

The Moral Dimension of the Fight against Corruption

Augusto Lopez-Claros

From the sidelines of economic research twenty-five years ago, corruption has now become a central preoccupation of development thinkers and policy makers. Postwar experience and insight, reflected in a growing body of academic research, highlight the causes and consequences of corruption in the development process and its remedies.

This essay identifies the primary sources and effects of corruption. Why does it destroy human prosperity and how does it impede sustainable development? How can we deal with its undesirable consequences? Clearly, corruption has moral and ethical dimensions involving the violation of trust and the abdication of principles central to the spiritual foundations of all the world's major religions, principles that have provided the moral underpinnings for many modern states, as, for example, the US Constitution.

Sources of Corruption

Economists agree that one important source of corruption stems from the distributional attributes of the state.¹ For better or for worse, the role of the state in the economy has greatly expanded over the past century. In 1913, the world's thirteen largest economies had public expenditures averaging

around 12 percent of GDP. By 1990, this ratio had risen to 43 percent, and in some countries to well over 50 percent. Associated with this growth was a proliferation of benefits under state control and of the ways in which states impose costs on society. The larger the number of interactions between officials and private citizens, the more opportunities for citizens to illegally pay for benefits to which they are not entitled or to avoid costs or obligations for which they are responsible.

The larger the number of interactions between officials and private citizens, the more opportunities for citizens to illegally pay for benefits to which they are not entitled or to avoid costs or obligations for which they are responsible.

The typical citizen has countless reasons to engage with government officials: to obtain a birth certificate and a passport, pay taxes, open a business, drive a car, register property, and engage in foreign trade. Individuals and businesses must comply with myriad regulations. The World Bank's *Doing Business* report, a useful annual compendium of business regulations in 190 countries, paints a sobering picture of the numbing levels of bureaucracy and red tape endured by businesses globally.²

Often businesses perceive paying bribes as a way to save time and enhance efficiency and as the only way to short-circuit the onerous regulations in many countries without undermining their competitive position relative to those who routinely pay bribes.

Augusto Lopez-Claros is the director of the Global Indicators Group at the World Bank. Previously, he was chief economist and director of the Global Competitiveness Program at the World Economic Forum.

For example, central planning absurdities in the Soviet Union nurtured “corruption” on the part of factory managers, who made a mockery of efficiency in resource allocation. The more insane the rules, the more participants in any system will find ways to break them.

Where tax laws are unclear or difficult to understand, tax inspectors and auditors can “interpret” them, allowing unwholesome “compromises” with taxpayers. The provision of goods and services at below-market prices also creates fertile ground for corruption and invariably gives rise to rationing mechanisms to manage excess demand, requiring the exercise of discretion by government officials.

Some bribes are offered as incentives for bureaucrats, such as “speed money,” typically used to “facilitate” transactions or jump the queue. Some economists argue that bribery improves efficiency, provides incentives to work more quickly, and allows those who value their time to move faster. However, Gunnar Myrdal pointed out that, over time, bureaucrats deliberately slow things down, find imaginary obstacles or create new ones to attract facilitation fees.³ Ironically, “speed money” is paid not to speed things up but to avoid artificial delays created by corrupt bureaucrats and, far from enhancing efficiency, only serves to strengthen the bribery machinery.⁴

How Does Corruption Destroy Human Prosperity?

Corruption damages the social and institutional fabric of a country by undermining sustainable economic development, cutting into government revenue, and limiting productivity. When taxes are seen not as a public benefit but rather as a questionable business proposition, tension develops between the government and taxpayers, who

expect to see a payoff in better schools, infrastructure, and a better-trained and healthier workforce. Money leaking out of the budget is not available to lighten the burden of the poor through investment in education and training, public health, and modernizing infrastructure. When this implicit contract is sabotaged, taxpayers feel justified in avoiding paying taxes or, worse, engaging in bribery themselves.

Corruption damages the social and institutional fabric of a country by undermining sustainable economic development, cutting into government revenue, and limiting productivity.

Second, corruption distorts the decision-making process connected with public investment projects. Large capital projects become tempting opportunities for corruption, as when larger or more complex projects are undertaken, which are more than warranted by the country’s real needs. The world is littered with the skeletons of white elephants, many built with external credits. Where resources are scarce, governments cut spending elsewhere. Vito Tanzi argued that corruption reduces expenditures on health and education, areas less vulnerable to bribery.⁵

Third, empirical evidence indicates that the higher the level of corruption in a country, the larger the share of its economy that goes underground, beyond the reach of tax authorities. Studies show that when corruption undermines foreign direct investment, mimicking a tax, investors will seek less corrupt countries. In an analysis of data on direct investment from fourteen source countries to forty-five host countries, Shang-Jin Wei of Columbia University concluded that “an increase in the corruption level from that of Singapore to that of

Mexico is equivalent to raising the tax rate by 21–24 percentage points.”⁶

Fourth, corruption discourages private-sector development and innovation and encourages inefficiency. Bright young entrepreneurs, intimidated by bureaucratic obstacles, financial costs, and the burdens of dealing with corrupt officials, will take their ideas elsewhere. Economic growth is jeopardized when corruption discourages entry into the market or precipitates early departure. In a 1995 analysis using indices of corruption and institutional efficiency, Paulo Mauro showed how corruption lowers investment and hinders economic growth,⁷ rendering many small- and medium-sized enterprises—often the engines of economic growth and job creation in the developing world—unable to protect themselves from proliferating requests for bribes.⁸

Fifth, corruption contributes to a misallocation of human resources. To sustain a system of corruption, officials and those who pay them are constrained to invest time and effort to developing certain skills, nurturing relationships, and creating supporting institutions and opaque systems, such as secret bank accounts and off-the-books transactions. Surveys of businesses show that inordinate time is spent in corrupt countries ensuring compliance with regulations, avoiding penalties, and dealing with the bribery system that underpins them.

Sixth, corruption creates uncertainty. The terms of the “contract” with a bribed bureaucrat must be constantly renegotiated to extend the life of the benefit or prevent its collapse. Indeed, a business, having flouted the law, may find it difficult to extricate itself from extortion. In such an uncertain environment with insecure property rights, firms cannot invest and make long-term plans. Short-term maximization of short-term profits becomes an optimal strategy, leading to such outcomes as deforestation

or exhausting a non-renewable resource. Uncertainty perverts the incentives that prompt individuals to seek public office. Corrupt politicians aim to remain in office as long as possible, not because they are serving the public good but because they fear losing pecuniary benefits.

Seventh, when corruption betrays trust, the moral stature of the bureaucracy and the state are delegitimized in the public mind. Even when corrupt transactions are shrouded in secrecy, the details leak out and tarnish the reputation of the government. With its credibility compromised, the government can no longer be a constructive agent of change in other areas of policy. Corrupt governments can no longer serve as credible enforcers of contracts and protectors of property rights and will have difficulty persuading individuals and businesses to pay their taxes. With trust betrayed, popular discontent follows. Clausen, Kraay, and Nyiri used recent evidence from the Gallup World Poll to prove the negative correlation between corruption and confidence in public institutions.⁹

When corruption betrays trust, the moral stature of the bureaucracy and the state are delegitimized in the public mind.

Eighth, bribery and corruption are contagious and undermine the stability of the state by spawning organized criminal groups, who overwhelm the police and infiltrate legal businesses; protection rackets create a climate of fear and uncertainty; tax inspectors extort businesses; corrupt police kidnap innocents and demand ransom; officials demand payment for meetings; aid money disappears into private coffers; capital flight leads to disinvestment; and separate centers

of power emerge to rival those of the state, further reducing the probability that criminals will be caught.¹⁰ In this vicious cycle, the police and other organs of the state themselves become criminalized, businesses not only have to deal with corrupt bureaucracies, but become vulnerable to attacks from competitors who will pay the police or tax inspectors to harass and intimidate.

Strategies to Fight Corruption

What options exist for governments hoping to reduce corruption? Rose-Ackerman recommended a two-pronged strategy aimed at increasing the benefits of honesty and raising the costs of corruption,¹¹ a sensible combination of reward and punishment as the driving force of reforms. Indeed, a number of strategies are available, many having a strong underlying ethical foundation.

Pay civil servants well. Undercompensating civil servants clearly affects their motivation and incentives. If public-sector wages are too low, employees find themselves pressured to supplement their incomes in “unofficial” ways. IMF economists Van Rijckeghem and Weder sampled developing countries and found that low public-sector wages correlate with a higher incidence of corruption.¹² It is no coincidence that the country with the highest paid civil servants, Singapore, also has low levels of corruption.

Create transparency and openness in government spending. Governments use their monetary resources to satisfy specific needs, some relatively transparently and usually in the public interest. The more open and transparent the process, the less opportunity for malfeasance, allowing citizens to scrutinize government activities and debate the merits of public policies.¹³ Press freedom and literacy also shape the context for reforms, and an active, participating civil society is vital in supporting strategies for reducing corrup-

tion. Transparency in tax systems particularly determines public perceptions of how fairly public funds are spent. Nobel laureate Amartya Sen notes that societies operate better under some presumption of trust. The freedom of individuals to deal with one another under “guarantees of disclosure and honesty” is essential in preventing corruption and other abuses.¹⁴

Cut red tape. The correlation between corruption and bureaucratic red tape, as captured by the *Doing Business* indicators, suggests the importance of eliminating needless regulations, while safeguarding essential regulatory functions of the state. The regulations of many countries are often outdated, no longer correspond to present realities, and lure officials into illegal activity.¹⁵

The elimination of red tape can best be promoted as a reform to modernize the state. The most competitive economies have managed to lighten the regulatory burden as a way of enhancing economic efficiency, essential to healthy competition. Rose-Ackerman suggests that “the most obvious approach is simply to eliminate laws and programs that breed corruption.”¹⁶

Replace regressive, distorting subsidies with targeted cash transfers. A 2015 study by the IMF on the global scale of energy subsidies for petroleum, electricity, natural gas, and coal, factoring in the cost of negative externalities from energy consumption (e.g., global warming, pollution), estimated these to amount to an astronomical \$5.3 trillion per year, equivalent to about 6.5 percent of global GDP and from 5 to 35 percent of total government revenues depending on the region. Sixty percent of the benefits from gasoline subsidies accrue to the richest 20 percent of households. The authors of the IMF study estimate that removing such subsidies could yield a 21 percent reduction in CO₂ emissions,¹⁷ reduce global energy demand, and mitigate the effects of

climate change. Factoring in the wasted opportunities, such as much-needed schools, infrastructure, hospitals, environmental effects associated with artificially low prices, etc., it is obviously better to replace expensive, regressive subsidies with targeted cash transfers aimed at the poor.

Establish international conventions. Because corruption in a globalized economy has increasing cross-border effects, improving the growing international legal framework for corruption control is another key option open to governments. In addition to the OECD's Anti-Bribery Convention, the United Nations Convention against Corruption entered into force in 2005 and by early 2016 had been ratified by 140 of the initial 178 signatories. The Convention creates a global framework involving developed and developing nations and covers domestic and foreign corruption, extortion, preventive measures, anti-money-laundering provisions, conflict-of-interest laws, and means to recover illicit funds deposited by officials in offshore banks. The effectiveness of the UN Convention as a tool to deter corruption will depend on the establishment of adequate national monitoring mechanisms to assess government compliance.

Others argue for more robust implementation of the anti-corruption laws in the forty signatories to the OECD's Anti-Bribery Convention. Governments must crack down on companies that continue to bribe foreign officials, instead of shielding them from compliance with anti-corruption laws in a misguided attempt to make them more competitive in other countries. Trade promotion should not trump corruption control. Governments still suffer double standards, criminalizing bribery at home while looking the other way when bribery involves foreign officials in non-OECD countries.

Deploy smart technology. Facilitating arm's-

length relationships between officials and civil society can eliminate many of the illicit transactions that result from direct contact.¹⁸ Online platforms have been particularly successful in public procurement, one of the most fertile sources of corruption, where state purchases of goods and services can amount in most countries to between 10 and 25 percent of GDP. Because awarding contracts can involve bureaucratic discretion, more countries are counteracting the histories of graft, kickbacks, and collusion in public procurement through procedures that guarantee openness, competition, a level playing field for suppliers, and clear bidding procedures.

Consultation and the role of women. Development programs have long tended to see women as passive recipients of help. While the strategies underlying traditional approaches have sought to improve the treatment of women and their objective circumstances, Sen argues that, through consultation, women are seen as agents of change, as "dynamic promoters of social transformation," who effect change in the lives of all members of society. Beyond the benefits for women themselves, the widespread involvement of women in the economic, social, and political life of the nation is vital in fighting corruption, given the evidence that women workers are less prone to corruption and nepotism than men. The criminology research literature has long established that "male criminal participation in serious crimes at any age greatly exceeds that of females, regardless of the source of data, crime type, level of involvement or measure of participation."¹⁹

Strengthening Moral and Ethical Standards

In his examination of bribery through the ages, Noonan observes that "the common

good of any society consists not only in its material possessions but in its shared ideals. When these ideals are betrayed, as they are betrayed when bribery is practiced, the common good, intangible though it be, suffers injury.”²⁰ Experts may insist on disguising bribery and corruption in the language of costs and benefits and economic choices, but we ignore their obvious moral dimension at our peril and at the cost to society when efforts to limit their corrosive effects are compromised.

We ignore their obvious moral dimension at our peril and at the cost to society when efforts to limit their corrosive effects are compromised.

Corruption has by now been criminalized in virtually every country on the planet, although enforcement of the laws condemning it may be weak.²¹ There is little doubt that bribery is regarded everywhere as a perversion, requiring secrecy, deception, and the use of euphemisms (gifts, contributions) by the guilty when exposed. Bribery interacts with power.²² However, a plutocracy, in which wealth and money rule, is not likely to be sustainable, as it inevitably generates opposition, even revolution. Those who pay bribes understand this, do not advertise their actions, and act furtively on the margins of morality. As Noonan puts it, “When government officials act to enrich themselves they act against the fabric on which they depend, for what else does government rest upon except the expectation that those chosen to act for the public welfare will serve that welfare?”²³

It is not enough to change ill-conceived or outdated rules, close loopholes, offer incentives, and devise harsh punishments. A strategy based solely on the design of bet-

ter rules and harsher punishments can be expensive and inefficient; first, because of the need to build a credible enforcement infrastructure to catch and deal with offenders; second, because it pits regulators and practitioners in a cat-and-mouse game. When the stakes are high, the mice are often well equipped to win, and the underpaid cats are overstretched and outsmarted. The 2008–2009 global financial crisis revealed huge gaps in the regulation of the “shadow” banking system (hedge funds, investment banks, and other off-balance sheet vehicles) but also showed that poorly paid regulators are no match for the creativity of bankers willing to stretch the rules in an effort to disguise reality and boost short-term profits.

One might reasonably assume that when budgets are approved and executed with clear rules and transparent procedures, they are less likely to be abused for personal enrichment. But they are far more likely to be effective if they are supported by efforts to strengthen the moral and ethical foundations of human behavior. In the long term, moral education and the strengthening of the ethical principles underpinning society must accompany anti-corruption strategies. A fine example is the attempt by the World Health Organization (WHO) to create a framework for better governance in the pharmaceutical sector of its member countries. The global pharmaceutical market is worth some US\$600 billion per year, and the industry is rife with opportunities for abuse and corruption from the conduct of clinical trials to the filing of patents, licensing of establishments, sale and distribution, public procurement, and prescriptions, to name a few. The WHO program aims not only to reduce corruption through the application of transparent, accountable administrative procedures but also to “*promote ethical practices* [emphasis added]” by identifying four key values to underpin the framework for

good governance in the sector: justice, truth, service to the common good, and trusteeship. In addition, it calls for explicit training of officials to ensure their understanding of the role of such values in the operation of the sector.²⁴

Moral education and the strengthening of the ethical principles underpinning society must accompany anti-corruption strategies.

To achieve this, the civic responsibility component of secular education requires reinforcing. Religious leaders, who bear such heavy responsibility for the decline of religion as a force for social cohesion, must set aside sectarian differences and, instead, emphasize the ethical and moral roots of their respective faiths, so they can help individuals and societies identify more strongly with the spiritual, rather than the material, dimensions of human nature. This will involve partnerships with all the organizations and social forces that have a solid ethical foundation.²⁵ The Sustainable Development Goals adopted by the United Nations in 2015 are a recent example of ethical principles of justice, solidarity and good governance applied to the challenges facing the world, and AIESEC, the international student organization, has put them at the center of its program planning. Many communities are encouraging their pre-adolescent youth in acts of community service to discover the rewards of altruistic action. School materials on values-based education are in increasing demand. Faith-based organizations have mobilized to respond to climate change and other social issues. With stronger underlying ethical standards, the struggle against bribery and corruption will be immeasurably reinforced and will complement recent

progress in improving the legal framework designed to combat them.

Notes

1. Tanzi, Vito. 1998. Corruption around the world: Causes, consequences, scope, and cures. *IMF Staff Papers*, 45(4):559–94.
2. The correlation coefficient between the rankings of 164 countries on Transparency International's latest Corruption Perceptions Index and the rankings on the *Doing Business* report's Ease of Doing Business Index is a very high 0.80. The more complex and inefficient the regulatory framework underpinning the activities of the private sector (as captured by the Doing Business indicators), the higher the level of corruption.
3. Myrdal, Gunnar. 1968. *Asian Drama: An Inquiry into the Poverty of Nations*. Pantheon.
4. The Foreign Corrupt Practices Act of 1977 forbids American businessmen and corporations from bribing foreign government officials, and imposes stiff penalties, including prison terms, on those engaged in the paying of illegal bribes. Because other OECD countries were not subject to such restrictions—in fact, the payment of bribes continued to be tax deductible in most other OECD countries, as a cost of doing business abroad—American companies began to complain that they were losing business to other countries. These developments gave considerable impetus to US government efforts to persuade other OECD members to ban bribery practices, leading in 1997 to the adoption of the OECD's Anti-Bribery Convention (see below).
5. Tanzi, op. cit.
6. Wei, Shang-Jin. 2000. How taxing is corruption on international investors? *Review of Economics and Statistics* 82(1): 1–11.
7. Mauro, Paulo. 1995. Corruption and growth. *The Quarterly Journal of Economics* (August): 681–712.
8. See Aghion, P. et al. 2016. Taxation, corruption, and growth. *European Economic Review*, 86:24–51; and Bentzen, J. S. 2012. How bad is corruption? Cross-country evidence of the impact of corruption on economic prosperity.

- Review of Development Economics*, 16(1):167–184.
9. Clausen, Bianca, Aart Kraay, and Zsolt Nyiri. 2011. Corruption and confidence in public institutions: Evidence from a global survey. *The World Bank Economic Review* 25(2): 212–249.
 10. See Ambraseys and Bilham. 2011. Corruption kills. *Nature*, 469:153–155.
 11. Rose-Ackerman, Susan and Bonnie J. Palifka. 2016. *Corruption and Government: Causes, Consequences, and Reform*, Cambridge University Press.
 12. Van Rijckeghem, Caroline, and Beatrice Weder. 1997. Corruption and the rate of temptation: Do low wages in the civil service cause corruption? IMF Working Paper 97/73. Washington, International Monetary Fund.
 13. See Pappa et al. 2015. Fiscal consolidation with tax evasion and corruption. *Journal of International Economics* 96:S56–S75.
 14. Sen, Amartya. 1999. *Development as freedom*. Oxford University Press.
 15. See Holcombe and Boudreaux. 2015. Regulation and corruption. *Public Choice*, 164(1–2):75–85.
 16. Rose-Ackerman, op. cit.
 17. Van Rijckeghem and Weder, op. cit.
 18. See Andersen et al. 2011. Does the internet reduce corruption? Evidence from US states and across countries. *World Bank Economic Review*, 25(3):387–417.
 19. From a study conducted by the National Academy of Sciences of the United States, cited in Swamy et al. 2001. Gender and corruption. *Journal of Development Economics*, 64(1): 25–55.
 20. Noonan, John T. 1984. *Bribes*. Macmillan Publishing Company, New York.
 21. For instance, the OECD’s 1997 Anti-Bribery Convention committed its members to “take such measures as may be necessary to establish that it is a criminal offence under its law for any person intentionally to offer, promise or give any undue pecuniary or other advantage, whether directly or through intermediaries, to a foreign public official.”
 22. See Bobonis et al. 2016. “Monitoring Corruptible Politicians.” *American Economic Review*, 106(8):2371–2405.
 23. Noonan, op. cit., p. 704.
 24. Anello, Eloy. 2008. A framework for good governance in the public pharmaceutical sector. Working draft for field testing and revision. April. World Health Organization.
 25. See Dixit, 2015. How business community institutions can help fight corruption. *The World Bank Economic Review*, 29 (suppl_1):S25–S47.