

# ANALYZING CORRUPTION THROUGH AN INTERNATIONAL EVALUATION

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## Abstract

*Corruption is a term carrying many different and complex interpretations. Corruption is difficult to detect and eliminate, because the both parties have a vital interest in concealing the matter. The fundamental difficulty with exposing an instance of corruption lies in the fact that its victims: individuals, institutions, competing companies, or the public at large, are usually unaware that such an abuse has taken place. Negative effects of corruption are often seen to play a central role on political legitimacy and institutional performance. Corruption in the public sphere is a particularly interesting and revealing area to study at the initial stage. In the literature the main explanations of what causes corruption can be divided into three categories: a) moral, b) functional and c) political-economic. Some international corruption scandals have fostered more attention to the corruption issues, not only in the countries, where the corruption level is rather high, but also in the countries that where regarded as almost free from corruption. Counteracting corruption requires actions in the following areas: prevention, education, and disclosure and elimination of corruptive practices. Finally, anticorruption strategies are related to the reform of state institutions.*

## 1. Introduction

Corruption is a term carrying many different and complex interpretations. It is commonly believed that corruption (from Latin *corruptio*, meaning depraved condition, state of decay or bribery) is one of the most dangerous social-economic and political diseases. The Oxford Reference Dictionary (1986) defines corruption as being “morally depraved, wicked; influenced by or using bribery”. Corruption is difficult to detect and eliminate, because the both parties have a vital interest in concealing the matter. All the participants give a high priority to maintaining confidentiality and taking any precautions necessary. The fundamental difficulty

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with exposing an instance of corruption lies in the fact that its victims: individuals, institutions, competing companies, or the public at large, are usually unaware that such an abuse has taken place. The victim, therefore, makes no attempts to prosecute a claim, the incident is undetected, and any countermeasures are greatly obstructed. Negative effects of corruption are often seen to play a central role on political legitimacy and institutional performance. Corruption in the public sphere is a particularly interesting and revealing area to study at the initial stage. "Corruption is behavior which deviates from the formal duties of a public role because of private-regarding (personal, close family, private clique) pecuniary or status gains; or violates rules against the exercise of certain types of private-regarding influence" (Nye 1967: 418). Corruption is commonly also defined as misappropriation of government property or revenues made possible through government regulation: "the sale by government officials of government property for personal gain" (Shleifer and Vishny).

Corruption has been used in various spheres and can also be defined in many different ways, as it been written above, but each definition misses some aspects. The most common definition of corruption using the above-mentioned looks, as the following – taking advantage of public office for personal or other political interests. However, economists deal with the meaning of corruption as a public economic policy issue. In this context corruption undermines the state's capacity to carry out its nominated functions in the economy (regulation, rule setting and enforcement; redistribution of income; stabilization of economy). Using this context, it can be easily seen, that economic policy distortions and weak state institutions provide such environment that is conducive, leads to corruption. For example, where the borders and the markets between the states are not clear and are not properly regulated, distinctions between what is public and what is private are obscured and corrupt behavior may ensue. In the same way, regulations invite economic agents to find ways, including bribing public officials, to secure favorable interpretations. Also exchange and trade restrictions tend to breed informal, frequently corrupt channels for a market-induced transaction. In this sense, statements that link corruption to economic performance are essentially statements about the link between structural/policy distortions and economic performance.

In the literature the main explanations of what causes corruption can be divided into three categories: a) moral, b) functional and c) political-economic. The last one of these traditional explanations can be subdivided into two categories. One deals more with macro-level explanations and the other one is more oriented towards micro and rational-choice oriented explanations.

There are various methods for combating corruption. On one hand they are similar, but on the other they have some national differences, due to cultural traditions. "Combating corruption is like judo. Instead of bluntly resisting the criminal forces, one must redirect the enemy's energy to his own decay" (Lambsdorff and Nell 2006: 57).

## **2. International organizations and their work**

The struggle against corruption is becoming very actual in all countries and in the international level. Several of the major international organizations in economic and political sphere work in order to fight corruption. The United Nations' General Assembly took steps already in 1996 to combat corruption. The UN stated that the organization should examine the possibility of developing a legally binding instrument (United Nations 1997: 22). Due to this document member states dedicated themselves to carry out measures to combat various forms of corruption in international business transactions. The declaration specifically orders that the member states are supposed to punish bribery of foreign civil servants. Another known organization is the international chamber of commerce that focuses on improving corporate self-regulation programs. It encourages international business communities to fight actively corruption. The chamber has issued rules against corruption and published the manual to assist companies in this field (Brademas and Heimann 1998: 20).

Among the most distinction organizations, that work against corruption is Transparency International (TI). It has influenced public perception and its corruption perception index, rating countries has received much publicity. The Transparency International (TI) ranked 163 countries by Corruption Perceptions Index (CPI) in 2006. CPI is a composite index. This index tries to assess the degree to which public officials and politicians are involved in corrupt practises. Its method has some limitations; it is based on the perception of business people, risk analysts, investigative journalists and the general public. Despite this, the index is one of the best available approximations for the level of corruption. Because the index is based on polls, the final results are subjective and at some extent are less reliable for countries with fewer sources. Also there are differences between countries: for example a matter viewed as acceptable tipping in one country may be considered as bribery in another. Therefore the poll results are supposed to be understood very specifically, measuring mostly public perception, rather than presenting an objective measure of corruption. The scores range from 10 (squeaky clean) to 0 (highly

corrupt). A score 5.0 is the number TI that considers the borderline figure distinguishing countries, which other have or do not have serious corruption problems. Illustration of this can be seen in the Table 1.

**Table 1. The Corruption Perceptions Index for the countries of the Baltic Sea Area (by the water drainage)**

Country	2004 CPI Score	Country rank 2004	2005 CPI Score	Country rank 2005	2006 CPI Score	Country rank 2006
Finland	9.7	1/146	9.6	2/159	9.6	1/163
Denmark	9.5	3/146	9.5	4/159	9.5	4/163
Sweden	9.2	6/146	9.2	6/159	9.2	6/163
Norway	8.9	8/146	8.9	8/159	8.8	8/163
Germany	8.2	15/146	8.2	16/159	8.0	16/163
Estonia	6.0	32/146	6.4	27/159	6.7	24/163
Lithuania	4.6	45/146	4.8	44/159	4.8	46/163
Czech Republic	4.2	51/146	4.3	47/159	4.8	46/163
Latvia	4.0	57/146	4.2	51/159	4.7	49/163
Slovakia	4.0	58/146	4.3	47/159	4.7	49/163
Poland	3.5	69/146	3.4	70/159	3.7	61/163
Belarus	3.3	74/146	2.6	107/159	2.1	151/163
Russia	2.8	95/146	2.4	126/159	2.5	121/163
Ukraine	2.2	128/146	2.6	107/159	2.8	99/163

**Source:** The 2004; 2005; 2006 Transparency International Corruption Perceptions Index

In 2004, Estonia stood at the 32<sup>nd</sup> place among ranked 146 countries by the Transparency International's CPI (6.0 points) and in 2006 the situation has been improved the 24<sup>th</sup> position among 163 countries (6.7 points). Our neighbour country Finland (9.7 points) was ranked as a least corrupt country, the first position and in 2006 was also on the same position with (9.6 points). Russia was on the 95<sup>th</sup> position in the ranking list by CPI (2.8 points), in 2006 has dropt this position and became 121<sup>st</sup> with (2.5 points). The other Baltic countries Lithuania took 45<sup>th</sup> place (4.6 points) and Latvia 57<sup>th</sup> place (4.0 points) in 2004, both countries have improved their positions and became on the 46<sup>th</sup> place (4.8 points) and 49<sup>th</sup> place (4.7 points) correspondently. During the last three years (2004 to 2006) almost all countries presented in the Tab.1 more or less have the stable position of CPI.

Organization for Economic Cooperation and Development (OECD) has started its work against corruption in international business in 1989 under the initiative of the United States. During the period from 1994 till 1996

Recommendations on Bribery in International Business Transactions and the Tax Deductibility of Bribes to Foreign Public Officials were worked out. Probably the most significant achievement internationally has happened in 1997 by signing of the OECD (Organization for Economic Cooperation and Development) Convention on Combating Bribery of Foreign Public Officials. Representatives of 34 nations have signed the Convention (Eizenstat 1998: 4). This convention is a major achievement for the rule of law for international business. One of the priority issues for the OECD is ethics and standards in the public sector. Through its Public Management Programme (PUMA) the OECD supports and facilitates the efforts of the member countries to achieve higher standards of effective and good governance (OECD – PUMA 2001).

The Council of Europe is another actor that plays an important role in struggle against corruption. In 1995 a program to combat corruption was worked by the Multidisciplinary Group on Corruption, and in 1999 the Group of States Against Corruption (GRECO) was established. The aim of the Group was to work out the agreement for the members of the European Union to fight the corruption using the program that was worked out earlier.

The U.S. Agency for International Development (USAID) is one of the important and prime government agents in the efforts to combat with corruption in the international business (Atwood 1998). Various international institutions (WTO, the World Bank, the IMF and others) are also playing very important role in the struggle process against corruption. During the last years the various research project were undertaken in these institutions that followed by publications. For example, Huang and Wei also Arvis and Berenbeim found that pegged exchange rates (currency boards or dollarization) are typically not optimal in countries with serious corruption. Some of the most significant studies on corruption coming out of the IMF in recent years are collected in Abed and Gupta . Arvis and Berenbeim reported results of the research conducted by the World Bank and the Conference Board in East Asia. Government procurement contracts are one of the most important areas for generating immense opportunities for bribes, kickbacks, and other corruption phenomena. It is emphasized that “Only by pooling research and experience between public sector organizations, at the national and multilateral levels, and civil society, business and academia can best practices be widely determined and disseminated. Building effective anticorruption agencies is one priority area where progress is being made”(Pope and Vogl 2000: 6-9).

### **3. The concept of sustainable development**

Poor governance has hampered sustainable economic growth, development of private sector economic activity, and the reduction of social equity and poverty. Sustainable development is a term that nowadays is widely used by politicians. The concept of sustainable development is in the process of development; therefore the definition of the term is constantly revised. Sustainable development is about promoting an integrated approach. It includes economic, social and environmental objectives. Economic objectives include growth, efficiency and stability. Sustainability is a systemic concept, showing the continuity of economic, social, institutional and environmental aspects of human society. Sustainability affects every level of organization, starting from the local neighborhood to the entire planet. The original term was “sustainable development”; the Agenda 21 program of the United Nations adopted this term. There are various attitudes what aspects of life can be included in “sustainable development”. Despite differences, there are common principles in most charters or action programmers to achieve sustainable development, sustainability or sustainable prosperity. These include the following:

- dealing cautiously with risk, uncertainty and irreversibility;
- integration of environmental, social and economic goals in policies and activities;
- ensuring appropriate valuation, appreciation and restoration of nature;
- conservation of biodiversity and ecological integrity;
- ensuring inter-generational equity;
- equal opportunity and community participation/sustainable community;
- recognizing the global dimension;
- a commitment to best practice;
- no net loss of human capital or natural capital;
- the principle of continuous improvement
- the need for the good governance (Hargroves and Smith 2005).

There are three main types of sustainability: institutional; economical and financial; ecological. The main question for institutional sustainability may be formulated as the following: can the strengthened institutional structure continue to deliver the results of the technical cooperation to the ultimate end-users? Thinking about the results, as a matter of fact, they may not be sustainable. For example the planning unit strengthened by the technical cooperation ceases to have access to top-

management or is not provided with adequate resources for the effective performance after the technical cooperation terminated. Also institutional sustainability can be linked to the concept of social sustainability. Speaking about economical and financial sustainability we try answer for the question: can the results of technical cooperation continue to yield an economic benefit after the technical cooperation is withdrawn? Thus economic (distinct from financial) sustainability may be at risk, if the end-users continue to depend on heavily-subsidized activities and inputs.

The United Nations has declared a Decade of Education for Sustainable Development starting from January 2005. Individuals and organizations can join in sharing resources for creating a sustainable future. All development assistance should be implemented with the aim of achieving sustainable benefits. Ten key factors that influence sustainability development can be mentioned. Among them are: government policies; management and organization; financial and economic.

Any government, in order to reduce implementation costs of policy reforms and to make insignificant the risk of policy reversal, has to have the support of citizens for its policy reforms. Cottarelli and Giannini pointed out three by-now widely shared beliefs, namely that: (1) credibility of purpose is indeed the crucial problem to be confronted in the reform process; (2) any policy that aimed at being believed should be based on clear and relatively simple announcements against which to evaluate subsequent policy actions; (3) some form of delegation is likely to strengthen the credibility of the announced policy path (Cottarelli and Giannini 1997: 31). Recent studies have shown that the size of government remains high and the scope of government activities has not necessarily become appropriate - "As markets expand in transition economies, the size and scope of government should also be reformed (Gupta et al. 2003: 54). Failures to reform the role of government may be due to strong vested interests. Unfortunately, for some aspects of state governance (especially, connected with the influence of corruption) only qualitative data are generally available (Kaufmann et al. 2000). An important issue of the relationship between politicians and the state bureaucracy in determining policy decisions is recently studied by Alesina and Tabellini (2004) and by Huber and Shipan (2002).

High levels of corruption push entrepreneurs to underground and this is one of the main factors of the increasing role of the shadow economy in all countries. More commonly used definition of the shadow economy is: "...all economic activities that contribute to the officially calculated (or observed) gross national product but are currently unregistered" (Schneider and Enste 2000: 78). The interesting question, do labor market rigidities lead to more underground economic activities, is recently

studied by Anderberg - he found that underground economic activities are more strongly correlated with a commonly used index of unemployment protection than with effective tax rates (Anderberg 2003). The shadow economy and corruption are known to go always together and their impact on the economic growth cannot be underestimated (Vostroknutova 2003).

A distinction between the individual captor firms and influential firms is important to emphasize (Hellman et al., 2003). Influential firms tend to be inherited from the previous Communist system – large, still state-owned or formerly state-owned firms, having secure property rights and close formal and/or informal with the state officials and politicians. State capture can be interpreted as a clear form of corruption. Captor firms are likely to be large new private firms with no state owned predecessor, having less secure property rights and weaker ties to the state. Captor firms seek to purchase advantages (including individual protection for their own property and contract rights) directly from the state officials in an environment where state is not able to provide the public goods necessary for effective entry and competition. Quite clearly, state capture is associated with large social costs for the rest of the economy and generates gains only to captor firms. The authors found that the state capture generates micro-level gains for the captor firms in Russia, and this phenomenon leads also to a number of macroeconomic problems that impose negative externalities on the rest of the economy: lower SME growth; lower regional government revenues; lower public spending on social services.

### **Concluding Remarks**

Nowadays the world's economies become more globalized and domestic economies become more integrated, rising business crime rates in various regions are no longer a local problem. Thus, crime needs to be combated simultaneously on both the national and international level. Today economies shape cultures, as the value systems, attitudes, and rules of conduct and the principles applied in the business world trickle into other areas of social life. Also, the weaknesses and malfeasance of the business world tend to become a part of modern society.

The role of the state in the modern economy is increasing. Property rights, government's structures, measures, and rules of exchange are the fields where modern states establish rules for economic actors. States suppose to provide stable and reliable conditions under which firms organize, compete, cooperate, and exchange. There are a lot of political discussions on the content of laws, their applicability to given firms and markets, and also the extent and directions of state intervention into economy. They favor certain groups or firms. Some states have



greater capacities for intervention than others. It depends on the nature of the situation and the institutional history of the state.

In many countries lack of transparency of laws, and rules creates a fruitful ground for corruption. It can be noticed in transition countries. Laws or various regulations are written in a way leaving grounds for different interpretations. Rules are often confusing and some times are changed without proper public announcements.

Counteracting corruption requires actions in the following areas: prevention, education, and disclosure and elimination of corruptive practices. Prevention involves the removal of sources of corruption, especially by passing effective laws and promoting good initiatives by governments, central and local administration and non-governmental organizations. The goal is to clean up laws, regulations and procedures that encourage corrupt dealings. It is essential to eliminate legal loopholes, ambiguous regulations and to avoid situations, which enable officials to use complete discretion while making decisions. The public sector structure needs to be examined; a unified system for public procurement should be introduced.

Structural reforms help to improve economic governance and reduce the opportunities for rent-seeking behavior. Poor governance generally creates opportunities and incentives for corruption.

Any realistic strategy must be based on the principle that there are always two sides in a process. On one hand there are those who demand acts of corruption on the part of public sector employees and on the other hand there are public employees willing to perform these acts for a bribe. It means that demand and supply exist in a case of corruption. It can be pointed out that fight against corruption is often connected with the process of reforms. Therefore corruption will decrease only in those countries where governments are willing to substantially reduce some of their functions.

One of the advantages of the fundamental economic reform approach is that by linking anticorruption strategies to reform of economic policies and institutions, the fight with corruption can be seen as one of the issues concerning economic policy. Continuous economic reform aimed at reducing policy distortions and strengthening economic institutions are bound to reduce the opportunities for corruption, while progress in establishing an effective administrative and legal system and in creating a more open society is likely to facilitate detection of corruption behavior and raise the cost to those who may be engaged in it. Thus, anticorruption strategies are related to the reform process-taking place in government institutions.

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