount will be retained directly by the National Customs...

In effect, this means that both the estimated import duty collections by Customs and the percentage it is allowed to retain must be agreed to by the Ministry of Finance (of which the Treasury is a part). In principle, this should not be difficult; but difficulties were in fact caused by two circumstances: first, that the Ministry resented its exclusion from the Customs Board, which according to initial plans was to have been chaired by the Minister, and second, the Customs resented that collection targets were agreed in the budget between the Ministry and the IMF (as part of the IMF program) without consulting the Customs about the problems it faced in the initial phase of reforms. That these problems have finally been ironed out was the result of personal intervention by the current Finance Minister, Ronald MacLean,<sup>31</sup> and Customs Director Ballivián. It is now expected that an IMF advisor will soon arrive, and that this should accelerate the introduction of reformed standards and procedures, and the gradual transference of the valuation function from the private firms to the Customs, as well as development of the major training programs that must accompany such reforms.

A major problem area, of great concern to the Customs Board and Director, is that of enforcement. There are two aspects to this: the capacity of the Customs itself, and support from other arms of government. The Customs’ main enforcement instrument is the newly recruited COA (Customs Police), which has shown itself to be of high quality but much too small (at 50-60 staff) to cover the large number of customs posts over Bolivia’s large geographic area. One priority is to double the size of this staff; but as Ms. Ballivián points out, the ratio of enforcement officers to customs officials is very much higher in advanced countries, and even at 100-120 will be woefully inadequate in Bolivia, except for more or less random operations.

The small enforcement capacity of Customs itself underlines the importance of support from other government agencies, to wit: the police, the Attorney General’s Office (or Prosecutor’s Office, *Fiscalía*, ([literally, “public ministry”] in Spanish), and the judiciary,

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<sup>31</sup> Mr. MacLean gained a place in the history of anti-corruption initiatives in Latin America by his initially successful, although unfortunately not long-lived, efforts as Mayor of La Paz in the 1980s.

which is a separate branch of government under the Bolivian constitution.<sup>32</sup> Because a major pillar of the reform is regarded to be the new penalties for contraband and Customs bribery, the competent and honest support of the *Fiscalía* and judiciary are crucial. And the police is sometimes necessary to allow the Customs to carry out its basic functions: for example, to prevent strong-arm tactics by *contrabandistas* and their supporters.

The uneven performance of the judiciary in enforcing the Customs Law has already been illustrated by events over the past few years. The lack of convictions in the case of blatant smuggling by Aerosur Airlines staff—described in Box 2—shows the vulnerability of the judiciary to the twin evils of incompetence and bribe-taking. While the judicial system has so far acted quite energetically in the scandalous RENASA case—see Box 3—it lost a key potential witness who allegedly died of poisoning. In other cases, less spectacularly, the record has been similarly mixed. Another matter of concern is that the Constitutional Court, one of the supreme judicial authorities of the nation, has consistently ruled against the Customs in cases brought by those wishing to strike down particular sections of the Customs Law. And the same Court until now has refused any discussions with the Customs leadership.

### **Box 2. Aerosur Scandal**

The greatest media coverage of customs scandals came after the current reform was underway, and the customs was already under the leadership of its current Executive President, Amparo Ballivián. In late 1999 a passenger airliner of the Bolivian private company Aerosur was caught with a cargo of smuggled goods at the Viru Viru Airport in Santa Cruz. The airport customs unit inspected the plane and denounced the presence of smuggled goods.

The Santa Cruz Viru Viru airport is a primary customs zone under the current law (see Box 1). Under this law, the customs can inspect cargo. Airlines must comply with inspections. In this particular case, undeclared cargo found in the airliner included luxury goods, rubber tires and other items subject to customs and other duties. There is little doubt that the pilot and crew did not expect customs inspection to lead to charges of smuggling, and that similar cargo went through customs without any problems in the past.

The current Customs followed the law and reported the case to the District Attorney. The District Attorney filed charges against the pilot, part of the crew, and the person to whom the cargo was addressed. A local court in Santa Cruz dismissed the case. This dismissal was regarded by Customs Executive President Amparo Ballivián as a damaging blow to customs reform.

For a period of two months, November and December 1999, the media reported almost obsessively on the Aerosur case. Reports centered on the scandalous aspects of the case, but ignored niceties of the legal proceedings. When the case was finally dismissed by the courts, the media denounced judicial corruption in front page headlines. Political implications of this case, if any, were not extensively exposed. The net effect of media coverage was to show that the new customs authorities were actively fighting corruption and would not blink at uncovering the type of operations that airlines apparently allowed to take place in a routine manner before the new

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<sup>32</sup> Indeed, with the exception of the ombudsman, all the agencies of the judicial system (Supreme Court, Constitutional Court, Judicial Council and Attorney General) reside in Sucre—which is formally the national capital, even though all other government agencies are located in La Paz.

customs law made smuggling into a criminal offense. The media, through the Aerosur case, publicized the fact that smuggling was now a criminal offense and helped establish a clear precedent that the risk of customs violations had increased, even for those who felt protected under the previous spoils and political patronage system

Some lawyers believe that Aerosur had a legitimate line of defense, (namely, that bringing “high flying” smugglers to court by the Customs was unprecedented). The Santa Cruz Court accepted this argument. The media were directly responsible for establishing a social sanction on smuggling, and for sending a message to respectable, white-collar smugglers, that they risked exposés similar to that of Aerosur.

### **Box 3. RENASA Scandal**

The latest customs scandal, known as the RENASA case, has political implications. This scandal reached its climax in August 2000. The media gave extensive coverage to the RENASA case, which contained enticing ingredients from a circulation and ratings point of view, such as the alleged poisoning of a key witness who was cooperating with the prosecution.

RENASA is the name of a company that won a contract to run a customs warehouse in Cochabamba, one of Bolivia’s largest cities. The customs office, by virtue of the contract, had offices within the RENASA warehouse and by law kept the authority to inspect goods, estimate their values, determine customs and other duties, and control the entrance and departure of goods at the gates of the warehouse. The customs, under the direction of Ballivián, conducted a quiet investigation of allegations of fraud in RENASA. An audit was conducted, and an extensive ring of RENASA and customs employees was uncovered.

One of the main fraudulent operations of the RENASA ring consisted in forging documentation. Papers showed a fraction of a certain lot of goods paid duties and were consequently cleared to leave the warehouse. Actually 100% of that particular lot of goods was allowed to pass through customs, most of it without paying any duties. Afterwards customs and warehouse employees forged the remaining documentation in order to show that actually 100% of the goods had left and paid duties. In some cases, crates full of junk remained at the customs as unclaimed merchandise, when the goods subject to duties had been taken out of the warehouse without any duties being paid. This and other operations of similar complexity required the active or passive complicity of just about everybody in the RENASA premises, including warehouse and customs employees at all levels. In fact, the criminal ring kept computerized records of their operations in order to keep control of payoffs and shares of the profits.

These records became a part of the case presented by the public prosecutor to a court in Cochabamba. The court ordered the detention of over a dozen persons, who remain in jail to this date. The presentation of evidence of the tampered documentation took eight courtroom days, but the media did not show details of these careful legal proceedings. However, lengthy shots of junk being taken out of crates by inspectors were shown by TV channels on prime time. Cameras lingered over metallic and other types of junk, while indignant reporters caused viewers to feel that the RENASA ring enjoyed protection from high places. The media were also interested in the fact that among those detained were members of families of high social standing and others from respectable middle class backgrounds, all with close connections to the ruling party, ADN. This was definitely a case of white collar crime, though plenty of blue collar associates participated in the operation in auxiliary capacities. For a highly conservative community such as Cochabamba, these revelations were indeed scandalous.

The media denounced a visit by the top regional authorities of ADN, the ruling party, to the RENASA prisoners in the Cochabamba jail. The local ADN chief is also a respected member of Cochabamba business and social circles. When one of the prisoners fell ill and eventually died at a local clinic, the media followed up on charges by his relatives that he had been poisoned because he was cooperating with the prosecution. The unspoken implication in media reports was that the man had been poisoned as a result of the visit of ADN officers. The local clinic refused to confirm these charges, and the coroner's report did not make any mention about poisoning. The man's family, however, managed to obtain a sample from the clinic and sent it for analysis to Chile, where objective labs could not be subjected to undue pressures. The Chilean lab reports, widely publicized by the media, found two brands of rat poison in the sample. The media did not bother to investigate how the rat poison got into those samples, implying that the poison was indeed the cause of death, when the possibility exists, at least in theory, that the poison might have been added to the samples at some point after the man died.

The RENASA case proved that whoever still felt protected by political connections could no longer engage in smuggling and fraud without a real risk of going to jail.

When, and in what way, the special judicial tribunals, or Customs Courts of Sentence, will be established, is still a moot point (see Box 4). This must await the full implementation of the new Criminal Procedures Code, which specifies, *inter alia*, the way in which the judges of all the new Courts of Sentence are to be selected. One potential difficulty is that the judicial reform currently underway—with the backing of donors such as the World Bank and USAID—is moving in the direction of eliminating special tribunals other than the new Courts of Sentence for customs offenses. But since the full implementation of the Criminal Procedures Code is scheduled to take place in at least another year, there is a need to improve the ability of the current penal system to deal with Customs felonies.

#### **Box 4. New Customs Courts**

The 1999 Customs Law aims at increasing the risks of noncompliance with its mandates by regarding a wide variety of such violations as criminal offenses. To implement convictions for such offenses, Article 189 of the Customs Law calls for specialized Sentencing Courts of Customs (“Tribunales Aduaneros de Sentencia”). The law also specifies non-criminal infringements of the Law and procedures to deal with those types of violations.

The inclusion of criminal and non-criminal customs codes in the Customs Law poses potential problems of duplication and contradiction with the prescriptions of two existing generic codes, the Criminal Code and the Criminal Procedures Code. At the same time, a new generic Criminal Procedure Code has been approved in Bolivia to take effect in mid-2001, with emphasis on oral procedure and citizen judges. Until this code comes into effect, all cases must be judged under the existing code. In this transition phase there seems to be room for anticipating features of the new oral code, as well as opportunities for stressing features of the current code before it is phased out. Nevertheless, the new Constitutional Court may be called upon to resolve legal contradictions and duplications, as well as problems of principle, particularly when claims are made against the constitutionality of certain prescriptions. The fact that there is room for interpretation among conflicting codes makes for a defense lawyers' paradise. Although no one questions the integrity of the Constitutional Court and of most Justices of the Supreme Court,

the main factor weakening intended deterrence of the new Customs Law seems to be the lack of an independent, competent judiciary at other than the highest levels. At present the court system is a source of impunity for powerful political figures and wealthy business people. If the new Customs Courts were to be formed of independent and competent judges, this would no longer be the case. According to the new Criminal Code, judges will include both those with legal training (“technical judges”) and citizens. Some legal opinion suggests that the inclusion of citizen judges, especially in a field as complex and technical as customs, may be unconstitutional. Allegations of defense lawyers about matters of unconstitutionality (with regard to this issue and others) will have to be sorted out over time by higher courts.

When Customs detects offenses, it must turn evidence over to the public prosecution and may become a party to a subsequent lawsuit. Since the new Customs Law treats many customs offenses as criminal offenses, the Customs cannot apply effective sanctions by itself. Most cases must go to the courts, and the ability of the courts to deal with them is limited first, because of a lack of judges who are familiar with the intricacies of the customs and the Customs Law and second, because appointments to the court system and the public prosecution in Bolivia are subject to clientelism and appointees automatically become part of the patronage system. Thus, most judges and prosecutors are neither competent to deal with Customs issues nor independent of political and economic pressures.

The Customs Board has established an effective and reliable legal department, with the advice of expert outside counsel, to start and monitor cases before the courts, and to advise the Customs Board. Furthermore, the Judicial Council—the supreme judicial body responsible for screening credentials of appointive judges—has agreed to recommend several candidates for special training as judges in customs matters, and the *Fiscalía* has likewise agreed to appoint several prosecutors for such training. In this way—at least, it is thought, until mid-2001—the Customs will make do with normal judicial processes to enforce the new criminal penalties embodied in the Customs Law.<sup>33</sup>

An even weaker link in the chain is criminal investigation, which in theory is conducted by a special branch of the Police known as the *Policía Técnica Judicial*, which is supposed to work under the direction of a public prosecutor. The training, equipment and professionalism of these investigators leave much to be desired. The Customs must conduct its own investigations and turn results over to the prosecution.

In spite of shortcomings of the justice system, the Customs has substantially increased the risk of sanctions for customs offenders. This effort has been helped by the continuing interest of the media in corruption in general and in customs cases in particular. The Customs Board and President Ballivián keep the media well informed about these matters. More broadly, Customs, for the first time, is concerned about publicity. A recent newspaper insert setting out progress in the Customs reform was a first step. There is no doubt in the mind of the Customs leadership that because of the importance

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<sup>33</sup> For analysis of the problems of meshing the nascent judicial reform with the criminal-penalty features of the Customs Law and its enforcement, see Box 3.

of mobilizing and maintaining public—and thereby political—support for this effort, communications with the public will need to be an effort carried out with both energy and skill.

Another area on which recent progress has been made is setting up an Ethics Office within the Customs. This office will promulgate norms throughout the agency and also get involved in particular cases where ethical breaches are alleged. The delay in setting up this 3-person office has been due to the need to assess fairly the very large number of applications that have been received for these positions. The new Director, an Ethics Specialist, and a lawyer hired face three immediate tasks of the Ethics Office are: 1) drafting a workplan; 2) drafting an ethics code for the customs; and 3) pursuing legal processes initiated by the customs.

The time-horizon for full implementation, in the sense of smooth operation, of the “long-term” strategy is considered to be 5 years by the Customs leadership, although the major elements of that strategy—proper assignment of professional staff, installation of computer system, etc.—should be put in place over the next 6 months. One uncertainty mentioned by some interviewees concerns the fact that the process of getting the system fully operational will take place during a period of national elections, and there is some uncertainty about the impact of a new government on the political support for the reform. Such uncertainty is not surprising, perhaps, in view of the fact that the President’s party has changed from the previous one in every election since 1985. Nevertheless, the main opposition party—MNR—which has a good chance to elect the next President, is headed by a dedicated reformer (Sánchez de Lozada) who strongly backed, indeed helped formulate, the Customs reform. The possibility that the next President is from another party is perhaps somewhat more worrisome. Even though the Director of Customs and the Customs Board are legally protected from arbitrary dismissal by the President, a ruling party inimical to the reform could make life difficult for the Customs leadership and try to undermine the anti-corruption elements of the reform. This is why relentless pressure—and at the time continuing support—from the international organizations supporting the reform will play an important role over the next several years.

## IV Analysis

### 1. Overview

An anti-corruption initiative in an agency like the Customs can be analyzed in terms of changing the incentives faced by principals (political authorities), agents (Customs staff), and clients (those engaged in foreign trade), as well as the relationships among these three groups. The Bolivian customs reform was (consciously or subconsciously) designed to make progress on all these fronts. The stated aims of the reform—increasing collections, facilitating trade, and reducing corruption—concisely summarize the ways in which politicians, the private sector, and officials are expected to change their behavior as a result of the reform. *Increasing collections* is a compressed reference to the macroeconomic need, and international pressure, for a reformed Customs, which politicians must take into account. *Facilitating trade* will, it is hoped, greatly reduce a major incentive for contraband activity, namely, the cost (in either time or “speed money”) of bringing imports or exports through legal channels<sup>34</sup>—although this incentive is also being reinforced by the criminal penalties the new Customs Law now imposes on contraband activity and bribe-taking or –giving. Finally, *reducing corruption* is shorthand for the set of personnel and management reforms intended to change the behavior of Customs officials.

The political decisions and policy instruments that are needed to accomplish these aims are discussed in more detail below. The next three sections examine the political reasons for the decision to carry out the reform—for an agency that had been as politicized as Customs was in Bolivia could certainly not have been reformed without “political will” being exercised at the highest levels of the government and of the main political parties of the government coalition and the opposition, and without broad public support. Answering the question of how it came about that such political will and public support were mobilized in 1997-2000, to reform an agency that had been deeply corrupt, with the apparent acquiescence of the political elite for nearly a half century previously, should have important implications both for the future reform agenda in Bolivia and for other countries.

Parts 5-7 of this section look at what might be called the “technical” aspects of the reform. While some readers might question the relevance of such details to a study of anti-corruption initiatives, the leaders of the reform are convinced that technology plays a crucial role in reducing the discretionary element in official actions in the Customs. The elements of modern personnel management—merit-based hiring and promotion, security of tenure when governments change, adequate pay, defined career paths, etc.—are the basis of any civil service reform. And in the Bolivian case, Customs reform is the pilot project for reform of the entire civil service. Another major aspect is enforcing the criminal penalties that are intended to deter illegal actions by both private traders and Customs officials.

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<sup>34</sup> It is for this reason that the above narrative has paid ample attention to the technical side of the Customs reform, which is absolutely crucial if substantial progress is to be made in facilitating trade.

The final two sections look at the broad, long-run economic and political implications of customs reform. While the economic effects, despite some possible short-run losers, seem clearly positive, the political effects are seen as somewhat problematic.

## **2. Why now? The Role of International Organizations.**

While the possibility of customs reform was raised in the early 1990s by the IDB, and some initial steps toward a new Customs Law were taken under the Presidency of Jaime Paz Zamora (1989-1993), nothing along these lines was undertaken under the Sánchez de Lozada administration (1993-97), when IMF and World Bank programs were stressing other structural problems, such as privatization of state-owned enterprises, the badly needed reform of the pension system, and the devolution of public expenditure. As mentioned earlier, Customs reform was on the IMF and government's agenda—indeed, the September 1997 Article IV Consultation Decision by the IMF Executive Board politely notes the need to “intensify Customs reform,” as if this were an ongoing effort—and had been discussed by IMF missions with the government, but the other reform efforts cited above took precedence.

On September 18, 1998, the IMF Executive Board approved a three-year program for Bolivia under the Extended Structural Adjustment Facility (ESAF), which was re-named in late 1999 the Poverty Reduction and Growth Facility (PRGF). That program specified, as one of its policy conditions, reform of the Customs Administration. It should be noticed that such programs are based on a Policy Framework Paper that is jointly agreed upon by the country authorities and both the IMF and World Bank staffs. Customs reform is not, strictly speaking, a “performance criterion” in the same sense as quantitative targets relating to monetary and fiscal variables, contracting external debt, or introducing new exchange restrictions; but there are a number of “structural benchmarks” related to the customs reform, the progress toward implementation of which must be appraised by the IMF and taken into account before the Fund approves each annual tranche of the agreement.<sup>35</sup>

Behind this formal commitment of the Government of Bolivia to the IMF, and implicitly also the World Bank, lay an important political decision taken in the first months after President Banzer took office in September, 1997, after an initial conversation with the IMF Resident Representative. An IMF technical assistance team, led by Patricio Castro of the Fund's Fiscal Affairs Department, was already beginning its work in late 1997.

The increased emphasis of the IMF and World Bank on Customs reform at this time apparently stemmed from several factors. First, the IMF was concerned with the fiscal situation, and recognized that corruption in both the Customs and the IRS was a major source of fiscal weakness. Second, both the Fund and the Bank were going through a phase of growing attention to “governance” issues, and it was recognized that action would have to be taken on the governance front for Bolivia to be eligible to participate in

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<sup>35</sup> See IMF (1998).

the new HIPC (Highly Indebted Poor Countries) program of debt relief. Finally, it was felt that the previous government had been successful enough with regard to privatization and pension reform to make it possible for the new administration to take up new reform tasks.

While highly placed interviewees acknowledged both the political pressures placed on the Banzer government by corruption scandals (in Customs and elsewhere), and the strong role played by the private sector in pushing for customs reform, there was a consensus that the reform would not have occurred without both pressure and support from the international organizations: Fund conditionality and technical assistance, plus \$30 million of assistance from the World Bank and the IDB.

Interviewees also emphasized the fact that this effort has been carefully coordinated among these three agencies as part of an unprecedented donor coordination effort led by Vice President Quiroga at the start of the Banzer Administration. This coordinated approach has, in effect, strengthened the pressure on the Bolivian government to lend its political support to the reform efforts.

While the international donor initiative was probably a necessary condition for getting a serious anti-corruption program off the ground, the main international organizations involved do not appear to have fully reckoned with the economic and political consequences. Nor did either the government or the international donors prepare any strategy to deal with the fact that the timing of serious Customs reform in mid-1999 coincided with the beginning of an economic slowdown and successful inroads of the drug eradication program in Chapare. Neither the international donors nor the government prepared any measures to counter the combined effect of these three developments on employment and income, and thus were caught by surprise by the massive road blocks and riots in April and September 2000. This was perhaps in part because the international specialists assisting with the Customs reform failed to grasp its importance on the wider Bolivian context.

### **3. Why Now? The Role of Domestic Political Support.**

It is generally agreed that strong international pressure and support finally moved along a reform for which the private sector had been lobbying in vain for a number of years. Nevertheless, without the unambiguous and enthusiastic support of the President, and at his urging, that of the major political parties, it is hard to see how the reform could have taken off. What were the incentives behind this political support? And how was this support mobilized?

First of all, one needs to recall the political obstacles that had traditionally blocked Customs reform—e.g., why the first initiatives of the IDB in the early 1990s failed to take hold. The Customs, as already pointed out, was one of the principal sources of party finance. It was one of the “plums” eagerly sought after by coalition partners; and parties not currently in the government hoped to get their share of the spoils after the next

election. This perhaps explains in part why even the reform-minded Sánchez de Lozada administration (1993-97) did nothing in this area.

Nevertheless, the views of the international agencies, as mentioned earlier, were a significant political factor within the Bolivian political context. Customs reform, all parties and politicians knew, was something that had to be carried out sooner rather than later. One of the earliest incidental factors precipitating customs reform was the introduction of corruption into the political debate. This was the direct result of a report by Transparency International in which Bolivia was shown to be the second most corrupt nation in a group of over 50 countries surveyed by TI. This report was issued during the last year of the Sánchez de Lozada administration, essentially a campaign year.

Once President Banzer took office in August 1997, Vice President Jorge “Tuto” Quiroga Ramírez took energetic initiatives in a number of fields—economic policy, coca eradication efforts, organizing donor coordination, and carrying out a major consultation (“national dialogue”) among economic, social and political elites. The national dialogue revealed a great deal of concern about corruption, and Vice President Quiroga followed up the dialogue by organizing teams of experts, supported by international assistance, to develop the main lines of an anti-corruption strategy. The result was the National Integrity Plan (NIP). The NIP office under the Vice President commissioned surveys that confirmed public concern with corruption, and in particular showed that the Customs was considered an especially corrupt public agency (along with the police).

President Banzer had already agreed to the IMF’s proceeding with a customs reform project. But the planning being undertaken by the IMF and Bolivian experts was not yet a reform, in the absence of a full-fledged political decision. The first Customs Director, Ruben Darío Castedo, was forced to resign by corruption exposés in the media. At that point, the President decided that the IMF efforts needed to be complemented by stronger means with support of the armed forces and appointed a close associate, General Juan Carlos Monje, who soon became immersed in his own customs scandals and was also forced to resign. Both of these scandals are described in detail in Box 5.

### **Box 5. Two Customs Directors Resign Under Media Pressure**

President Banzer’s first two Customs Directors resigned as a direct result of newspaper and TV reports that charged them with corruption.

During the first year of the Banzer administration, the media’s attention was focused on Customs Director Rubén Darío (“Toti”) Castedo, a close political associate of President Banzer, who had occupied a similar position in the customs under Banzer’s earlier dictatorship (1971-78). Castedo was accused of regularizing “transformers,” illegally imported used vehicles from Asia with the steering wheel on the right, then transformed into left hand drives for Bolivia.

As a direct result of media exposés, President Banzer replaced Toti Castedo with retired General Monje, who was instructed to take a tough stand and apply a military hand to fight corruption in the customs. The media kept very close watch on Monje, who was accused of dealings with a secret army society known as the Logia Mariscal de Zepita. The allegations charged Monje with

using this society's members for a variety of illegal customs operations, including shakedowns of smugglers on highways.

General Monje was a methodical officer, who kept written records of transactions, including illegal payments received and made. The report that precipitated General Monje's resignation was the publication in the main Catholic newspaper, "Presencia," of a photograph of General Monje's notebooks, where illegal payments received and made were meticulously recorded. The President was suddenly involved in another, more damaging customs scandal, and was obliged to ask General Monje to resign.

After resignations under media fire of his first two Customs appointees, media pressure on the President to clean up the Customs became unrelenting. There was a barrage of news reports, editorials, fierce cartoons, political analysis and commentary on the alleged involvement of the President's close allies and family members in customs corruption.

At this point, the private sector took up Customs reform with great determination, as described in Section III.2 above. The umbrella business organization, the National Confederation of Private Entrepreneurs, took up the fight and added its considerable lobbying powers to the effort. The chamber of private customs dispatchers came out publicly in favor of this effort, despite being viewed with some suspicion by other private businessmen as having been implicated in customs corruption. Nevertheless, the coalition persisted and received good coverage by the press. They formed bill-drafting committees that included customs experts, and led the government in the process of drafting a new customs law. The Vice President intervened to facilitate the drafting of the law and its legislative approval.

#### **4. Why Now? The Role of Media and Public Attitudes.**

Bolivia has enjoyed full and uninterrupted freedom of expression since October 1982. Freedom of opinion and freedom of the press have allowed for the development of increasingly sophisticated and competitive media. The impact of the media has grown steadily with the rising literacy of the population and rapid increase in television ownership over the past few decades.<sup>36</sup> With greater freedom and impact, the media have contributed in a crucial way to the democratic transition, providing the necessary public forum for election campaigns and intense public scrutiny of elected governments.

The preceding section gives instances where corrupt Customs Directors were forced out through media pressure. In fact, customs reform has been a major theme in the media under the administration of President Banzer. Underlying this phenomenon were two recent developments: a report issued by Transparency International in 1997, and the emergence of media conglomerates in 1998, resulting in sharp competition for circulation and ratings.

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<sup>36</sup> Adult literacy has risen from under 50% 40 years ago to 75% in 1998 (90% for males). Television ownership was reported at 116 per 1000 population in 1998, that of radios, 675/1000. This audience is also progressively more urbanized—62% in 1999, compared with 40% in 1965. (Figures from various World Development Reports of the World Bank).

The 1997 Transparency International report placed Bolivia as the second most corrupt country in a sample of about 50 nations.<sup>37</sup> This report came out during the last year of the administration of President Sánchez de Lozada (1993-97). On the basis of this report, the media placed corruption at the center of the political agenda. Political parties took up corruption as a dominant campaign issue during the 1997 election. As late as October, 2000, the 1997 TI report was still a subject of media commentary.

Almost coincident with the 1997 TI report, during the first year of President Banzer's administration, increased competition among the media led to the emergence of two major conglomerates. A number of established newspapers and TV stations in the main cities of Bolivia merged or associated. These mergers in turn led to a significant increase in commercial competition. Each chain was composed of a central newspaper and TV station, plus a number of associated newspapers in the major cities of Bolivia.<sup>38</sup>

Competing media conglomerates were aware that according to surveys the public considered corruption to be an important issue. They soon realized the public loved to see rolling heads, the higher the better. Not surprisingly, competition extended to all fields, from glossy magazines on social life to yellow journalism. Each conglomerate founded its own scandal sheet, complete with nudity and violence (e.g., *Extra* and *Gente*).

For Bolivians, used to regarding the media as serious and respectable, though often highly ideological, the onset of media commercialism was a novelty. One beneficial effect of this development was that the quality of investigative reporting increased, as did the variety and quality of editorial commentary and analysis. At the same time the prestige and credibility of media, which was very high before this development, declined. Bolivian media, given the lack of credibility of the courts and the prosecution, are becoming used to acting in a judicial capacity. They accuse, they judge and they condemn with lightning speed. The accused has little opportunity for defense. What counts are big headlines and scandalous pieces of alleged evidence.

At the same time, the media played a critical role in the formation of a coalition of private sector actors interested in customs reform. The media gave coverage to officers of the Chambers of Commerce and Industry, of Exporters, of Customs Dispatchers and their umbrella organization, the Bolivian Confederation of Business Entrepreneurs. The media, as private firms, belonged to the latter as well. As mentioned earlier, these private sector associations played a helpful—some believe an important—role in moving along reform, indeed helping to draft the Customs Law, and suggesting names for members of the Customs Board.

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<sup>37</sup> An analysis of the TI ratings by an independent observer reveals that two-thirds of the weight of their index is based on the opinions of 7 "expert" individuals; the other third is based on a survey of 50 entrepreneurs. (George Gray Molina in "Leviatán," supplement to *La Prensa*, October 1, 2000).

<sup>38</sup> One group is composed of the newspapers *La Razón*, *Opinión*, *El Nuevo Día*, *Extra* and the ATB TV station. The other is composed of the newspapers *La Prensa*, *Los Tiempos*, *Correo del Sur*, *El Deber*, *Gente* and the P.A.T. TV station. The exact nature of the association of a given member varies, but for purposes of competition all the associates act together and support each other in different markets with different publics.

After merging into large conglomerates the media have acquired an overwhelming amount of power. Indeed, some academic students believe that the media business is not profitable, particularly not newspapers. They claim that the media are used by other business interests to gain influence in government. At the same time, the media seem to want a political role for themselves that is independent of parties, and it may not be surprising to find these conglomerates in the future putting up candidates of their own.

Be that as it may, as the Aerosur and RENASA cases show (see Boxes 2 and 3, Section III.3), as well as the forced resignations of Customs Directors Castedo and Monje (see Box 5, Section IV.2), the media have had a leading role in customs reform before and after the approval of the 1999 Customs Law and the appointment of the new Customs Board. Because one of the two largest conglomerates favors the opposition and the other is on the outs with the ADN party, which it once supported, the Banzer administration has been unusually vulnerable to media pressures, e.g., when political associates or relatives of the President were involved in corruption scandals (Customs-related or otherwise).

Despite the importance of publication of the TI ratings in 1997, there is no local TI chapter, and civil society has played a minor role in the Customs reform per se, although some prominent entities in civil society, especially the Roman Catholic Church, have played a much more important role in organizing and participating in the National Dialogues, and the latter, in turn, have influenced public opinion in the direction of regarding corruption as an evil to be attacked through reforms. The local NGO that hopes to become the Bolivian chapter of TI is *Equidad*, a small group of prestigious professionals who wish to distance themselves from active political participation. In 1999, *Equidad* organized two workshops on corruption, one with civil society and a second with political parties: the first workshop was well-attended, the second much less so. *Equidad* is also designing an integrity training pilot program for high schools and carries out ongoing analysis of developments regarding corruption.

Despite the media role described above, and although the Catholic Church has consistently spoken out against corruption as a matter of principle, Bolivia has lacked a sector of society dedicated in a systematic and organized way to public issues and to promoting the general good. There are many voluntary associations in Bolivia, but most of these are oriented to their own particular purposes. There are no independent think tanks of any consequence. One exception to this weak civil society, and of growing importance, are the grassroots organizations called “OTBs,” or Organizaciones Territoriales de Base,” registered under the 1994 Popular Participation Laws which devolved many governmental functions to 314 municipalities. The latter are governed by elected officials and the OTBs—now 15,000 in number—are supposed to select a committee in each municipality to monitor municipal government. OTBs include various types of labor unions and agrarian associations. In time, they may constitute a major base of civil society favoring anti-corruption activities.

## **5. Feasible Goals for Customs Reform.**

The three goals set out for the reform—increasing collections, facilitating trade, reducing corruption—are eminently sensible and are couched in such a way that they would be satisfied even with modest gains. The precise detailing of these goals raises questions of costs and benefits: what resources would have to be invested in order to greatly reduce contraband trade, and thereby, for instance, raise by 30% or 40% the amount of foreign trade passing through legal channels? Or is it sufficient to invest simply in the resources required to discourage underinvoicing of already legally channeled trade? What resources would be required to defeat the large businesses of smuggling in used cars, or foreign cigarettes, or household appliances? Should the Customs stick to controlling trade that passes through the Customs posts, or should it reach out to other channels of commerce? Can corruption be eliminated throughout the country, or should one stick to those regions that are more completely within the direct control of the central government? Will political interference, at either the central or regional/local level, compromise the goal of an entirely clean Customs administration?

These questions are difficult to address, and will not be answered within the scope of the present study. Complete elimination of contraband is not possible. But raising the costs to *contrabandistas*, through a variety of control and judicial instruments, is. To what extent streamlining Customs operations, and speeding up the passage of exports and imports, will encourage legal trade is not clear: the tax system creates another, fairly substantial margin between legal and illegal foreign trade (also domestic trade). To what extent the human resources policy will entirely clean out the formerly corrupt elements in the Customs is still not clear. (See Section III.2 on the management of Customs in Santa Cruz.) The goals should be high; but the results should not be judged in comparison with perfection. In particular, the collections goals should not be unilaterally determined by the Ministry of Finance, as was the case in the last budget exercise, but carefully discussed with the Customs, and fixed with due regard to estimated imports, reduced import tariffs, and the delays and obstacles in getting the reform fully underway, including those obstacles that are the responsibility of other branches of the government (see Section IV.7).

## **6. Design of the Reform Strategy: How Does it Compare to Reform Models?**

It may be helpful to evaluate the Bolivian Customs reform strategy in light of existing models of anti-corruption reforms. Since it is too early to be able to measure the degree of success of this reform, comparing it to models of successful reform could give some indication of its likely success. The comparison here will be to the well-known model set out by Klitgaard (1988), who develops a simple principal-agent-client model from which he derives, “a framework for policy analysis, a heuristic outline of anticorruption measures.”<sup>39</sup>

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<sup>39</sup> This entire section relies heavily on Klitgaard chapter 3 entitled, “Policy Measures.”

Klitgaard's framework of policy measures available to the principal, in this case Amparo Ballivián and the Customs Board, is grouped into five clusters: selecting agents, changing rewards and penalties, gathering information, restructuring the principal-agent-client relationship, and changing attitudes about corruption. What follows is a comparison of each of these clusters to the actual strategy of customs reform in Bolivia.

*a. Selecting Agents*

The first of these clusters, selecting agents for honesty and capability, includes measures such as screening potential employees for dishonesty by reviewing their past records or issuing honesty tests. In addition, this can include using outside guarantees of honesty. Presumably the first aspect of this measure has or is being accomplished in the Bolivian case through the elaborate screening process of potential employees at both high and lower levels. There is a committee of three for choosing applicants for each post—with one of the three not from the unit where that post is located—and decisions are required to be unanimous. The difficulties in finding a sufficient number of qualified applicants may be evidence of the rigor of this screening process. Also, the fact that this task has been contracted out to a private firm also contributes to eliminating corruption in the hiring process; this will be even truer in the second phase of the hiring process when the firm's success in nominating employees will be tied more closely to its profits.

There is widespread support and even admiration of non-political procedures for selecting customs personnel. For instance, the opposition by the Santa Cruz business elite to the replacement of the local customs manager (see Section III.2) was highly vocal, but it was isolated, denounced by respected commentators, and received no support from any other region or sector of the country. Customs President Amparo Ballivián managed to keep public opinion on her side on this issue.

*b. Changing Rewards and Penalties*

The second cluster, changing the rewards and penalties facing agents and clients, has two components according to Klitgaard. The first of these is shifting rewards. This includes raising salaries to reduce the need of officials to supplement their income, rewarding specific actions, using contingent contracts to reward agents according to their level of success, and using nonmonetary rewards. In the Bolivian context, salaries have been raised but because they are being supplemented by donor agencies on a declining basis, there is still some degree of insecurity that the Customs will be able to maintain these salaries when the donor money is gone. There is not yet an established rewards system for employees, but there is the stipulation that Customs would be able to hold on to 10% of its import duty collections gives the institution the means to give adequate pay to its staff, a counter-incentive to corruption, especially when combined with merit-based (rather than patronage-based) tenure. Presumably this amount would also be used to create further incentives for agents to succeed and to accept relatively undesirable postings. Because of disputes with the MOF over the meaning of this stipulation, there is some danger that these incentives might be reduced.

The second component of this cluster is penalizing corrupt behavior. This includes raising the general level of penalties, increasing the principal's authority to punish,

making penalties proportionate to the crime, and using non-formal penalties. Certainly, the criminalization of customs-related offenses goes a long way toward achieving these goals. The problem with this is that the authority of customs to punish only extends as far as the efficiency of the judicial sector will let it. As for nonformal penalties, the Bolivian press is a good tool for this last method of punishment as it is relatively outspoken and is taken quite seriously as in, for example, the General Monje debacle.

The strategy of changing rewards and penalties is aimed at increasing the agent's incentive to be productive and reducing incentives to engage in illicit behavior. We may consider the reluctance of potential employees to go to posts at the border to be evidence that this second aspect is working, i.e., the risks of getting caught (and the unpleasantness of living in the border towns), now outweigh the potential benefits of engaging in illicit behavior at those posts. More fundamentally, it is apparent that working for the Bolivian Customs no longer carries the social stigma it once did. The public announcements for Customs positions are drawing significant numbers of well-qualified and honest applicants.

*c. Gathering Information*

A more detailed description of this third cluster is the gathering and analysis of information in order to increase the chances that corruption will be detected. Klitgaard divides this cluster into 5 components. The first of these is improving auditing and management information systems. The Bolivian Customs is trying to accomplish this by making efforts toward the implementation of a computerized system as well as the 'smart-cards' system to track ground transit. The strengthening of the department for *fiscalización* (control and monitoring), which will examine enterprise records on a random basis, will be another measure along these lines. The second component is strengthening 'information agents.' This is being fulfilled by the UTISA and COA units, which conduct inspections that so far have been reported to be quite successful, although their efforts and size need to be expanded. The third recommended policy under this area is using information provided by third parties. As mentioned earlier, the media has played an important role in this arena, and while it helps mold public opinion, it is also responding to a public strongly averse to corruption. Fourth is using information by clients and the public: in the Bolivian case, the use of public opinion surveys (which reported public perceptions of corruption in Customs), and the high level of participation of the private sector throughout the reform program. The last component of this cluster is shifting the burden of proof to the agent so that the potentially corrupt have to demonstrate their innocence. To some extent this has been the case in the Bolivian reform in that pre-reform employees were dismissed for having been suspected of illicit activities. However, Article 16 of the Bolivian Constitution presumes the innocence of the accused until proven guilty, and this judicial principle, also a keystone of Anglo-Saxon jurisprudence, should stand as a safeguard against an excessive tendency to presume guilt in these cases.

*d. Restructuring the Principal-Agent-Client Relationship*

The idea behind this cluster of policies is that restructuring these relationships can remove the corruption-inducing combination of monopoly power plus discretion plus

little accountability. There are several policy options that fall under this heading. The first is inducing competition in the provision of service. The Bolivian privatization of warehouses and valuation has apparently not prevented the emergence of corruption in these activities. However, the use of private firms to assist in searching for new staff has not encountered problems of this sort, although the Customs has in other respects not been entirely satisfied with the firm and may contract a different firm to carry out the second phase of hiring. The danger of privatization is that the private monopoly will replace the public one. To some extent this was found to be the case in the first phase of human resources reform, i.e., the firm did not have a lot of incentives to actively pursue high-quality applicants because their reimbursement was not tied closely enough to the quality of their shortlists for the positions.

Another very important example of restructuring a principal-agent relationship is depoliticizing the link between a new Presidential Administration and the appointment of the Customs Director and Customs Board members, as well as making the appointment of Customs officials non-political (they now have tenure beyond the new presidential administration). In this case, the position of principal has shifted from the President of Bolivia to the Congress, and the agents are the Customs Board and Director.

The second policy option is to reduce the discretion of agents. This has been done in Bolivia to the extent that procedures have been simplified and efforts have been made to make sure that the private sector is aware of these procedures. Computerizing the Customs documentation system and installing 'smart-cards' is one approach to making Customs more dependent on automatic, machine recording of data, and less dependent on human judgment. While manipulation of warehouse computer data in the RENASA scandal (see Section III.3) suggests that computers only ensure honesty to the extent that those in charge of the computers are also honest, well-designed computer programs will allow investigators to trace most instances of such manipulation. Another option for separating Customs agent and client is moving toward a pre-shipment rather than post-shipment valuation system, another aim of the Bolivian reform.

An additional policy option being considered at this stage of the reform is rotation of agents among posts. This could reduce potential corruption by limiting the time in which corrupt agent-client relationships are based. (This method of rotation may also alleviate Customs' problem of finding people that are willing to take border posts).

The last policy category under this cluster is organizing client groups to make them less susceptible to corruption and creating an anticorruption lobbying force and citizen groups that will be able to promote and sustain the reform. In the Bolivian case, the National Dialogues and the National Integrity Plan are good examples of these; and reform initiatives have also benefited from lobbying by the Roman Catholic Church. The incorporation of opposition political parties into the reform, particularly into the structure of the Customs Board, is a major success in this area and will, it is hoped, help to sustain the reform beyond the next election.

### *e. Changing Attitudes About Corruption*

The rationale behind this cluster of policy options is raising the moral costs of corruption. The first category of measures is using training programs and publicity campaigns about the existence and costs of corruption. There have indeed been anti-corruption publicity campaigns in Bolivia and, to this end, the NIP, as mentioned earlier, is a major factor. Having a personal example—such as ‘the unimpeachable integrity of the principal’—is invaluable. In this respect, Amparo Ballivián’s well-earned reputation for integrity and determination is one of the major reasons why the Customs reform may be successful.

A second method under this category is promulgating a code of ethics. An Ethics Office in Customs is being created and would presumably produce such a document. The last method is changing the organizational culture. For a long time the title of *aduanero*, or customs official, has been a pejorative one; the component of the reform that seeks to improve the image of Customs will be a difficult task. Efforts at boosting morale will be equally difficult since the entire structure is changing, leaving many people who had been a part of Customs before the reforms particularly dissatisfied.

This comparison is not meant to be a comprehensive evaluation of the Bolivian Customs reform strategy, but merely in Klitgaard’s paraphrased words, a framework helpful for understanding why and how efforts succeed or not. That said, it appears that the strategy for reform of the Bolivian Customs Administration has been well designed and satisfies most of the suggested guidelines for reform.

## **7. Obstacles to Reform.**

The recent progress report issued by the Customs lists the “principal obstacles encountered” by the reform.<sup>40</sup>

- Inadequacy of human resources recruited through public announcements and competitive salaries;
- Delay in replacing the international coordinator of the reform, and therefore obtaining adequate advice on customs matters (i.e., standards and procedures);
- Lack of support from the prosecutorial and judicial agencies in enforcing the Customs Law;
- Delays in acquiring equipment and software for the new transit system, due to disagreement between Customs and the National Customs Dispatchers Association, which had agreed to finance these costs;
- Delay in formation of the Monitoring Committee for the reform program;
- Deficient mechanisms of coordination between the Customs and the Ministry of Finance and other ministries;
- Inconsistency of fiscal policies with the reform;<sup>41</sup>
- “Bad faith” shown by foreign traders in undervaluing their merchandise.

<sup>40</sup> Section VI, “Principales Obstáculos Encontrados,” in *Aduana Nacional* (July, 2000). p. 27.

<sup>41</sup> This refers to an amnesty for owners of illegally imported vehicles, allowing the latter to be registered legally with only minor penalty, even though some of these vehicles were imported while the Customs Law was already in effect.

It is interesting that while some of these “obstacles” are essentially technical delays or problems, which one could expect to be overcome in due course, most of them refer directly or indirectly to interactions between the Customs reform and still unreformed parts of the Bolivian polity and society—e.g., the corrupt judiciary, and the vast informal economy. The more ominous factors mentioned are the failure for the Customs reform to be backed up by the judicial system (see Section III.3), and the difficulty of coordination with the Ministry of Finance. These issues raise the basic question of the sustainability of reform in a single agency within the broader context of an unreformed political system, civil service, and judiciary. This is, of course, an inherent problem of “pilot projects,” when the project cannot be carried out in complete isolation from the rest of the economic and political system. In the case of Customs, some efforts were made to ensure such isolation: e.g., the non-coincidence of the Customs Board members’ terms, especially the Customs Director’s term, with that of the President. But the actual implementation of the reform does require cooperation from other branches of the government.

The answer, perhaps, is for the leadership of the reforming agency, as well as the political leadership (which is presumably supporting the reform), to focus on specific changes in a few units of the government that play key roles in supporting the reforming agency. In the case of Customs, this means the Attorney General’s office (*Fiscalía*), judiciary, police, and the Ministry of Finance. In the case of the latter, the problem is not corruption but coordination of policy between two agencies with different agendas and responsibilities.

The interactions with the judicial system and police have already been discussed in Section III.3. In these cases, the problem is unreformed, bribe-vulnerable officials and agencies being depended upon to support the criminal penalties called for in the Customs Law. In retrospect, some interviewees with key roles in the reform process, and no involvement in drafting the Customs Law, suggested that with the benefit of hindsight it might have been preferable to substitute administrative sanctions, which could have been enforced by Customs itself, for the criminal penalties whose enforcement depends on the police, *Fiscalía*, and judiciary. In favor of this view are the greater speed and certainty of administrative sanctions. The counterargument is that criminal sanctions may be stronger.<sup>42</sup> But at this stage amending the Customs Law is not an alternative being considered.

The current problem, as explained in Section III.3 and illustrated by the cases described in Boxes 2 and 3, is that the reform processes in Customs and the judicial system are unsynchronized both with regard to timing and targeted changes in the justice system.<sup>43</sup>

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<sup>42</sup> The current law provides for a number of administrative sanctions, in view of which the Customs has started a series of training and dissemination seminars for customs clients and agents on the application of administrative sanctions.

<sup>43</sup> Due to resistance to reforms from the Judicial Council, the World Bank during the year 2000 decided to postpone a second phase of assistance to the Bolivian justice system. The Bolivian justice system has proved to be a tougher challenge to reform than the Customs. So far it has resisted over a decade of donor-funded reforms as well as a major constitutional amendment in 1994 that aimed squarely at reducing the

This must frankly be seen as a strategic error, for which the proposed remedies, such as special training for a small number of selected prosecutors and judges, can be realistically hoped to give only partial relief for the time being. The appointment of special Customs Courts, which awaits enactment of the new Criminal Procedure Code, may help, but how this works out in practice remains to be seen. Another possible remedy, suggested by key interviewees, is much stronger support from the customs police, perhaps strengthened with the same kind of assistance from the United States government as has been received by the special police force known as FELCN in its drug eradication efforts, though at a much lower level of effort.

## **8. Economic Effects of a Successful Reform.**

The first economic question of interest is whether the reform of Customs will serve to increase private sector value-added. There are two main channels through which this could arise: first, through facilitating legal private sector imports and exports, and second, through a shift from illegal trade to legal trade. The first of these effects can be straightforwardly analyzed and is unambiguous in its effects. An increase in the speed with which exports and imports pass through customs reduces the cost of foreign trade, and thus reduces the cost of imported inputs and the supply price of exports. These cost reductions, in turn, increase the price competitiveness of internal production, and should lead to both an increase in import-competing activities and a rise in exports.

The shift from illegal contraband trade to imports and exports flowing through legal channels is more ambiguous in its economic effects. An argument could be made that illegally imported cars, household appliances, and other consumer goods, and inputs such as textiles and computer parts, increase the welfare of consumers and lower production costs, as compared to more heavily taxed legal imports. On the other hand, as indicated earlier, the large size of the contraband industry, if it can be so termed, is linked to a correspondingly large depletion of investment and entrepreneurship from legitimate manufacturing activities. And it can be argued, as well, that since manufacturing activities are difficult to carry on secretly, except on a very small scale, the capture of resources by contraband activity leads to a shift of resources from manufacturing to trade, and investment in transport equipment rather than fixed capital, and that this partly explains Bolivia's weak manufacturing sector, despite its low wages, which ought to imply a strong comparative advantage in light manufacturing. Thus, while a short-term allocative argument could be made to the effect that contraband trade raises welfare, the balance of long-term dynamic effects are likely to be negative.

Another important economic effect of a successful Customs reform is increased fiscal collections. It has been noted earlier that a shift from illegal to legal trade involves not only increased collection of import duties, but the more important value-added tax and

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opportunities for corruption. Apparently, political parties are not yet ready to give up this particular source of patronage and clientelism. One reason that is often cited for this attitude is that a number of key political figures face trials in the courts for various charges of corruption. An honest and effective judiciary might expose a corrupt fund-raising system that largely remains accepted and in place in the Bolivian political party system.

(where applicable) excise tax collections, which Customs is delegated to obtain for imports. To the extent that these additional revenues are then channeled into an increase in the government's infrastructural investments, or health and education expenditures, or even increased salaries as part of a civil service reform, Customs reform will have a long-term beneficial effect. But if the rise in government expenditures corresponding to the increased revenues goes into nonproductive expenditures, or is funneled into private pockets or party treasuries (not necessarily through the Customs but through other means), this is not the case.

Finally, it is useful to consider the short-term winners and losers from Customs reform. As Shleifer and Vishny (1993) have argued, this depends on whether the case is one of "corruption without theft" or "corruption with theft": in the former case, the customer pays the bribe plus the fee or tax charged by the government, while in the latter, the corrupt official pockets the entire amount paid by the client. In the context of the Customs, corruption without theft is exemplified by "speed money" paid to a customs official to expedite goods through customs, with the regular customs tax passed on to the government; corruption with theft, by bribes paid to customs officials to let goods pass through without paying any taxes at all. There would be broad public support for elimination of corruption without theft, because its effect is to raise import prices for traders, domestic producers using imported inputs, and consumers; while for import-competing producers—not a large constituency in Bolivia—corruption without theft produces an effect that is equivalent to a protective tariff. Corruption with theft, however, benefits a broad constituency of producers, traders, and consumers, as it is likely to lead to lower prices for a broad range of taxes—because all taxes have been evaded, and the bribe paid as the price of evasion is likely to be lower than the government taxes.<sup>44</sup>

Since bribing officials to let contraband trade through, or to validate heavily undervalued merchandise, has been the principal form of corruption in the Customs, there is a broad segment of the population that may be adversely affected by reforms that reduce the flow of contraband goods. This includes those trading in such goods but also consumers of all classes who benefit from lower prices. Unfortunately for those responsible for the reform, its implementation has coincided with a regional economic downturn. Over the first three years of the Banzer administration, the combined effects of the two main reforms, coca eradication and customs reform, in terms of reduced economic activity in Bolivia, are estimated at anywhere between \$350-800 million, equivalent to between 4.4 and 10% of GNP. Riding on a persistent economic slowdown partly caused by external factors, including the rise in the price of oil, the economic effects of customs reform and coca eradication have contributed to the largely destructive political mobilization of affected sectors of the informal and illegal economy (see Section IV.9).

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<sup>44</sup> On this latter point, see Shleifer and Vishny, *op. cit.*

## 9. Political Effects of a Successful Reform: Relation to the Broader Reform Agenda.

In view of the serious political crisis faced by the Bolivian government, indeed the entire society, as this report is being written, it would be well to distinguish between two types of effects: the explicitly intended effects, and what may turn out to be the actual political consequences. The analysis that follows is along these lines, ending with a description of the current internal conflict.

Among the explicitly intended political consequences of customs reform were:

- *Taking the Customs out of the patronage circuit and immunizing it against the political spoils system.* If the reform is successful, the authority of party leaders favoring the reform is strengthened. If it fails, the parties may revert to patronage schemes with a vengeance, and national party leaders may be less able to control local leaders.
- *Making the Customs into an exemplary pilot reform case under the National Integrity Plan.* As mentioned earlier, the Customs is one of several agencies chosen under the National Integrity Plan as a pilot project to implement institutional reform of the government. To the extent customs reform succeeds, the National Integrity Plan, the Office of the Vice President, President Banzer, the ruling coalition and even the opposition will be able to claim credit in the next election campaign.
- *Advancing the reform agenda started in 1985 with incentives from international cooperation.* Since 1985 no political party in Bolivia could expect to be taken seriously unless it supported and actively promoted the international reform agenda. At present, given the magnitude of the protest movement that evolved from April to September 2000, political parties are reconsidering the desirability and the convenience of continuing their adherence to the reform agenda promoted by the international community. It is critical for the international community as well as for the main Bolivian political parties that customs reform succeed and be judged to have succeeded by the Bolivian electorate.
- *Adding a measure of legitimacy to the discredited political party system.* Political parties are acutely aware of the need to show the electorate that they are cleaning up their act, at least in some of the most conspicuous places such as the Customs. The idea of a Customs Board explicitly backed by the main political parties was meant to give prominence and legitimacy to the political parties in the customs reform process. Another option would have been, as was the case of the Election Board, to choose a completely non-partisan Customs Board, and shift all responsibility for reform away from the hands of the political parties and into the hands of a group of respected non-partisan professionals. By contrast, the model chosen for the current Customs Board keeps a high degree of direct responsibility of political parties for the success of the reform process. Every member of the

Board has been appointed with the sponsorship of a political party, and every political party that sponsors a Board member is responsible for providing political backing to that member in line with the inter-party agreement to take politics out of the customs.

The actual political consequences that may be anticipated could be as follows.

- *Generating groups of both winners and losers from customs reform.* Some of the economic groups that might expect to benefit or suffer from the reform are indicated in Section IV.8. But there are also political groups among winners and losers. Both types of groups are enumerated in Table 3.

**Table 3. Winners and Losers from the Customs Reform**

<b>Winners</b>	<b>Losers</b>
Honest importers and exporters	Big time smugglers into and out of Bolivia
Formal transportation companies	Truckers unions & independent truckers
Chilean exporters to Bolivian formal sector	Chilean free trade ports (Iquique, etc)
Those fighting illegal drug traffic	Money launderers deprived of smuggling
Formal retailers of goods paying duties	Large informal sector retailing smuggled goods
Honest customs dispatchers	Dishonest customs dispatchers
Political party reformers within parties	Traditional party hacks in all parties
“Smurf” wing of ADN party (friends of the Vice President)	“Dinosaur” wing of ADN party
President Banzer	Politicians benefiting from the spoils system
Leader of the opposition, Gonzalo Sánchez de Lozada	
Amparo Ballivián, Customs Board	Previous customs/management (under prosecution or threat of same)
Donors (IMF, WB, IDB, USAID, etc)	
The long-term public interest	

- *Pressure from political parties on other public agencies to siphon off illegal funds.* National Integrity Plan officials admit that, in order to get some coalition parties out of the customs, the government had to offer them alternative sources of patronage and spoils. Prime among these was the Housing Fund, currently under liquidation due to past scandals. Other agencies where displaced customs “siphon operators” sought to be located include the road service, prefectures and other development funds. The Internal Revenue Service is known to be one of the next targets for reform, but is still valued by traditional party patronage and spoils operators.
- *Pressure on political parties from individuals displaced from the Customs to obtain similar positions.* Political party governance, to the extent it is based on the traditional patronage and spoils system, means that individuals displaced from

the Customs will put pressures on party leaders to obtain for them similar positions or promises of similar positions, in parts of the public administration that remain vulnerable to corruption.

- *The need to protect other vulnerable agencies from political party pressures to bleed them.* Consequent upon the previous point is the obvious need to protect the most vulnerable public agencies from increased pressures from personnel and parties displaced from the customs. A further step would be to follow recommendations from international donors to extend reform to agencies such as the Internal Revenue Service, the Road Service and the Development Funds. Hence the political costs of reform will increase, as will the risks to political parties, without a clear assurance that the benefits of reform will be necessarily rewarded by the electorate.
- *The need for the political party system to find alternative legal sources of funding.* The most enlightened segments of the main political parties have acted jointly to lay the foundations of a legal campaign financing system in Bolivia. The Political Party Law places clear restrictions on campaign financing. Parties are entitled to receive funds in proportion to results of the previous and the following election. The moment they receive such funds parties become subject to Election Board inspection and jurisdiction. As public agencies are taken out of the loop of patronage and of the spoils system, political parties may resort to new private sources of funding. Among these some may be bona fide contributors, while others, such as the illegal drug traffic or the major private investors, may seek to distort the democratic process through concentrated contributions. A pending task for Bolivian reformers is to introduce amendments to the Political Party Law that will protect the relative weight of ordinary citizens who make small contributions to the political party of their choice from being overwhelmed by the superior power of a few institutional contributors who may have a disproportionate degree of influence in determining the chances of different political parties to win elections.
- *Reaffirmation of the multi-party, consensual basis of Bolivian democracy.* Bolivian democracy since 1985 rests on the foundations of a multi-party consensus regarding the conditions of political competition and the need for inter-party cooperation on policies and programs that are in the interest of the nation as a whole. For instance, all the main parties support coca eradication, as they do economic stability and clean elections. Success in Customs reform will reaffirm the consensual basis of Bolivian democracy; conversely, the failure of such reform would cast doubt on the political advantage of continuing to support reforms in conjunction with all the other major parties. At a point when the electorate is up in arms against “the system,” should the major parties enter into a race in which they seek to show they are the most anti-system party, Bolivian democracy would then lose its main basis of support and enter a period of great uncertainty.

These general indications of long-term political results of the Customs reform have been forced into the background, at least for now, by the recent crisis and its aftermath. The disturbances in the spring and again the fall, had to some extent an economic basis. Violent protests started last April in Cochabamba, where army units fired live ammunition against demonstrators, with some deaths resulting, and with no successful judicial prosecution of those shooting. The protests revived in September over most of Bolivia with even greater virulence and persistence.

Between April and September, there were three major, broad-based national consultations about the unsatisfied needs of the poor, the requirements of small producers, and the concerns of the formal business and exporting sectors. These consultations were the National Dialogue, organized by the government in response to donor requirements for external debt reduction under the HIPC initiative; the Small Producers Forum, organized with the assistance of the Inter American Foundation and a gold mining company; and the Jubilee 2000 Forum, organized by the Catholic Church. There is no question that these consultations, successful as they seemed at the time they were conducted, did not detect the strength of the underlying sentiment of protest. In fact, to the extent that participants in these consultations did not perceive any follow-up actions by the government, the consultations themselves might have helped trigger the September events.

A fundamental cause of the unrest may be that the trend toward a liberalized, market-oriented economy, and increased integration in the global economy, have led to rising expectations, while the majority of the population remains impoverished and with limited access to elementary public services. Media reports of corruption in government have led to growing skepticism regarding democratic discourse, and a growing demand for participation in decisions that affect the lives of marginalized urban and rural majorities that do not feel fairly represented by political parties of government, and that resent the growing gap between the ostentatious prosperity of the elite and their own low standard of living. It is against this difficult social background that the hoped-for strengthening and cleaning up of the Bolivian party system will be compelled to proceed.

## V Lessons

The purpose of this study has been to describe and analyze the Bolivian customs reform. There are certain lessons arising from this study, some of which are generally applicable, and some of which apply solely to Bolivia. The points below are intended to be of general applicability, unless specific reference is made to Bolivia.

1. For many low-income countries, with weak economic and technical resources, both domestic political will and international support are necessary conditions for successful anti-corruption reform efforts.
2. International support has two dimensions: encouraging, or exerting needed pressure on, the national government; and providing technical assistance and financial aid. Coordination among international donors, an apparently unusual experience in Bolivia, has been credited with playing a useful role in the Customs reform, and seems like a useful principle to apply elsewhere. This having been said, there is some danger that reforms undertaken primarily in response to outside pressure may not be sustainable, in part because economic and political consequences of the reform are not being taken into account (see 14. below), in part because successful reform in the pilot agency will be jeopardized by institutional weaknesses in unreformed parts of the government (see 8. below).
3. Domestic “political will” means credible commitment of the government to a policy. Such commitment requires a strong, stable government or ruler able to overcome objections from those who will be affected by customs reform. Since customs reform, particularly when it affects deeply embedded political interests, takes time to take hold, the government or ruler should be expected to be in power for a relatively long time (at least 3 to 5 years, depending on local circumstances). Over the long run, for a policy to be perceived as non-reversible, there is need for some form of a multi-party agreement, in a democracy where elections take place at regular intervals, and the ruling party stands a chance of losing them to the opposition. When the main parties come to an explicit agreement about needed reforms, such as that of the Bolivian Customs, the credibility of the reform effort is greatly strengthened, as is its sustainability across succeeding administrations of different parties.
4. Successful reform requires high qualities from the leader of a reforming government agency: trust of the government, credibility vis-à-vis the public, competence, independence, and non-partisanship.
5. All three of these conditions—political will, international support, and high-quality leadership in the reforming agency—are likely to be required over a protracted period before a reform becomes institutionalized. This will certainly be true for Customs reform in Bolivia for a number of years to come. Clientelistic culture like Bolivia’s cannot be eliminated overnight. Although a start has been

- made to eliminate it from the Customs, and to some extent from municipal government through earlier reforms, it still thrives widely throughout the country's political landscape. If reform of the Customs results in greater corruption and patronage in other government agencies, and the reform effort does not persist over the coming years, the net benefits of the Customs reform will have proven to be only minor (mainly economic).
6. For this reason, the sustained efforts of business and civil society are needed to support the reform effort. The private sector can play an especially important part in efforts to clean up government agencies that interface with business; and more generally, can press the case that foreign investment requires a transparent and accountable local environment. Civil society can play a useful role in building public support for anti-corruption efforts, but in Bolivia, private lobbies on behalf of the public interest still need to be strengthened.
  7. In some societies it is enough to trigger widespread anti-corruption sentiment (as the TI 1997 report did in Bolivia) for the public to back customs reform as part of a movement to restore government integrity in general. Once such a climate is established, political parties may compete as to which one is less corrupt or, preferably, which one has better anti-corruption initiatives. In the same vein, a reticent private sector may be motivated to speak out if the right climate is established by the media (provided there is freedom of expression).
  8. Reform of a particular government agency has a better chance to succeed over the long term if it is part of a coherent, well-planned broader program to reform the government. A well-planned reform effort must take into account the interactions among different agencies of the government, and the pace of reform in each agency required to make the reform of the other agencies successful. For instance, the reform (or non-reform) of the justice system has a clear impact on the effectiveness of the Customs reform.
  9. By the same token, a successful pilot reform project will require some support from other, possibly unreformed, government agencies. In the case of the Bolivian Customs, the ultimate success of the reform program will depend in part on the ongoing reform of the prosecutorial and court systems—otherwise, the sanctions laid down by the Customs Law will not be credible. In general, Bolivian experience points to the advisability of emphasizing administrative sanctions, to implement which action can be taken by the reforming agency, rather than judicial sanctions, whose implementation depends upon an (as yet) unreformed judicial system. In the case of Customs, administrative sanctions could include the seizure of goods, which can impose severe economic penalties on the guilty importer, and loss of employment for a guilty customs agent.
  10. In a democratic polity, and in the presence of a free press, mobilizing support for an anti-corruption drive in the government can be difficult to carry out when the accompanying anti-corruption publicity implicates the government itself, or

- leading associates of the government. In a highly corrupt environment, a government that is leading the charge on corruption runs the risk of suffering from increased exposure of its own lack of honesty, and this in turn may result in credibility problems. One way of dealing with this is sharing the responsibility for customs reform among the main political parties and depoliticizing the leadership of the reforming agency, as has largely been accomplished in Bolivia.
11. The leadership of the Bolivian Customs has been removed from direct political interference by two devices: a) non-coinciding terms for the Customs Director and President, and b) the multi-party, yet non-partisan Customs Board, making both appointments subject to a two-thirds majority in the legislature. This principle has applicability to other countries. The Customs Board can be argued to have been the most critical element of institutional engineering, ensuring the translation of political will into a sustainable reform mechanism that would be difficult to alter by future administrations.
  12. One needs to take into account the economic and political effects of a reform. In particular, it is helpful to have some idea of who loses from a reform, in order to provide a safety net for losers who are in danger of becoming destitute, as well as being better able to respond to political opposition that may develop. There have been two kinds of losers in Bolivia: those whose livelihood was connected with smuggling or tax evasion enabled by corruption in the Customs, and clearly identifiable operators of the political spoils system.
  13. Unintended consequences ensue when the damage done to the economic losers is compounded by other economic developments. In the case of Bolivia, coca eradication, the fall in contraband trade (due to both Customs reform and reduced drug sales), and lower growth among regional trading partners have all contributed to an economic downturn beginning last year. This has been the background to the serious social disturbances taking place in September and October of this year. The general lesson here is that before undertaking a reform that has economic consequences for certain groups, those consequences should be carefully analyzed, as should be the political risk factors arising from those consequences. This is a responsibility both of the government and the international donors supporting the reform.
  14. Political parties are in greater need of financial resources during election years. In the case of Bolivia, Customs reform was begun at the start of the five-year mandate of President Banzer, which to some extent may have facilitated the interparty agreement to depoliticize the customs and forego customs spoils. But the reform may also have been facilitated by an implicit understanding that other political agencies would remain available as sources of financing for some time to come. Nevertheless, there is the danger that as sources of illegal political finance are progressively closed down, resistance to reform from remaining elements of the spoils system can be expected to increase, and this may weaken political support for reform further.

15. The above points illustrate the general proposition that there are costs as well as benefits to anti-corruption reforms. Where corruption is deeply embedded in the economic and social fabric, effective reforms imply some disruption of that fabric, including a short-term rise in unemployment and/or full income for some groups in the society. This is why it is important for the political leadership, and the international support for that leadership, both to publicize the long-term benefits of reform and to take concrete steps, if feasible, to relieve the economic impact on low-income groups that are adversely affected by reform measures.

## Appendix 1. List of Persons Interviewed

Raúl Adler	CEO, Compañía Industrial de Tabacos (CIT)
Pablo Alonso	World Bank, La Paz
Claudia Arce	Equidad member Catholic U, La Paz)
Amparo Ballivián	President & CEO, Customs Board Former Minister of Urban Affairs, World Bank experience
Rosario Baptista	Equidad member lawyer in private practice
Carlos Barrero	General Manager, Ovando Motors (Mitsubishi official representative)
Alberto Machicao Barbery	Vice-Minister of Tax Policy, Ministry of Finance (MIR party official)
Gloria Eyzaguirre	Chief Reporter, “Presencia,” main Catholic newspaper Investigative journalist, wrote book on corruption and politics
Luis F. Galleguillos	General Manager, Customs Formerly in private sector
José Garzón	Democracy Officer, USAID/Bolivia
Bruno Giussani	Member of the Customs Board (sponsored by UCS party) Executive President, Chamber of Exporters (CAMEX)
Edgar Justiniano	Academic Coordinator, University of the Cordillera Organizer of dialogue of small producers, early 2000
Fernando Knaudt	Equidad member businessman, importer
Eliahu Kreis	Resident Representative, International Monetary Fund
Alberto Leytón	Coordinator, National Integrity Plan (Office of the Vice President)

Ronald Grebe López	Equidad Member Head of Journalism School, Catholic U. La Paz
Gustavo Mejía	Computer Parts & Service provider; former police & army intelligence agent
Ernesto Mondelo	Sector Specialist, IDB La Paz
Manuel Morón	Manager, a private customs dispatching agency, Servicio Integrado de Gestión Aduanera (SIGA)
Fernando Gutiérrez Moscoso	Attorney for Customs Board
José Eduardo Gutiérrez Ossio	Director, Executing Unit, Customs Modernization Project (PROMA)
Antonio Peres	Equidad member lawyer in private practice
Juan Cristóbal Soruco Quiroga,	Equidad President, journalist
Antonio Soruco Villanueva	Member of the Customs Board (sponsored by MNR party)

## **Appendix 2. Current Forms of Contraband and Related Corruption**

The forms of contraband trade and related corruption in the Bolivian customs still remaining as of September 2000 can be characterized by three geographic regions, each with distinctive cultural characteristics:

1. One-shot border crossings (Western highlands – La Paz, Oruro, Potosí), and
2. Elaborate fraud schemes (Cochabamba)
3. Organized criminal rings (South Eastern Santa Cruz) and smuggling through Santa Cruz airport

These three regional patterns are described in sections 1,3 and 4, respectively. The second section of the Appendix deals with the problem of non-arriving in-transit trucks which has been a major source of contraband trade and associated corruption in Customs.

### **1. One-shot border crossings**

There is a large informal sector in the Western highlands of Bolivia, serving mainly La Paz, but also other cities. Typically, a La Paz informal merchant puts together some capital, determines what to bring according to seasonal and demand considerations, hires a trucker and crosses the Chilean border (about which more will be said below, including the problem of non-arriving in-transit trucks). The smuggled merchandise is brought back to warehouses that are protected from customs inspections by the Customs Law Regulations, which leave small tax contributors under the Simplified Regime as part of the “secondary zone,” (see Box 1).

From these warehouses the smuggled goods are distributed to well-known informal outlets, where customers buy goods at prices significantly lower than those of formal retailers. Informal merchants at these outlets offer further discounts to customers who do not insist on a sales tax receipt. Nevertheless, these merchants upon request extend informal receipts of their own, and even written warranties of up to one year, with names and addresses of repair shops at different cities. Facilities include home delivery at any city in Bolivia through the commercial transportation system. There is a great deal of acceptance and trust on the part of customers, who shop from a large selection of electric and electronic appliances, including computers and other office equipment; bicycles; and assorted household goods. City customers include people from all social classes and income levels.

The trucks that are hired for this purpose come from a large fleet of vehicles that are not properly registered, usually second-hand imports with previous use in Asia. Drivers usually come from Oruro and Potosí Departments, where small settlements cooperate with these drivers, who use a network of dirt roads on the highlands plateau. Truckers may have walkie-talkies to alert each other about customs police coverage, and in some cases are able to hide large trucks at camouflaged garages in small villages, from which smaller vehicles take merchandise into informal warehouses at larger urban centers.

Oruro and Potosí Departments are former mining districts that today are depressed regions, where smuggling is an important source of jobs.

## **2. Non-arriving in-transit trucks**

An international treaty signed by Chile and Bolivia requires the completion of import-export papers known as the International Cargo Manifest (ICM). Overseas freight unloaded at Northern Chilean ports are received by Bolivian customs personnel, who complete the ICM. This is a peculiar feature of treaties with Chile, consequent upon the War of the Pacific (1879), when Bolivia lost its seacoast to Chile.

ICM information is entered into the existing information system (IS). One code in the IS indicates that a given lot of merchandise has departed the point of origin, where the ICM was issued. Another code in the IS indicates that the merchandise has checked in at the declared destination within Bolivia. Declared destinations are warehouses under private contract with a Customs office inside. Merchandise is then inspected by Customs personnel, who complete papers determining the amount that has to be paid on account of several kinds of duties, including customs duties proper.

There are two basic ways of evading this system. One involves merchandise arriving at a Northern Chilean port, which is received by Bolivian authorities as overseas merchandise expressly in transit to Bolivia, but is in fact temporarily imported into Chile in order to avoid the ICM, after which it is re-exported to Bolivia. The second is merchandise arriving at Chilean ports and received by Chilean port and customs authorities as merchandise destined to Chile (duty free zones), which actually will be reshipped to Bolivia without an ICM.

Under the treaty, Chile is supposed to make sure that all cargo leaving its territory has an ICM, completed either by Bolivian Customs authorities at Northern Chilean ports, or by Chilean Customs authorities who complete ICMs for merchandise in transit to Bolivia. In fact, Chile has developed an alternative document, which allows cargo to travel into the no-man's land beyond the Chilean customs post at the Bolivian border as cargo traveling with destination to some point within Chilean territory. This is regarded by Chilean central government authorities as a subsidy to the depressed Northern Region, and Chilean customs authorities and police act accordingly.

Chilean police and customs are extremely well organized, well equipped, efficient, and in general honest. They make sure that no merchandise enters Chile without paying Chilean customs duties. They register merchandise that enters Chile with destination to Bolivia, and know which lots of merchandise will leave for Bolivia with or without a ICM. In all cases Chilean police and customs authorities keep a very close watch on the possibility that merchandise destined to Bolivia with or without a ICM will remain in Chile evading Chilean customs. Whether such merchandise enters Bolivia evading Bolivian customs does not concern them, despite treaty stipulations that oblige them to make sure that every lot of merchandise destined to Bolivia be covered by a properly completed ICM. Once merchandise is transferred to Bolivian trucks at the no-man's land, Bolivian

truckers may take it through back roads into Bolivian urban warehouses without benefit of a ICM, which means there will never be a record of expected arrival in the IS.

Bolivian truckers may also decide to check in at Bolivian border customs posts and obtain in-transit documents that declare a destination inside Bolivia, which generates an ICM. They may prefer to do this when they anticipate that there will be ways to get around customs duties or to pay lower customs fees at the destination point. The latter is the kind of fraud that is a specialty of Cochabamba customs warehouses, (see 3. below).

### **3. Elaborate fraud schemes (Cochabamba)**

Merchandise arriving with ICMs at the Cochabamba private customs warehouses is subject to fraud through undervaluation and other forms of adulterated reporting. This type of fraud operates in a community where everybody knows everybody else and there is a high degree of social control over illegal and unethical behavior. For this reason, fraudulent schemes are quite sophisticated and involve mutual controls by those associated in carrying out fraud.

A typical pattern of customs fraud in Cochabamba is that, first, merchandise is registered as arriving at a warehouse with a ICM. A part of this merchandise (say 20%) is registered as leaving the warehouse after having paid customs duties, but actually 100% of the merchandise leaves the warehouse. Since customs papers show that only 20% of the merchandise left, an inspection would show that there should still be 80% of a given lot within the warehouse. Since this is not the case, customs and warehouse officials conspire to touch up the remaining documentation, so that it shows 100% of the merchandise left and paid duties. In place of the departed merchandise, warehouse personnel fill boxes with junk, for which the warehouse charges storage fees. Just about everybody is involved and profits in some way.

This system depends on the mutual trust and cooperation of practically all warehouse and customs officials. Over time these groups have developed computerized records to check on each other and to keep track of the agreed upon participation in profits. There is trust, but there is also a high degree of suspicion that the next guy is taking more than is due to him, or in some other way “cheating” on the other partners. This scheme was discovered by the current Customs administration mainly because some disaffected conspirators denounced their partners and ruined the business. What made the difference in this case is that the central Customs office had the determination and the technical means to check on the allegations. Evidence of fraudulent operations took 8 business days to present in court with the assistance of slides showing forgeries of various documents, flow charts, organizations charts, profit sharing, and other aspects discovered by central Customs auditors.

This is the origin of the famous RENASA case, (see Box 3, Section III.3).

#### **4. Organized criminal rings (South Eastern Santa Cruz) and Smuggling in Santa Cruz Airport**

This is an area that is still largely out of control of the central Customs administration. Puerto Suárez, San Matías and other points along the Brazilian border are dominated by criminal rings operating on a big-time basis in conjunction with local merchants, customs authorities and the police. Trucks used for smuggling are usually expensive vehicles stolen from Brazil. They may be obtained by Bolivian smugglers in exchange for illegal drugs, or acquired in order to set up money laundering operations through smuggling. Control of the whole region is next to impossible with means presently available to the Customs. More effective control of the borders would require helicopters and additional 4WD vehicles are needed, as well as communications equipment, weapons, and trained police.

Large lots of smuggled merchandise evade the customs or go through Customs with forged papers. This activity is an important element of the local economy and is socially tolerated. Unlike the case of Cochabamba, a successful smuggler or member of a smuggling ring may enjoy respectable status in his community, regardless of spending habits, or perhaps even because of ostentatious spending. This merchandise goes directly to a network of local merchants, who act as retailers for local distribution and wholesalers for distribution at other cities in Bolivia. Everybody knows that these merchants are outlets for smuggled merchandise.

In addition there is considerable “ant” smuggling over the South Eastern border with Brazil, including smuggling suitcases of passengers traveling by rail into Bolivia. Smugglers typically are informal merchants with \$3000 to \$5000 in capital. They operate in the shadow of big time delinquents by offering tips to customs personnel. They are not insignificant as a group, because they constitute an army of thousands.

Another locus of smuggling generally believed to occur is at the Santa Cruz airport, through which containers with luxury imports are supposed to evade customs duties. The allegation is that the Santa Cruz airport customs authorities still enjoy the traditional protection of political parties in power, and that in exchange they still contribute funds to different higher-ups in accordance with established schedules. It is also alleged that the Santa Cruz airport customs post is involved in undervaluation of computer parts for business applications. Thus, chips worth thousands of dollars may be packed in monitor boxes that pay duties as monitors worth just over a hundred dollars. Central Customs authorities are puzzled about a 30% drop in customs collections in the Santa Cruz area since last year. It is also a concern of National Integrity Plan officers. Possible politically related corruption is suspected but this has not yet been definitely proved.

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