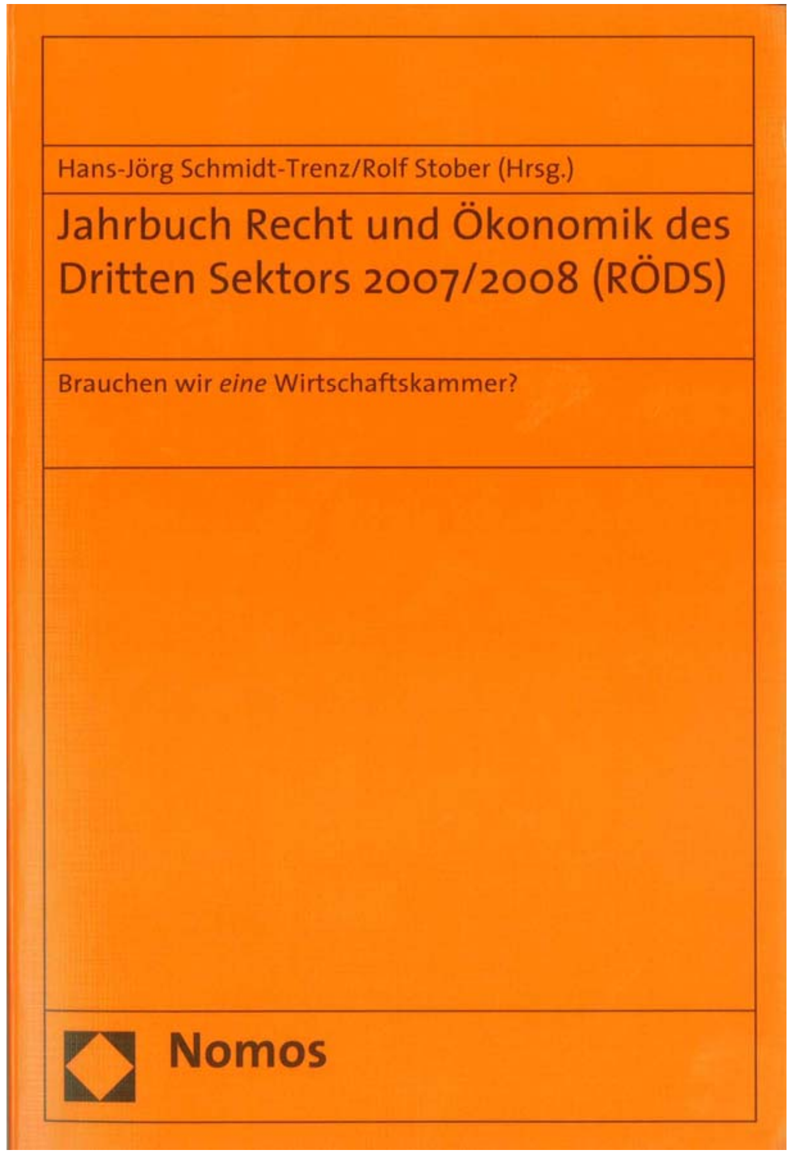
How Can Chambers of Commerce Contribute to Democratic Development?
[in English]

by Jean Rogers and Aleksandr Shkolnikov
2008



How can Chambers of Commerce contribute to democratic development?

Jean Rogers / Aleksandr Shkolnikov

I. Overview

Much of the approach of the New Institutional Economics is focused on the creation of systems of feedback and accountability that incentivize sound economic policies. It provides a particularly useful analytical platform in transition countries, where both policies and policy-making processes are in flux. In these countries the role of business associations and chambers may also be in flux, where the organized business community shifts from cronies to entrepreneurs and the organized bodies' relationship with both government and members evolves in response to market pressures. At the same time, these bodies provide crucial information and feedback on economic policies and are engaged politically through interest representation and constituent (member) outreach.

Successful chambers are inseparable from the legal system within which they operate, and they evolve and develop to address different needs at different points in time. Thus chamber models, just as institutions, cannot be transplanted across borders, and must emerge to address the needs and concerns of business communities and governments, taking into the account unique features of countries' political, socio-economic, and cultural foundations. This paper will explore in greater detail different chamber models and the impact the environment within which chambers operate has on their ability to succeed.

There are several recognized models of National Chamber systems including the Anglo-American model, the Continental model, and a number of variations of mixtures of the two[1]. However, these pure models often function quite differently in developing countries and emerging markets where governmental elites frequently capture control of the Chamber systems through a variety of de jure and de facto means.

Thus in transition questions, the question often arises: How can Chambers of Commerce best contribute to their intertwined political and economic development? Assessing the characteristics of the most effective organizational models requires addressing several related questions:

1 Markus Pilgrim and Ralph Meier, "National Chambers of Commerce: A Primer on the Organization and Role of Chamber Systems, CIPE, 1995, www.cipe.org/programs/ba/pdf/Chamber_Primer.pdf

- Does a mandatory membership model best capture the full int
spectrum of the business community in such countries?
- Or does a mandatory model inhibit democratic development and encou
state corporatism under certain circumstance (such as capture by poli
élites)?
- Given a mandatory chamber model, is there a need for volu
organizations to carry out the function of interest articulation thr
advocacy rather than through the classical tri-partite social dialog syste
- Do voluntary models emerge and organize sufficiently to provide a cre
voice for business in government dialogue?
- Under what circumstances can voluntary membership and
independence from government support democratic development?
- If underlying institutional structures in the political economy make
model more viable than another in certain countries, which political
legal institutions matter most for the business community and Cha
system?

II. Institutions, democracy, and public policy in developing countries

Despite the rapidly globalizing economy and the "flattening" of the worl
Thomas Friedman has called it, the environment for doing business and condu
day-to-day transactions differs markedly in emerging democracies or transiti
economies from their more established counterparts.

In the OECD countries it takes about 15 days to legally start a business, y
Latin America it would take more than 4 times as long – nearly 70 days.[2] Si
differences exist in tax policies, licensing procedures, and customs proce
Moreover, in addition to the legal and regulatory framework differences that exi
paper, a serious lack of enforcement in many developing countries increases thi
– except where norms of corrupt practices circumvent it.

Whether the issue is the result of poor regulations or poor enforcement of rul
is at the core of many countries' economic woes such as large informal s
economies and limited value creation. The influential development econ
Hernando de Soto of Peru has conducted detailed studies of the economic
political constraints facing business in many countries, and his findings
consistent regardless of the country's size, geographic location, or availabili
natural resources.[3]

One stark example de Soto offers of how regulations create business incentiv
disincentives can be seen in bankruptcy law. Defaulting on a loan in the

2 World Bank Doing Business Database www.doingbusiness.org
3 For more studies of Hernando de Soto, cp. www.ild.or.pe or legalempowerment.undp.or

damages future credit opportunities and results in loss of residual assets or reschedules payment according to court-determined terms. The businessman and creditor have access to the legal system to resolve any dispute and meet terms. In contrast, however, to default on a loan in Egypt or Kuwait is to risk being sent to debtors prison, not only depriving the businessman of liberty but also depriving the creditor of access to repayment that might be possible were the debtor to remain productive. Thus it is little wonder that an individual can move to Berlin or New York and become a successful entrepreneur, yet struggle in Lima or Cairo. Over the past two decades reformers have learned that many of these differences between countries significantly affect how democracies and market economies function around the world. Many continue to re-learn these lessons today.

How these policies arise is often quite different as well. In established democracies, mechanisms exist to engage civil society, ensure media openness, solicit public comments on draft laws, and hold political agents accountable for their actions or inactions. In many of the emerging democracies or transition economies, such mechanisms are often much weaker or missing altogether. Policymakers may not have the technical or financial capacity to draft effective laws or to analyze the impact of legislation. The public has limited or no access to draft laws, no direct opportunity for commentary, and may only learn of a new law once it has been enacted -- if an official notice indeed is ever published. For its part, civil society is often ill-prepared to be an effective participant in the governance process or to act as a watchdog over government actions.

Thus we see that on issues of keen interest to chamber members – licensing, taxation, commercial law, administrative law, customs, inspections, loan regulations, bankruptcy proceedings, and many others – the regulatory environment is typically cumbersome, opaque, and rife with contradiction. Similarly, the process of engagement that chambers typically use to address these issues – tripartite negotiations, media publicity, advocacy – may also be subject to the same problems. As an additional challenge, the role of the chamber itself is also typically evolving in these countries: interest representation is undergoing significant redefinition, public policy advocacy may be an entirely new concept, and the definition and composition of chambers may be under serious debate. This brings us to the question of institutions.

The significance of the disparity between how things work in developed and developing countries has been captured in great detail by Nobel Laureate Douglass North and his colleagues in the field of new institutional economics (NIE). Institutions – the rules of the game and incentives structures that comprise the political, economic, and social fabric of society -- are unique to each country, North argues. They cannot be copied or transplanted across borders and be expected to work in the same way. Instead, NIE scholars suggest focusing on countries' uniqueness and recognizing that neither political nor economic reforms can be engineered from the outside – they require local capacity, expertise, and ownership of the process.[4]

The tools of new institutional economics provide a particularly useful analytical platform for understanding reforms in transition countries, where both policies and policymaking processes are in flux. What roles do different stakeholders play in the reform process? How can bureaucracies be held accountable for their action and inaction? What is the role of the business community in contributing to the overall economic restructuring? How do institutions evolve over time? Finally, which institutions contribute to countries' development and which ones simply increase transactions costs and undermine development prospects?

The Center for International Private Enterprise (CIPE)[5] has twenty-five years of experience in addressing these questions. Though international experts and toolkits abound, there is no one-size fits all approach to policy reform and development. Just as institutions differ, so do policies, priorities, and implementation mechanisms. Yet many successful transition efforts share one thing in common: they involve open channels of communication between the broad-based business community as part of civil society on one side and policymakers on the other. They successfully employ the institution of democratic policymaking, or democratic governance.

To transition successfully to market-oriented democracies, many developing countries must first break corporate-state relationships, getting rid of corporatism and insider-dealings between individual government officials and their cronies in the private sector, replacing those relationships with transparent mechanisms for policymaking. Such systems provide much better opportunities for developing effective economic policy for broad-based growth, rather than pushing through laws and regulations than benefit individuals and undermine broader developmental prospects. While the idea is simple, implementing it is a much harder task. It does not take place overnight and in many cases, in addition to new policy tools and regulations, it requires new awareness – and self-awareness – of individuals' roles as government officials or business leaders.

Unfortunately, in many of the emerging democracies with opaque public policy environments the business community itself is not always prepared to be an effective contributor in a democratic process. In such cases, the role of business associations and chambers may also be in flux, where the organized business community shifts

4 North, Douglass. "Economic Performance through Time" Nobel Prize Lecture http://nobelprize.org/nobel_prizes/economics/laureates/1993/north-lecture.html

5 CIPE was established by the U.S. Chamber of Commerce in 1983 in connection with the National Endowment for Democracy to strengthen democracy around the globe through private enterprise and market-oriented reform. Working primarily with business associations, chambers of commerce, and economic policy institutes CIPE has supported more than 1,000 initiatives in over 100 developing countries, involving the private sector in policy advocacy and institutional reform, improving governance, and building understanding of market-based democratic systems.

from cronies to entrepreneurs and the organized bodies' relationship with both government and members evolves in response to market pressures. Yet, in a proper framework, these bodies have an opportunity provide crucial information and feedback on economic policies and can be engaged politically through interest representation and constituent (member) outreach.

Successful chambers are inseparable from the legal system within which they operate, and they evolve and develop to address different needs at different points in time. Thus chamber models, just as institutions, cannot be transplanted across borders, and must emerge to address the needs and concerns of business communities and governments, taking into the account unique features of countries' political, socio-economic, and cultural foundations. Chambers can play a central role in market-oriented reforms and public sector transparency. Different chamber models and the environment within which they operate affect their ability to help countries achieve democratic governance and long-term economic prosperity.

III. Economic reform and chambers of commerce

Academics and practitioners alike have long debated the proper relationship between the concepts of democracy, economic growth, and market reforms. Setting aside the many disagreements and all the economic and theoretical studies on the linkages between countries' political systems and their economic performance, from the practical point of view one can argue that for business to succeed it needs a good business climate. This is often a good starting point that commands almost universal agreement. Opinions on what constitutes a good business climate, however, often differ. From the business perspective, a good business climate relates closely to institutions of a market economy.

Predictable tax rates, effective property rights institutions, contract enforcement, and access to information are all institutions of a functional market economy. They are required for business to succeed – not just today or tomorrow, but in the long term. In this sense, a market economy is much more than individual transactions in a market place to balance out supply and demand – a market economy is about repeated transactions over time with people who may never meet. But how can these institutions come about?

In established economies of Western Europe, for example, market institutions have been evolving for hundreds of years, and the economic and political picture of countries we observe today is based on decades of trial and error, evolution, and a series of interdependent complex processes that might not be comprehended fully by outsiders. Property rights, for example, are much more than regulations; in the OECD countries property rights are largely recognized as a key social institution. Many of the emerging democracies, seeking to establish the same institutions in order to reach similar levels of prosperity and stability, are finding that copying policies from one country to another does not work. Important as it may be to have property rights regulations, they are insufficient and alone may not create needed institutions that are widely recognized and respected by members of society and tha are fairly and consistently enforced by the government.

It is important to recognize that all countries have institutions and to conside both how they work and why they exist the way they do before contemplating an reform. Informal institutions should be part of the consideration. In the absence o formal institutional arrangements, business people often devise a set of informa rules that facilitate market activity. These informal rules make business possible, ye the enterprises are typically quite limited in their operations without the rights an benefits of formal legal status.

Institutions cannot be imposed; they evolve over time and require proper channel to facilitate that evolution. Developing a market economy requires time an participatory political processes that provide the necessary mechanisms for informa institutions to evolve into a codified set of formal institutional arrangements Authoritarian governments, by suppressing the free flow of information an interactive decision-making, are inherently less capable of providing a prope climate for such institutional reform than democracies. In such systems policymakers may design laws and regulations according to their own needs, th needs of their cronies, the preferences of their superiors, or according to limite information lacking "real world" feedback. In these cases, the outcomes, like th process itself, lacks accountability pressures from those most affected by the policie and thus has no self-correcting incentive. Democracies, by providing platforms fo free flow of information, public debates, and a vibrant civil society, provide greate opportunities for institutional reform. From an economic standpoint, democracie can be viewed as systems with opportunities for economic actors to channel ke information to policymakers on a day-to-day level; policymakers are thu sufficiently empowered and informed to shape business policies conducive t growth.

Realistically, few countries have perfected feedback mechanisms or full countered special interest influence. However, established democracies clearly ten toward more inclusive policymaking with more open information flow, while close regimes use a more top-down approach. The real challenges face those countrie oscillating in between – weak, fragile, rebuilding, backsliding, or transitionin democracies – which are a huge number of countries. In such countries, election may put politicians in office, but mechanisms of civic engagement in public polic are largely absent or remain weak. In such environments the challenges are twofolc On the one hand, there is a need to increase legislators' capacity to fulfill their rol as envisioned in the very idea of democratic government. On the other hand, there i a need to increase the capacity of civil society organizations to represent thei constituents, participate in the public policy process, and act as a watchdog ove government's actions. In order to link the two sides, formal communication an feedback mechanisms must also be established.

In many emerging economies, chambers of commerce are uniquely positioned t meet these challenges. As representatives of the broad-based business communit they can provide key information on the effects of legislation, the needs facing th business community rather than individual companies, and barriers that hamper job creation and growth. At the same time, chambers of commerce can evaluate implementation of government objectives in key business sectors and ensure that policymakers deliver on their promises.

While chambers can perform such vital functions as part of a democratic society, it does not necessarily mean they do so. A host of different chamber models and approaches means that sometimes chambers of commerce are part of the problem, suppressing the flow of information and undermining the emergence of market institutions. Non-transparent chambers heavily dominated by insiders, for example, can serve as a tool for cronies to exert influence over the policy process, leading to what the World Banks has called "state capture" – whereby individual interests can shape legislation behind the doors to benefit their own narrow interests rather than interests of the broad business community and society in general.

IV. How institutions impact chambers' role

The role that chambers perform in a democratic society depends on several interrelated issues. Chambers depend on the legal framework within which they operate, since that framework creates incentives for action or inaction in different policy areas. The legal framework also can define the scope of their operation and the ability of chambers to develop innovative services to address members' concerns. Chambers themselves, however, can influence the legal framework and country's institutions, thereby adjusting their own role.

Chambers of commerce can be both redistributive and value-creating organizations. From the redistributive perspective, chambers are viewed as mechanisms for organized interests to influence public policy to gain welfare transfers from less powerful or unorganized groups. For example, when chambers put in place industry protection measures or secure subsidies for a limited group of producers, the conventional economic framework suggests that such measures improve the welfare of the favored group yet reduce the overall welfare by eroding competition. Chambers can also be viewed as a value creation mechanism. In such a framework, chambers can express business concerns to policymakers, streamline procedures, provide services to members, or help improve contract enforcement.

In developing countries the redistributive nature of chambers is often the focus of analysis. Chambers can certainly exist as tools used by insider business interests to dominate policy priorities or mechanisms whereby governments can levy additional taxes on business. Such chambers can be found in many developing countries with unstable institutions, opaque business practices, and weak legal framework. The value creation aspect of chambers as described above, however, is not sufficiently recognized in many developing countries.

As business organizations inseparable from the legal environment that defines what they can or cannot do, chambers have traditionally been evaluated through a prism of private and public law chambers. While there are arguments by both sides on the benefits of one system over the other, CIPE's own experience highlights the important fact that each of the chamber models can succeed or fail depending on the initial conditions, the structure of government and business community, and other factors. For example, while the private law system generally suggests putting in place a voluntary membership dues structure, chambers in countries emerging from conflict may find it difficult to collect sufficient membership to cover basic operations. Business leaders may not recognize the benefits that a chamber provides or, alternatively, chambers may not actually provide any significant benefit. Public law chambers, in contrast, may build on economies of scale and provide services to large segment of a business community.

In contrast, mandatory membership that is part of the public law chamber models may be unsuitable for developing countries undergoing rapid transition since it may distort incentives for chambers. Rather than being pressured to innovate and constantly respond to the needs of the business community in a competitive environment, mandatory membership chambers may become moribund, having a solid membership base regardless of their performance. Similarly, heavy government influence over activities of public law chamber in countries with weak democratic governance institutions may mean that chambers can be used by cronies to push for insider agendas rather than serve the business community. With a developed judicial system, members can hold the chamber accountable for not fulfilling its duties; in developing countries riddled with corruption, members of the public law chambers may have few opportunities to demand accountability.

The broader point is that the traditional analysis of private vs. public law chambers is increasingly difficult to apply. One reason is that developing countries often have a hybrid model. Most importantly, however, the traditional analysis does not adequately consider how private law chambers and public law chambers behave under different country conditions.

Setting aside the traditional public-private law comparison, several factors can be identified that limit the ability of chambers to become value-creating organizations. Removing many of these obstacles and promoting sound governance institutions helps chambers to become active participants in the process of building market-oriented institutions:

Government influence

The influence governments exert over chambers of commerce significantly affects their ability to act as a voice of business in public policy debates. While in established democracies, transparency ensures that the relationship between governments and chamber leadership is open and can be scrutinized by the press, in weak democracies there are many incentives for governments to use chambers for achieving political goals.

There are many ways in which governments can influence chamber activities. For example, they can nominate individuals to serve on boards of directors, encouraging greater political responsiveness at members' expense. Such mechanisms can become tools for placing insiders to run business organizations merely to ratify government policy or, worse, to strengthen individual leaders' own economic priorities. Government influence also can be seen in funding. If chambers are heavily dependent on government funding and subsidies to sustain their activities, they are less likely to criticize policies, especially when budgetary and governance changes can be done swiftly behind closed doors.

One way of limiting government influence over chambers is promoting transparency. When decisions are made openly and can be scrutinized by the public, opportunities for insider decision-making and transactions are reduced. At the same time, there is also a need for broader set of reforms that include press freedoms and anti-corruption initiatives that further reduce undue influence.

Structure of the private sector

The business community does not operate as a single entity. In fact, there are typically several distinct communities within the business sector. These include the powerful business elites, smaller firms, 'leading-edge' firms in globally competitive markets, informal entrepreneurs, and state-owned companies – all of which have very different interests. Which sector is dominant in a country has a strong impact on the institutional environment in which chambers and associations operate. In most developing countries, the informal sector is a large part of the economy. Or state-owned firms may be central, affecting debates regarding privatization and competition policies. Where elites or cronies dominate political discourse, advocacy challenges are far different that where smaller firms for a broad economic base. The interests of each of these communities and their relationship to the chamber affect the chamber's access and credibility, its positioning in policy debates, and its choice of services. Engaging the business community in the broadest possible sense ensures greater participation and feedback, as well as a diversity of competitive ideas, all of which ultimately strengthen chambers as well as the political processes and checks on government power.

Membership structure

Weak and fragmented business communities may undermine the ability of chambers to become effective representatives of business interests within a voluntary membership model. It is especially evident in cases where large businesses can dominate smaller members due to a vast difference in resources and organization's own internal governance failures. In such cases, major members can "capture" chambers and set activities and direct services to respond to their own needs, rather than for the benefit of all members.

Regardless of membership structure – whether mandatory, voluntary, or mixed – the central point of analyzing chambers from this perspective should be the incentives that they face in voicing the needs and concerns members rather than representing a select group or simply responding to government directives. Although a voluntary membership structure coincides to a greater degree with market institutions, one cannot establish a membership structure without a careful study of country conditions and incentives the private sector faces in engaging in public policy. Membership structures should be established according to their ability to resolve the collective action problem and facilitate chambers effective in channeling key information on business activities to government officials.

Access to policymakers

Access to policymakers is also an important feature that affects chamber success. The private sector struggles to be heard in many countries regardless of chamber law status.

There are two primary approaches for chambers to improving their access to policymakers. They may seek official consultative status, becoming a permanent feature in designated government committees and ministries. This allows chambers to participate in discussions and to present opinions of the business community when pertinent. Some chamber models allow for official consultative status at the outset, while others provide possibility for chambers to gain such a status on their own. Regardless, the ability of chambers to participate in various government structures must be evaluated from the perspective of chambers' own ability to voice *independent* opinion.

Alternatively, chambers can develop effective advocacy programs without special status, using all available resources to reach out to policymakers either directly or indirectly through media and public events. This is, in fact, the essence of democracy, whereby chambers as civil society organizations engage political leaders in a dialogue. Although political will to listen to the private sector may be lacking, and effective chamber program and help create political will and leverage reform-minded individuals within government structures.

Neither official consultative status nor advocacy confers a guarantee of success but they do challenge policymakers to listen and respond to the private sector input.

Internal capacity

Perhaps the most important barrier to chambers' effective participation in promoting economic reform is their own weak internal capacity. Human resources, for example, can be a rather important issue affecting chambers, especially those undergoing transitions from a command-style economy to market-oriented economic structures. Chambers can quickly find themselves ineffective if people in charge continue to operate according to rules (formal and informal) of the old system. In Ukraine recently this was referred to as "trying to achieve progressive goals through Soviet methods". Changing firmly entrenched mindsets and work habits, however, can take considerable time. By extension, this capacity problem manifests in many areas, including weak governance structures, lack of strategic planning, poor financial management, inability to design and conduct advocacy programs, and weak membership base, to name a few. In a "chicken or egg" conundrum, these capacity issues are often attributed to the poor governance systems and weak economies in which the chamber exists; the chamber challenge is to lead reform while undergoing change itself.

How these issues combine under local circumstances heavily influences the status, activities, and strength of the chamber in each country. In Germany, for example, the Association of German Chambers of Industry and Commerce handles such public service functions as apprenticeship and other training programs as well as foreign trade promotion. The Association of German Industries, however, has emerged as a voluntary membership organization focused on advocacy. As a typical European model, this has been successful -- predicated on a strong and predictable legal framework, an open society, and a vibrant business sector. Many EU accession countries have debated this approach at length, including Estonia, Hungary, Poland, and Slovenia, which opted for a private law model to break significantly with their traditional government intervention in the economy. Bulgaria and Romania adopted a mixed model and have struggled to strengthen the advocacy component of their representation of the business community. Serbia and Albania maintain a public law model that is viewed as ineffective by most businesses, evidenced by the low 5-10% rate of dues payment. On the other side of the world, China has begun to consider private business associations and there is a wide gap in understanding to address first, such that when inviting a U.S. Chamber delegation to visit, they requested that chamber's "book of regulations for controlling members", which made no sense to U.S. Chamber members accustomed to setting the Chamber's agenda.

CIPE's own programs focus heavily on the underlying issues of business sector strength. Through training and support, CIPE seeks to build chambers and associations that are strong organizations – constructive representatives in society, financially sound, well governed, and effective advocates of sound economic policies, investment, business development, and broad-based job creation.

V. *Conclusion*

Chambers of commerce have a unique role to play in the development of countries. They can facilitate bottom-up economic reforms, and in the process, strengthen institutions of democratic governance. While many chambers in developed economies are able to fulfill this role, the weak institutional climate of many developing countries often prevents them from doing so.

In many developing countries we see two types of chambers. On the one hand there are those that push for market reforms, seek to hold politicians to their electoral promises, demand sound economic policies, and represent the interests of the business community and society broadly. On the other hand, there are those that are simply an extension of government in the private sector, directing activities of business rather than representing their interests in government. The challenge for reformers is help to develop chambers that resemble the former rather than the latter.

There are different chambers models, each with their own set of strengths and disadvantages. However, applying lessons of new institutional economics, one must be careful in advocating a specific chamber for developing countries. A greater emphasis must be placed on analyzing countries' economic, political, and social structures as well as current country conditions to determine the best set of strategies for setting up private sector representative organizations. Developed with concepts of incentives and local ownership in mind, chambers can fulfill their role as part of civil society in developing countries.

As we address the question "Do we need a single Economic Chamber?" the experience from other lands can sharpen our understanding of institutional issues that must be first be addressed to best answer the question.

When the Chamber – and its members – analyze these underlying factors, it can better clarify and fulfill a most effective role.

Bibliography

Becker, Gary S. "A Theory of Competition Among Pressure Groups for Political Influence." The Quarterly Journal of Economics, Vol. 98, No. 3, pp. 371-400, August 1983.

CIPE. "Creating a Voice for Entrepreneurs in Montenegro." Center for International Private Enterprise, Economic Reform Case Study #0601, August 2006.

CIPE. "National Business Agenda Guidebook." Center for International Private Enterprise, 2007.

De Soto, Hernando. "The Other Path: The Economic Answer to Terrorism." Perseus Books Group, 2002.

Dixit, Avinash K. "Lawlessness and Economics: Alternative Modes of Governance." Princeton University Press, 2007.

Fields, Gary S. and Guy Pfeffermann. "Pathways out of Poverty: Private Firms and Economic Mobility in Developing Countries." Kluwer Academic Publishers, 2003.

Kornai, Janos, "The Great Transformation of Central Eastern Europe: Success and Disappointment." Economics of Transition, Vol. 14, No. 2, pp. 207-244, April 2006.

North, Douglass C. "Institutions, Institutional Change and Economic Performance." Cambridge University Press,1990.

Olson, Mancur. "The Logic of Collective Action: Public Goods and the Theory of Groups." Harvard University Press; Revised edition January 1, 1971.

Olson, Mancur. "The Rise and Decline of Nations: Economic Growth, Stagflation, and Social Rigidities." Yale University Press, 1984.

Pilgrim, Markus and Ralf Meier. "National Chambers Of Commerce: A Primer on the Organization and Role of Chamber Systems." Center for International Private Enterprise, 1995.