

Topic 6: Corruption

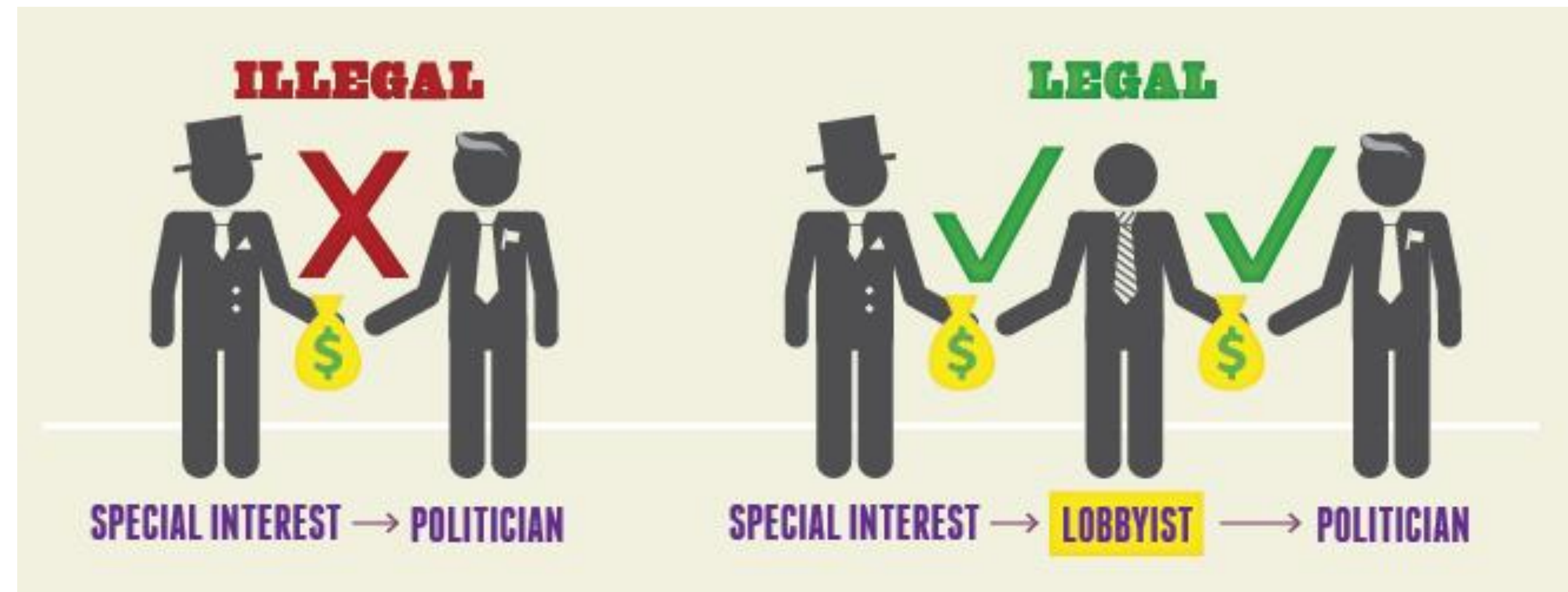


Definition of corruption

Corruption is the abuse of entrusted power for private gain.
Transparency International



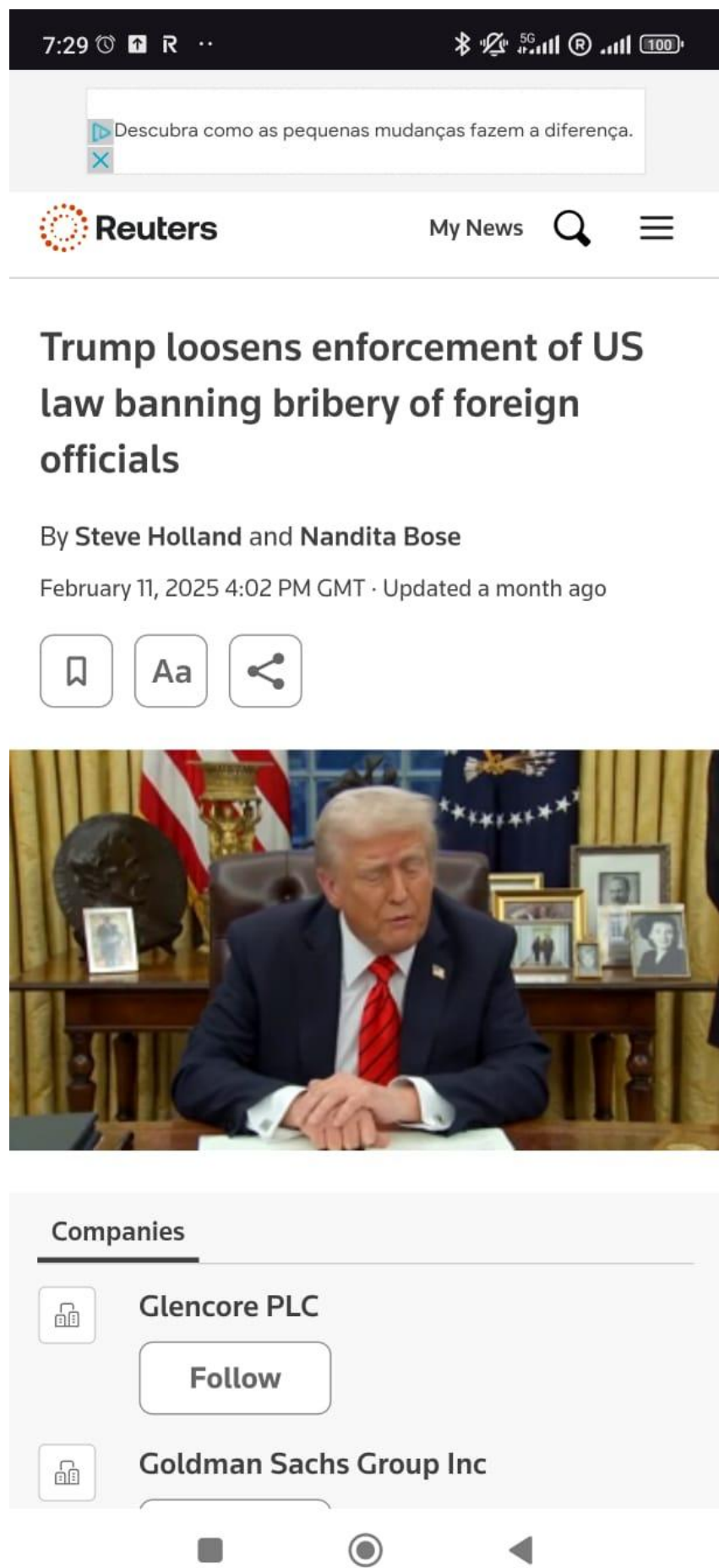
Teodorin Obiang, VP of Equatorial Guinea, son of the President, accused of buying a mansion and sports cars in France with public funds.



Lobbying is legal in the US

Is it always illegal?

Definition of corruption



Proposed Changes: The Trump administration is considering loosening enforcement of the U.S. law that bans bribery of foreign officials, potentially altering how the Foreign Corrupt Practices Act (FCPA) is applied.

FCPA Overview: The FCPA prohibits U.S. companies and individuals from bribing foreign officials to gain business advantages. It has been a cornerstone of anti-corruption efforts globally.

Potential Impact: Relaxing enforcement could lead to increased corruption risks and undermine international efforts to combat bribery. Critics argue it may give U.S. companies a competitive edge but at the cost of ethical standards.

Global Implications: Such changes could have significant implications for global anti-corruption policies and may influence how other countries enforce similar laws, potentially weakening international cooperation on corruption issues.

Is it always illegal?

Corruption: principal-agent

Corruption always arises in the context of a principal-agent relationship (Becker and Stigler, 1974).

The **Principal** is the party whose interest should be followed as the implicit or explicit rule.

The **Agent** is the party who is supposed to follow/implement the interests of the Principal.

Then there is a **Third Party** whose interests are different from the Principal's.

Corruption is transfer of value from the Third Party to the Agent, in exchange for going against the interests of the Principal, i.e., breaking the rule.

Examples of corruption

- Black market in price or supply-regulating contexts.
- The Barcenas' papers in Spains: Partido Popular's B account.
- Public services: health, police.
- Internal functions in bureacracy: data, documents.
- Political pacts and support.
- Narcotics traffic.
- Nepotism.

TELEF.:		OBSERVACIONES:		Hootlet	
FECHA		Entradas	Salidas		
10/99	R. Rato (2.º Semestre 99)		2.280.000		
11/99	M. Rajoy (2.º Semestre 99)		2.100.000		
	Paseo A.C. (2.º Semestre 99)		3.300.000		
	Jaime Mayor		2.100.000		
2.808		Entrada Salidas			
7/7	D. G. pedat 3.º trim. 2.500x3		7.500		
15/7	M. Rajoy 2.º Sem. 400x6		2.400		



Guinea-Bissau is a key transit point for the Latin American drug trade (archive image)

Authorities in Guinea-Bissau say they have seized 2.63 tonnes of cocaine that was found on a plane at the capital's international airport.

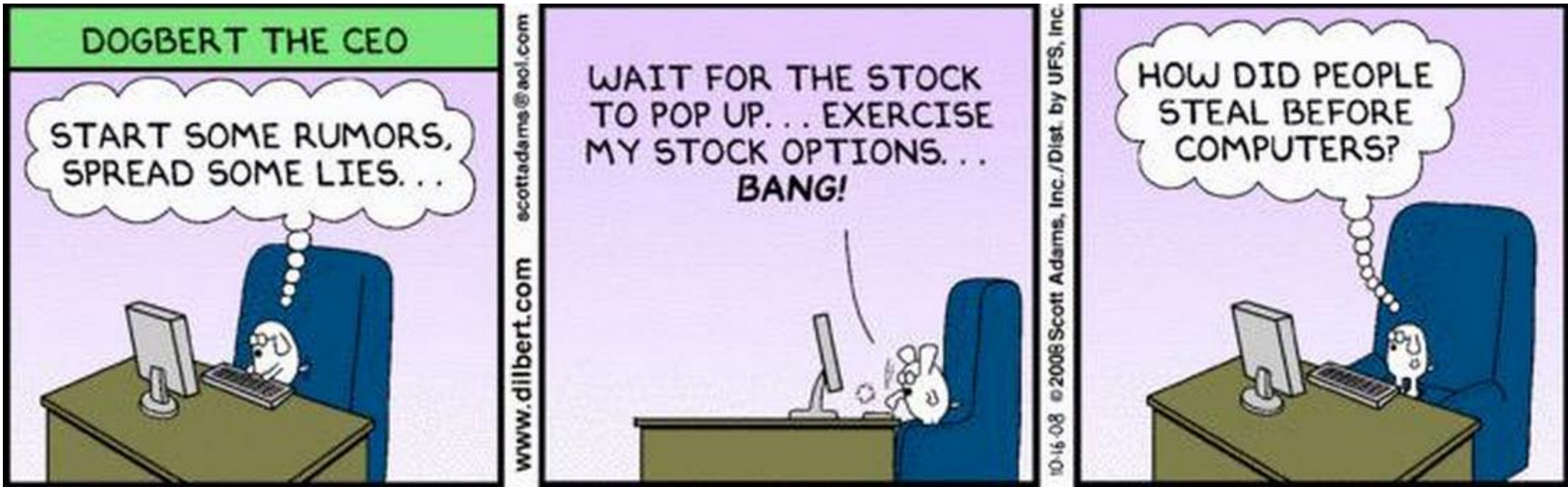
Definition of corruption: does it always involve a public official?

Corruption typology

POLICY	PERSONNEL	BEHAVIOUR & OPERATIONS
<div>1. Bias in domestic policing strategies</div> <div>2. Improper allocation and distribution of funds</div> <div>3. Political interference</div> <div>4. Influence of interest groups</div> <div>5. Penetration by organised crime</div> <div>6. Reaching performance targets</div> <div>7. Purposefully weak oversight</div>	<div>13. Poor leadership behaviour</div> <div>14. Nepotism in payroll, promotions, appointments</div> <div>15. Theft from salary chain</div> <div>16. Weak values and standards</div> <div>17. Criminal activities</div> <div>18. Personal problems (drugs, gambling, being blackmailed..)</div> <div>19. False personal asset declarations</div> <div>20. Biased rotations</div>	<div>24. Evidence tampering or theft</div> <div>25. Small bribes from public</div> <div>26. Uncontrolled operational independence</div> <div>27. 'Noble cause'</div> <div>28. Levying illegal fines</div> <div>29. Disclosure of privileged information</div> <div>30. Misuse of informants</div> <div>31. Discriminating behaviour</div> <div>32. Extortion</div> <div>33. Lack of officer identification</div> <div>34. Inaction due to 'Bonds of loyalty'</div>
FINANCE	PROCUREMENT	
<div>8. Improper asset disposals</div> <div>9. Purposefully weak financial control</div> <div>10. Illegal private activity</div> <div>11. Providing private security</div> <div>12. Facilitation payments</div>	<div>21. Bias in technical requirements</div> <div>22. Improper contract award or delivery</div> <div>23. Misuse of confidential tenders</div>	

CurbingCorruption.com

When a CEO follows private interest against the interests of the company's stakeholders.



Petty corruption vs. grand corruption



Working paper 564

Informal payments in the public health sector in Guinea-Bissau

Nichola Kitson

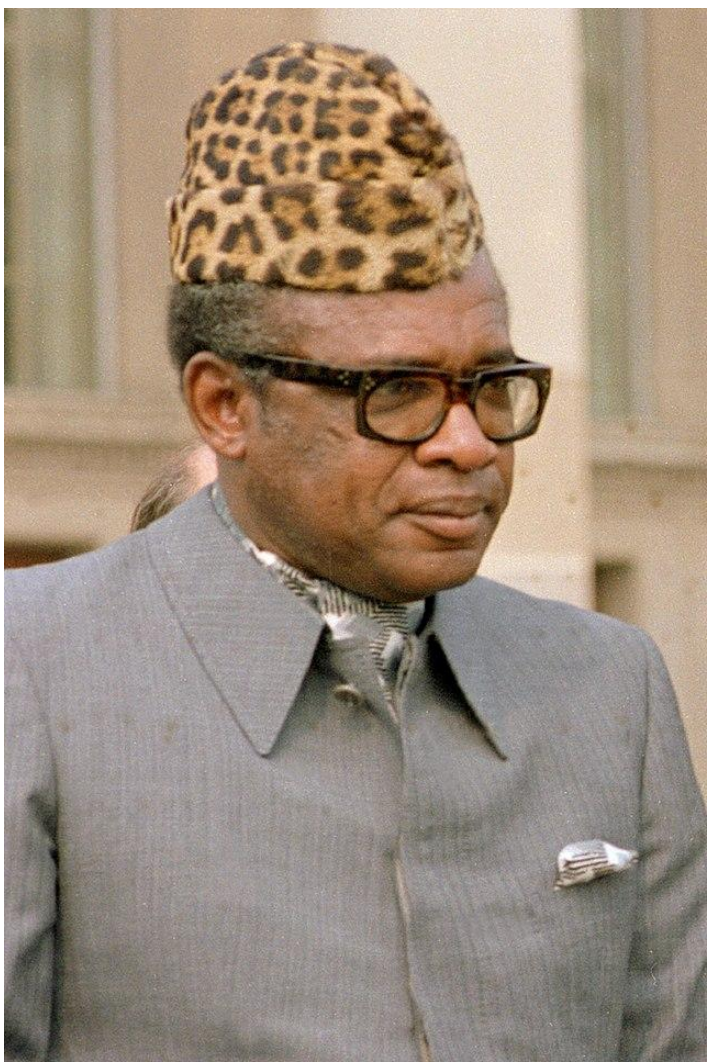
October 2019



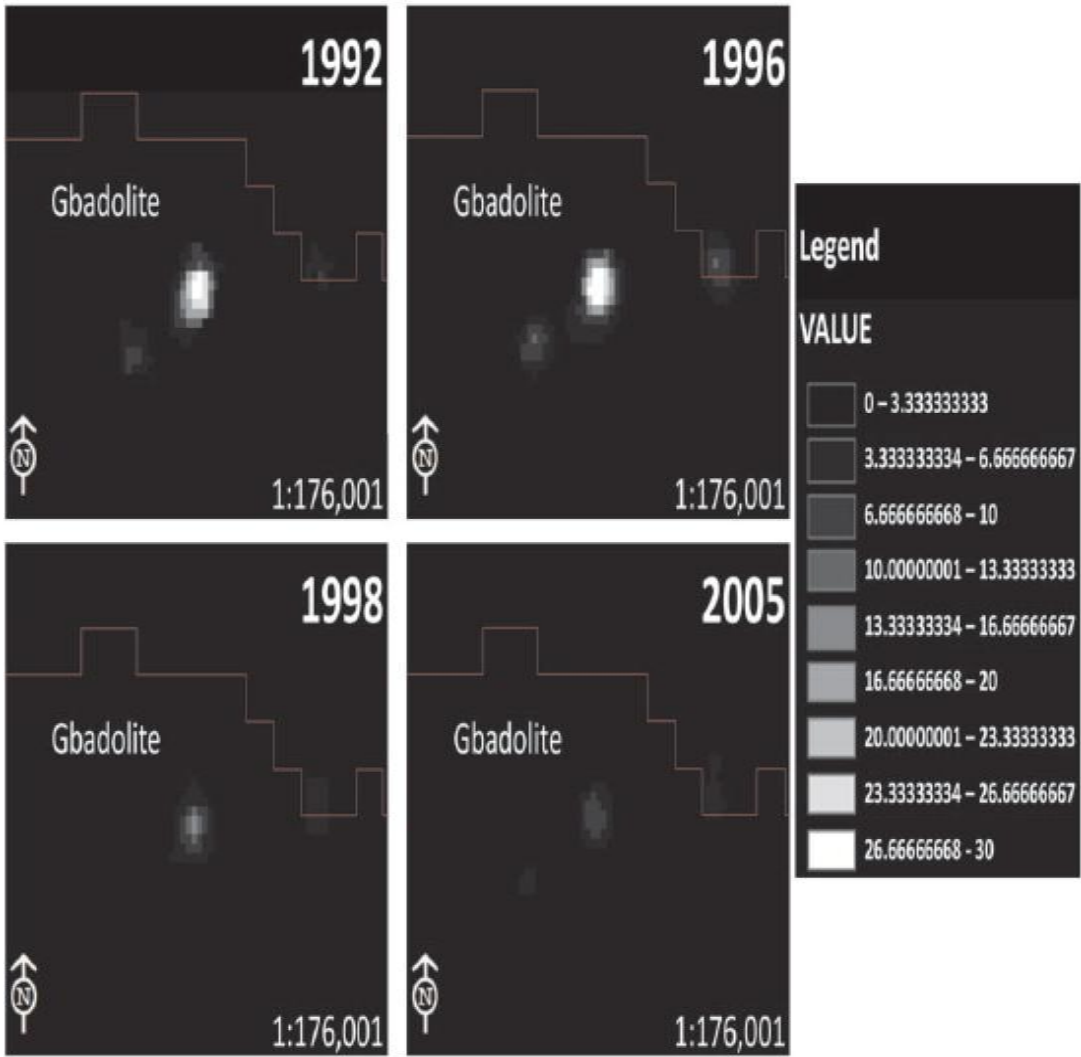
- Informal payments are widespread in the health sector in Guinea-Bissau. They impact negatively on equity and introduce distortions that are sub-optimal from the point of view of efficiency and quality. In the worst cases, treatment may be withheld or deliberately delayed with a view to soliciting informal payments, sometimes with catastrophic results for the patient.
- Informal payments in the health sector in Guinea-Bissau fall into four categories: solicited unofficial salary supplements; cost-contribution payments; genuine and faux nepotism; and unsolicited donations.
- Factors influencing the prevalence of informal payments include low remuneration and demotivated health workers; asymmetries of information and power; a culture of demanding informal payments; and a lack of accountability.
- In view of the political environment in Guinea-Bissau, this paper advocates for experimental and incremental approaches to tackle informal payments. These approaches should be monitored and evaluated by a coordinating body of reform champions, in particular by a scaled-up Health Worker Forum, accompanied by measures to increase knowledge and awareness of those using the health service. There is also a need to start a dialogue on issues via an in-country health financing conference.



Sector de São Domingos, north of Guinea Bissau



Gbadolite, DRC (hometown of Mobutu Sese Seko)



Hodler and Raschky (2014, QJE)

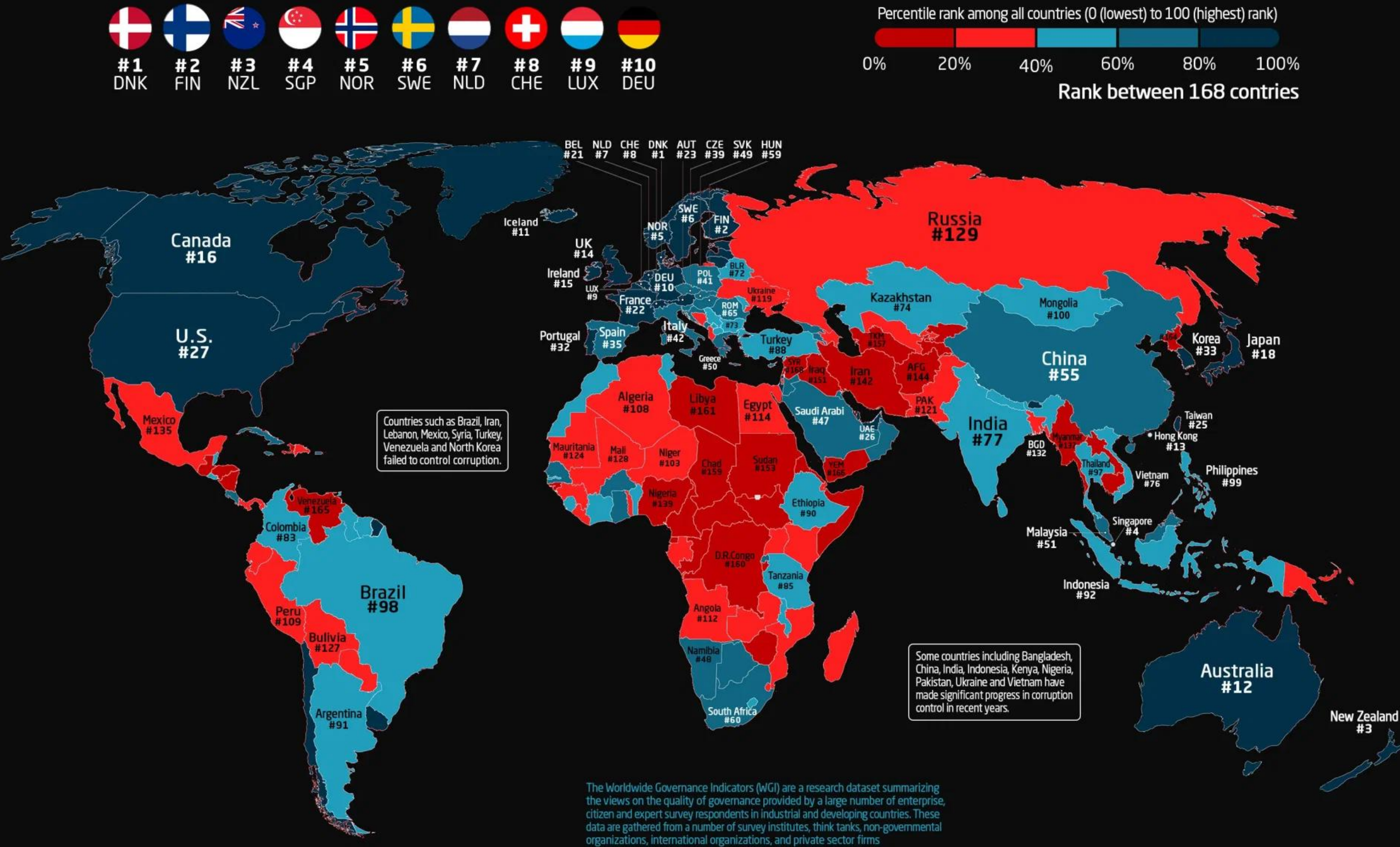
Before Mobutu's rule, Gbadolite was a small community with less than 2,000 inhabitants. Mobutu, who was born in the nearby area, invested heavily in transforming his ancestral home into a symbol of wealth and power. He built three large palaces, an international airport capable of accommodating the Concorde, a five-star hotel, a hospital, and various infrastructure projects

Corruption perceptions

The Worldwide Governance Indicators (WGI) compile data reflecting perceptions of governance quality from diverse sources, including surveys of enterprises, citizens, and experts in both industrialized and developing nations.

CORRUPTION CONTROL in the Worldwide Governance Indicators 2022

Control of corruption captures perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as “capture” of the state by elites and private interest.



Can corruption grease the wheels?



Bypassing regulations/high regulatory costs:
business can circumvent burdensome regulatory environments => more efficiency and productivity.

Measurement of corruption: Public Expenditure Tracking Surveys (PETS)

Objective: To track and evaluate the efficiency and effectiveness of public expenditures, especially in rural areas, by identifying areas of concern and impediments in resource flows.

Methodology: PETS involve extensive mapping exercises to understand fund flows through different government levels. They collect and analyze budget data, often complemented by facility surveys and qualitative research.

Applications: PETS are used to monitor specific programs or public spending in targeted districts and regions. They help civil society organizations and policymakers understand funding flows, identify areas of leakage, and make informed policy decisions.

- **Examples:** In countries like Ghana, Zambia, and Chad, PETS have revealed significant leakage rates in non-wage expenditures, highlighting the need for improved tracking and accountability⁴.

- **Civil Society Role:** Civil society organizations use PETS to monitor government programs, ensuring that funds reach intended beneficiaries and improving service delivery

PETS – Reinikka and svensson 2004 – 1

Focus on a large public educational program in Uganda - a capitation grant to cover schools' nonwage expenditures - financed and run by the central government, using district offices as distribution channels.

Comparison of disbursed flows from the central government (intended resources) with the resources actually received by schools.

250 primary schools were surveyed and data on receipts were collected for 1991-1995.

According to official statistics, 20 percent of Uganda's total public expenditure was spent on education in the mid-1990s, most of it on primary education. One of the large public programs was a capitation grant to cover schools' nonwage expenditures. Using panel data from a unique survey of primary schools, we assess the extent to which the grant actually reached the intended end-user (schools). The survey data reveal that during 1991–1995, the schools, on average, received only 13 percent of the grants. Most schools received nothing. The bulk of the school grant was captured by local officials (and politicians). The data also reveal considerable variation in grants received across schools, suggesting that rather than being passive recipients of flows from the government, schools use their bargaining power to secure greater shares of funding. We find that schools in better-off communities managed to claim a higher share of their entitlements. As a result, actual education spending, in contrast to budget allocations, is regressive. Similar surveys in other African countries confirm that Uganda is not a special case.

PETS – Reinikka and Svensson 2004 – 2

Reinikka and Svensson find that, on average, schools received only **13 percent of central government spending on the program**. Most schools received nothing; the bulk of the grants was captured by local government officials (and politicians).

They also find large variations in grants received across schools: actual spending, unlike budget allocations, is regressive, as schools in better-off communities experience a lower degree of capture.

This is suggestive of a bargaining model between schools and local officials: **the poor seem to be harmed by corruption**.

PETS – Reinikka and svensson 2004 – 3

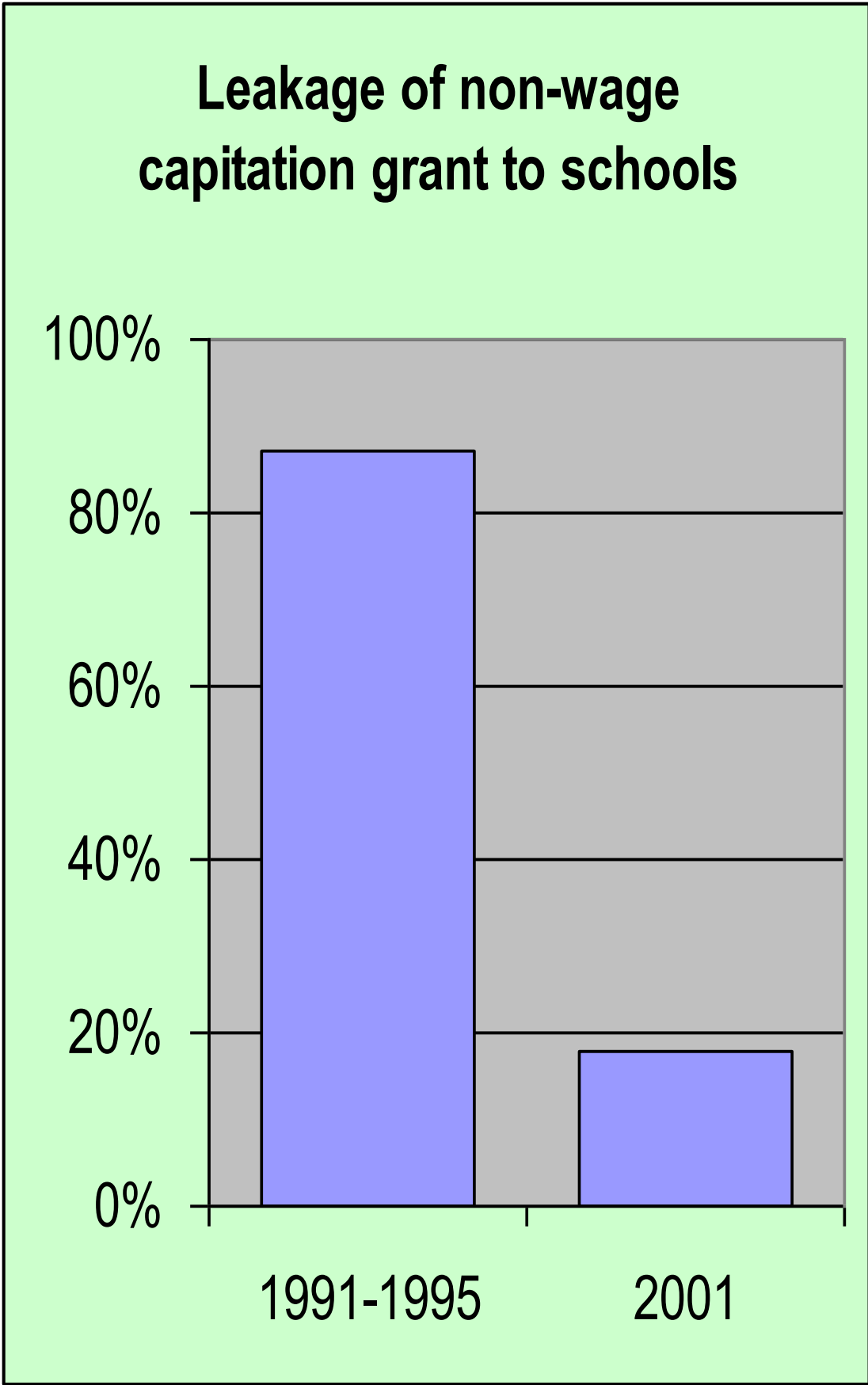


TABLE III
CAPTURE OF NONWAGE FUNDS IN PRIMARY EDUCATION: EVIDENCE FROM PUBLIC EXPENDITURE TRACKING SURVEYS IN SUB-SAHARAN AFRICA

Country	Year	Expenditure program	Sample size	Capture (percent)
Ghana	1998	Nonwage spending in primary education (multiple programs)	126	49
Tanzania	1998	Nonwage spending in primary education (multiple programs)	45	57
Uganda	1995	Per-student capitation grant	250	78
Zambia	2001	Fixed school grant	182	10
Zambia	2001	Discretionary nonwage grant program	182	76

a. GDP per capita is expressed in constant (1995) US dollars. Sample size is the number of schools surveyed. Capture is the share (in percent) of entitled funds not reaching the schools (average).
b. Source: Ye and Canagarajah [2002] for Ghana; Price Waterhouse Coopers [1999] for Tanzania; Das et al. [2002] for Zambia.

Major improvement in 2001 in Uganda: 18% capture.
PETS, transparency measures, awareness campaigns, capacity building

Challenges with PETS

However, PETS are not a magical solution:

- Expensive.
- Problems of reporting, unclear allocation rules for resources, in-kind transfers make PETS not fully reliable.
- Not a substitute for information systems or audits; better seen as a complementary tool.

Measurement of Corruption: Direct Observation

BARRON AND OLKEN 2007 - 1

Truck drivers in Aceh, Indonesia, make a variety of illegal payments, including payments to police and military officers to avoid harassment at checkpoints along the roads, payments at weigh stations to avoid fines for driving overweight, and protection payments to criminal organizations and the police.

Enumerators accompanied truck drivers along their regular routes to and from Aceh: from November 2005 to July 2006, 304 trips to and from Aceh, with more than 6,000 illegal payments directly observed along the routes.

ABSTRACT

This paper tests whether the behavior of corrupt officials is consistent with standard industrial organization theory. We designed a study in which surveyors accompanied truck drivers on 304 trips along their regular routes in two Indonesian provinces, during which we directly observed over 6,000 illegal payments to traffic police, military officers, and attendants at weigh stations. Using plausibly exogenous changes in the number of police and military checkpoints, we show that market structure affects the level of illegal payments, finding evidence consistent with double-marginalization and hold-up along a chain of vertical monopolies. Furthermore, we document that the illegal nature of these payments does not prevent corrupt officials from extracting additional revenue using complex pricing schemes, including third-degree price discrimination and a menu of two-part tariffs. Our findings illustrate the importance of considering the market structure for bribes when designing anti-corruption policy.

Measurement of Corruption: Direct Observation

BARRON AND OLKEN 2007 - 2

On average, drivers spent about USD 40 per trip, i.e., 13% of the total cost of a trip, on bribes, extortion, and protection payments.

Corrupt officials behave like profit-maximizer firms:

1. The average bribe paid in North Sumatra increased significantly in response to a reduction in the number of checkpoints in Aceh.
2. 'Downstream' checkpoints – i.e., those that are closest to the final destination – receive higher bribes than 'upstream' checkpoints.
3. Officials at checkpoints charge higher prices to those drivers with observable characteristics that indicate a higher willingness to pay (e.g., newer trucks).

Corruption Determinants and Deterrents

FISMAN AND MIGUEL (JPE, 2006) - 1

They develop an empirical approach for evaluating the role of both social norms and legal enforcement in corruption by studying parking violations among United Nations diplomats living in New York.

Natural Experiment:

Mission personnel and their families benefit from diplomatic immunity, a privilege that allowed them to avoid paying parking fines prior to Nov. 2002.

All else constant: diplomats/same demographic profile; same location (close to the UN building).

ABSTRACT

Corruption is believed to be a major factor impeding economic development, but the importance of legal enforcement versus cultural norms in controlling corruption is poorly understood. To disentangle these two factors, we exploit a natural experiment, the stationing of thousands of diplomats from around the world in New York City. Diplomatic immunity means there was essentially zero legal enforcement of diplomatic parking violations, allowing us to examine the role of cultural norms alone. This generates a revealed preference measure of government officials' corruption based on real-world behavior taking place in the same setting. We find strong persistence in corruption norms: diplomats from high corruption countries (based on existing survey-based indices) have significantly more parking violations, and these differences persist over time. In a second main result, officials from countries that survey evidence indicates have less favorable popular views of the United States commit significantly more parking violations, providing non-laboratory evidence on sentiment in economic decision-making. Taken together, factors other than legal enforcement appear to be important determinants of corruption.

Corruption Determinants and Deterrents

FISMAN AND MIGUEL (JPE, 2006) - 2

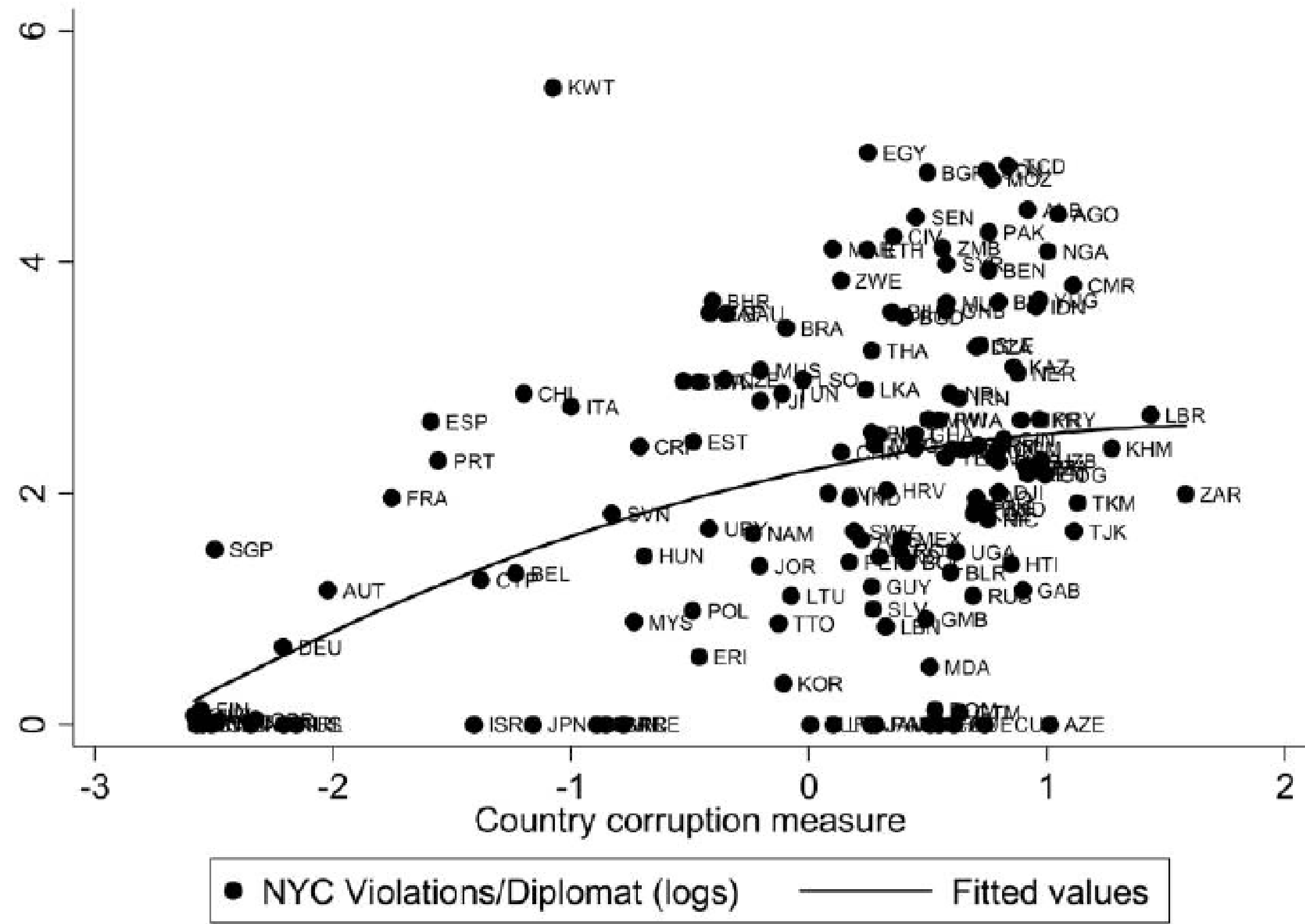
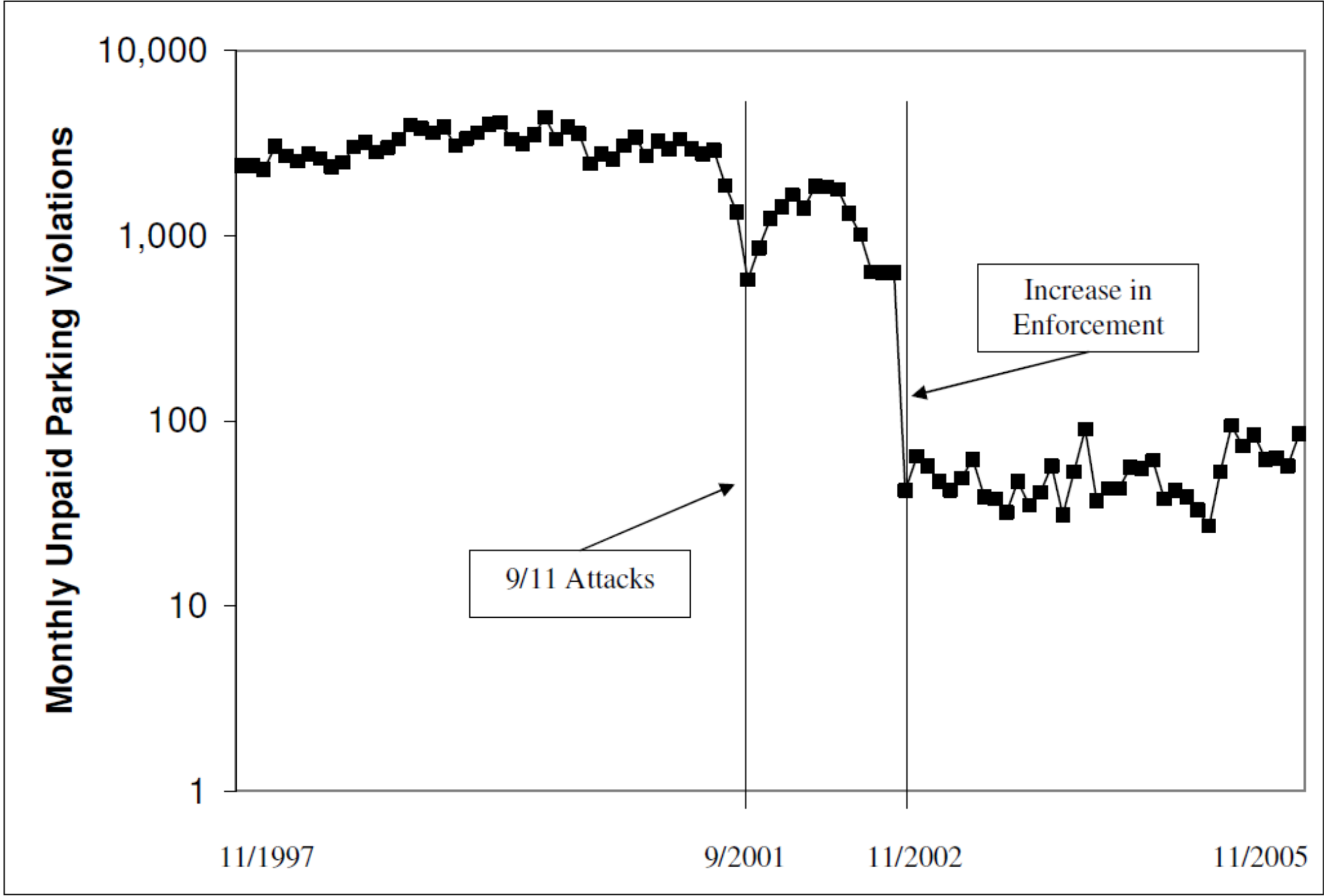


FIG. 2.—Country corruption and unpaid New York City parking violations per diplomat (in logs), pre-enforcement (November 1997 to November 2002). Country abbreviations are presented in table 1. The line is the quadratic regression fit. The y-axis is $\log(1 + \text{Annual NYC Parking Violations/Diplomat})$.

Corruption Determinants and Deterrents

FISMAN AND MIGUEL (JPE, 2006) - 3

Figure 1: Total Monthly New York City Parking Violations by Diplomats, 1997-2005 (log scale)



Corruption Determinants and Deterrents

FISMAN AND MIGUEL (JPE, 2006) - 4

Results:

Parking violation corruption measure is strongly positively correlated with other (survey-based) country corruption measures and that this relationship is robust to conditioning on region fixed effects, country income, and a wide range of other controls.

This suggests that home country corruption norms are an important predictor of propensity to behave corruptly among diplomats.

By exploiting the increase in the legal punishment for parking violations after Nov 2002, enforcement matters too: it led to immediate decline of approximately 98 percent in parking violations.

Evidence in favor of weak convergence to zero-enforcement with tenure in New York.

Is corruption efficient? Macro

MAURO 1995 - 1

First study providing evidence of a negative impact of corruption on economic growth, through a negative effect on investment.

Tries to distinguish causation from correlation, by exploring the (positive) relation between corruption and ethnolinguistic fractionalization (measuring the probability that two individuals drawn randomly from a country's population will not belong to the same ethnolinguistic group) – this was highly disputed methodologically.

CORRUPTION AND GROWTH*

PAOLO MAURO

This paper analyzes a newly assembled data set consisting of subjective indices of corruption, the amount of red tape, the efficiency of the judicial system, and various categories of political stability for a cross section of countries. Corruption is found to lower investment, thereby lowering economic growth. The results are robust to controlling for endogeneity by using an index of ethnolinguistic fractionalization as an instrument.

Is corruption efficient? Macro

MAURO 1995 - 2

TABLE I
BUREAUCRATIC EFFICIENCY INDEX

1 5-4 5	4 5-5 5	5.5-6 5	6 5-7 5	7.5-9	9-10
Egypt	Algeria	Angola	Argentina	Austria	Australia
Ghana	Bangladesh	Dominican Rep	Ivory Coast	Chile	Belgium
Haiti	Brazil	Ecuador	Kuwait	France	Canada
Indonesia	Colombia	Greece	Malaysia	Germany	Denmark
Iran	India	Iraq	Peru	Ireland	Finland
Liberia	Jamaica	Italy	South Africa	Israel	Japan
Nigeria	Kenya	Korea	Sri Lanka	Jordan	Hong Kong
Pakistan	Mexico	Morocco	Taiwan	Zimbabwe	Netherlands
Thailand	Philippines	Nicaragua	Uruguay		New Zealand
Zaire	Saudi Arabia	Panama			Norway
	Turkey	Portugal			Singapore
	Venezuela	Spain			Sweden
		Trinidad/Tobago			Switzerland
					United Kingdom
					United States

BE is the bureaucratic efficiency index, which I compute as the simple 1980–1983 average of three Business International indices: judiciary system, red tape, and corruption. A high value of the BE index means that the country's institutions are good.

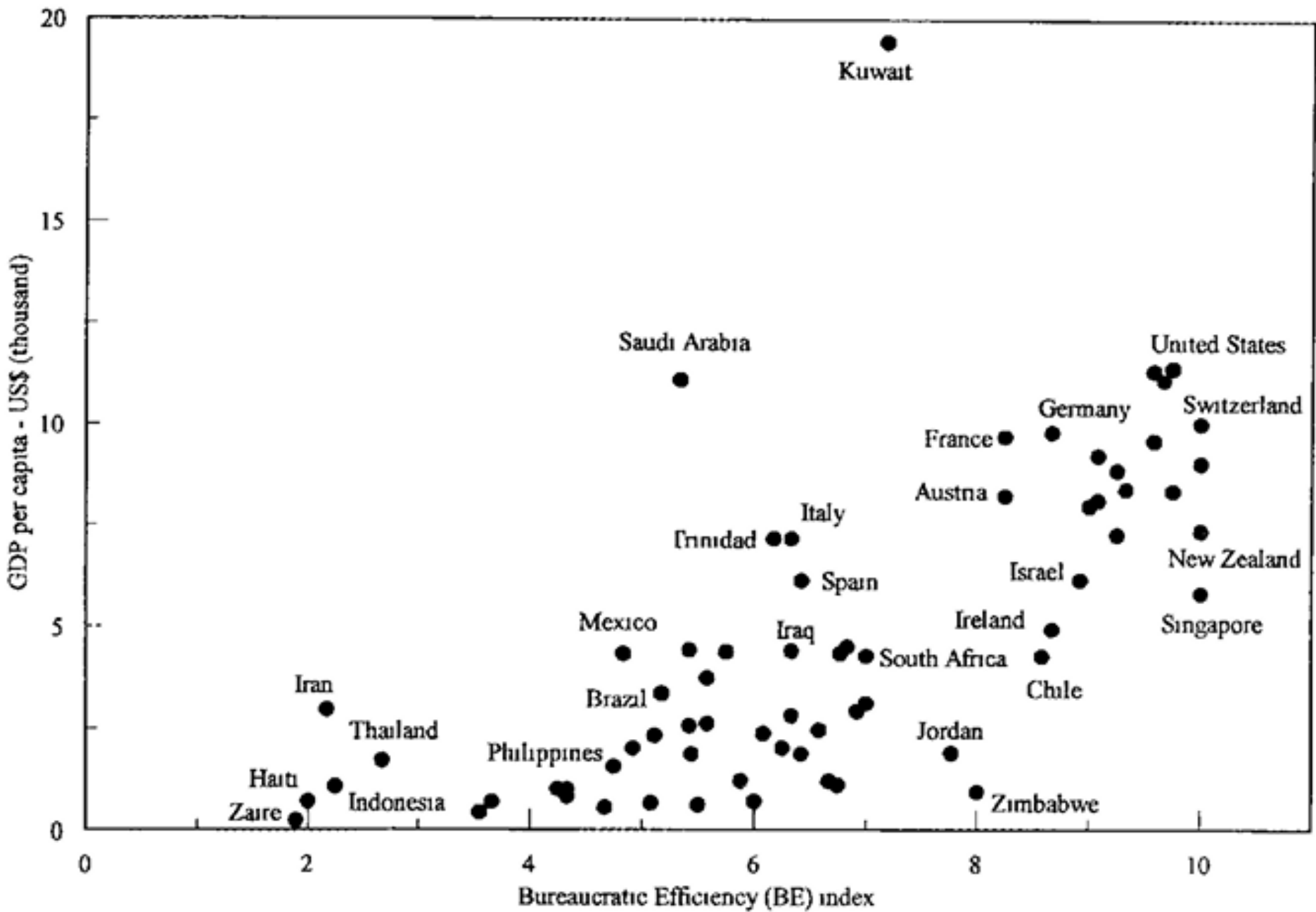


FIGURE I
Per Capita Income and Bureaucratic Efficiency
BE index is 1980–1983 average of BI indices of corruption, red tape, and judiciary
Per capita GDP at PPP in 1980 is from Summers and Heston [1988].
67 countries, $r = 0.68$

Is corruption efficient? Macro

MAURO 1995 - 3

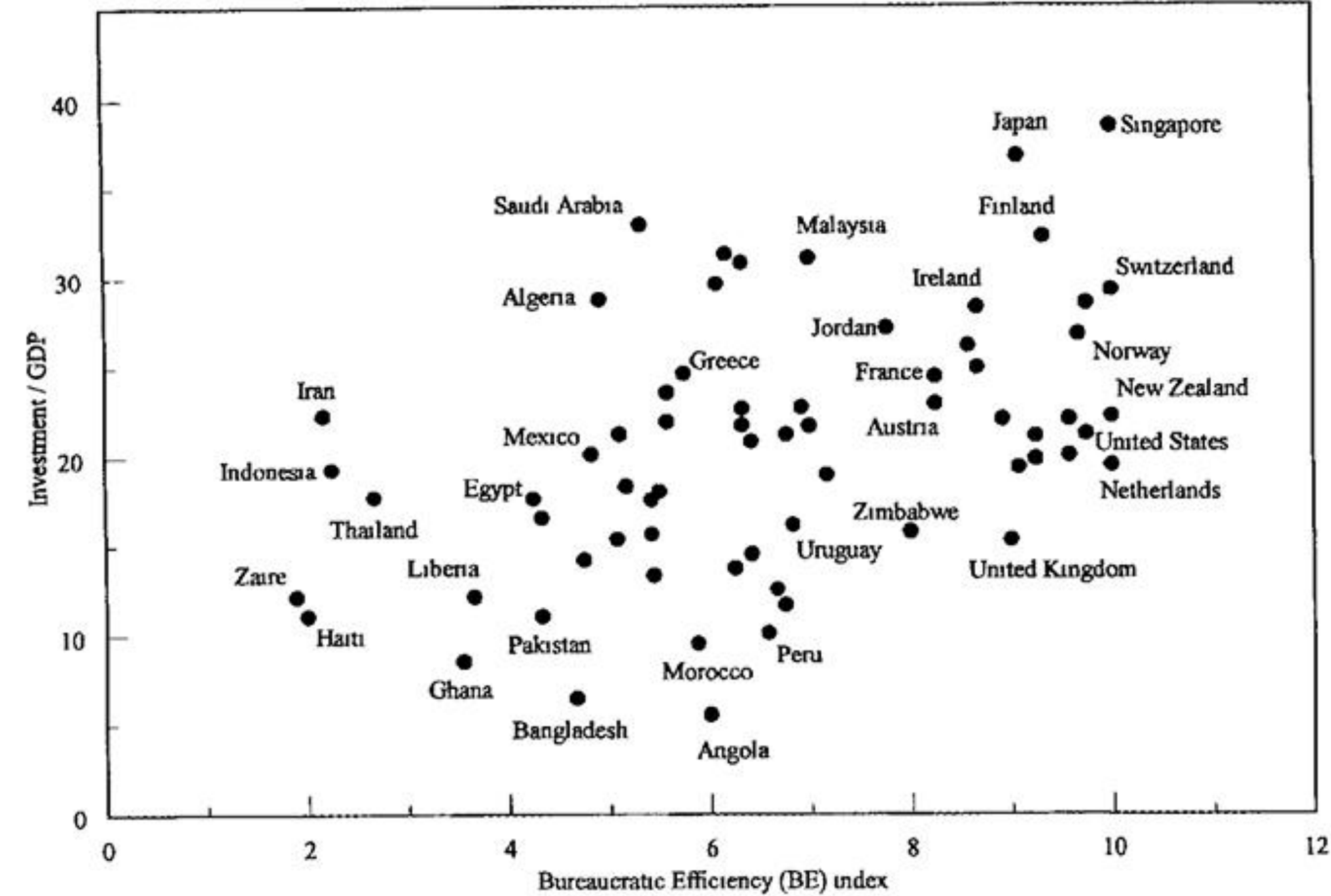


FIGURE II

Investment and Bureaucratic Efficiency

BE index is 1980–1983 average of BI indices of corruption, red tape, and judiciary.
Average investment 1980–1985 from Summers and Heston [1988].
67 countries, $r = 0.46$.

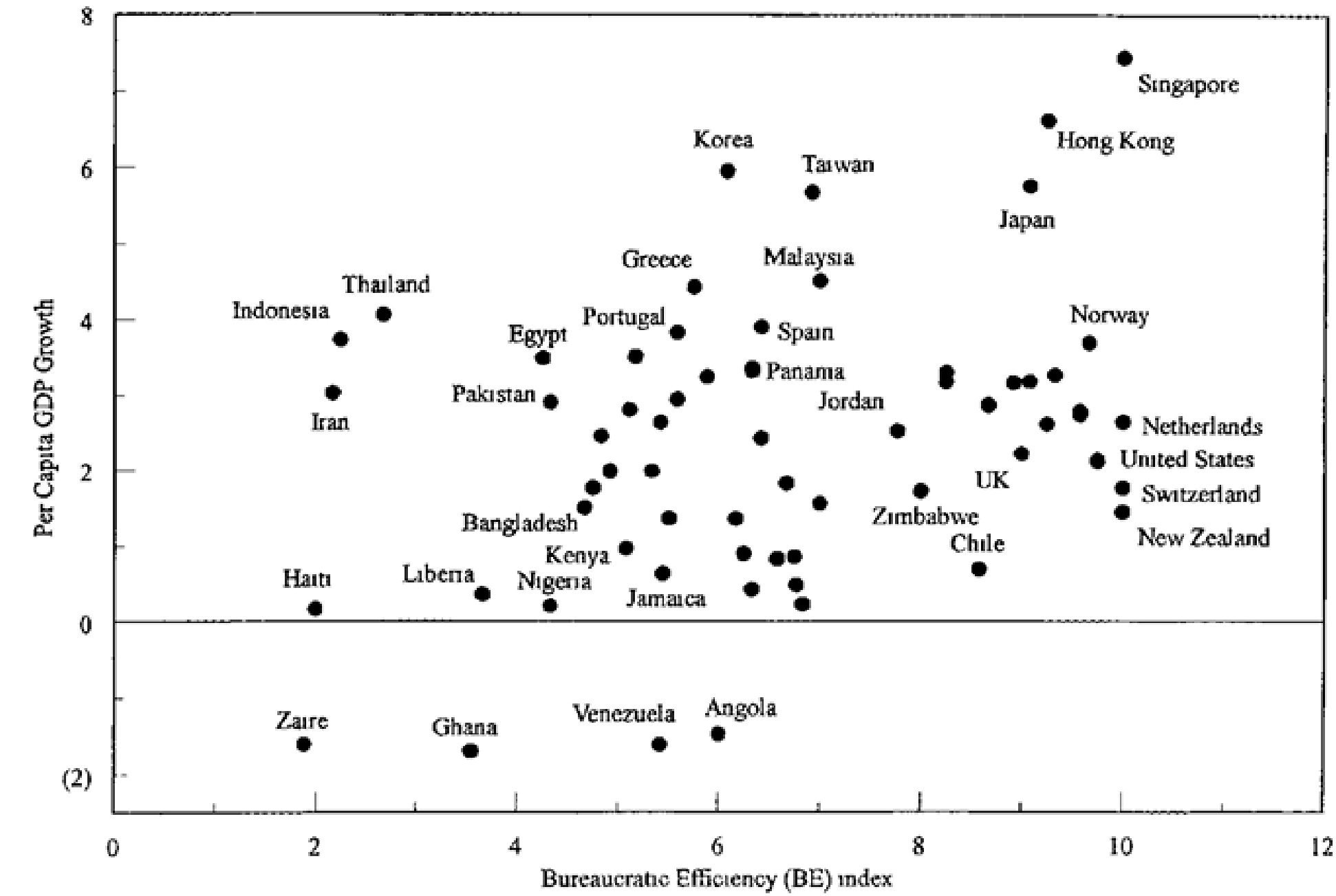


FIGURE III

Growth and Bureaucratic Efficiency

BE index is 1980–1983 average of BI indices of corruption, red tape, and judiciary
Average GDP per capita growth 1960–1985 from Summers and Heston [1988].
67 countries, $r = 0.32$

Is corruption efficient? Micro

BERTRAND, DJANKOV, HANNA, AND MULLAINATHAN (2007) - 1

Study follows a sample of applicants through the process of obtaining a driver's license in New Delhi (India).

Experimental setting (RCT) in which surprise independent driving tests were submitted to all participants – this was key for the derivation of welfare consequences of corruption.

Main research questions:

Can corruption be used to speed up the process of getting a license ('grease the wheels')?

Do bad drivers use bribes to get a license (social welfare question)?



Two facts on India: more than 146k deaths due to road accidents, 6 out of 10 licenses are given without a driver's test (2016).

Is corruption efficient? Micro

BERTRAND, DJANKOV, HANNA, AND MULLAINATHAN (2007) - 2

Design - three experimental groups of applicants:

1. Control
2. Bonus group: promise of financial bonus if license was got in 32 days or less.
3. Lesson group: free driving lessons.

Is corruption efficient? Micro

BERTRAND, DJANKOV, HANNA, AND MULLAINATHAN (2007) - 3

Bonus group very effective at getting license quickly: 42 percentage points more likely than control to get the license in 32 days or less.

But this fact could be due to corruption or more effort in learning how to drive...

Lesson group not effective at getting license quickly.

‘Grease the wheels’ confirmed.

Bonus group more likely to have bad drivers: 18 percentage points more likely to obtain license and fail independent test.

Is corruption efficient? Micro

BERTRAND, DJANKOV, HANNA, AND MULLAINATHAN (2007) - 4

Table 3: Obtaining a License

	Obtained License (all tracked) (1)	Obtained License (2)	Obtained a license in 32 days or less (3)	Obtained a License without taking Licensing Exam (4)	Obtained License & Did Not Have Anyone Teach Them to Drive (5)	Obtained License & Attended a Driving School (6)	Obtained License & Automatically Failed Ind. Exam (7)	Obtained License & Exam Score < 50% (8)
Comp. Group Mean	0.45	0.48	0.15	0.34	0.23	0.03	0.29	0.32
Bonus Group	0.24 (0.05)***	0.25 (0.05)***	0.42 (0.04)***	0.13 (0.05)***	0.29 (0.04)***	0.03 (0.02)	0.18 (0.05)***	0.22 (0.05)***
Lesson Group	0.12 (0.05)**	0.15 (0.05)***	-0.05 (0.04)	-0.03 (0.05)	-0.12 (0.04)***	0.35 (0.03)***	-0.22 (0.04)***	-0.18 (0.05)***
N	731	666	666	666	666	666	666	666
R^2	0.12	0.14	0.31	0.12	0.26	0.26	0.24	0.20
Fstat	14.24	13.50	87.60	7.48	61.38	52.83	64.48	51.12
P-value	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00

- Notes:
1. This table reports on the subjects' ability to obtain a license and their driving ability, by experimental group.
 2. Each column gives the results of an OLS regression of the dependent variable listed in that column on indicator variables for belonging to the bonus and lesson group. All regressions include session fixed effects, age, religion fixed effects, an indicator variable for marital status, an indicator variable for whether the individual had ever driven a two-wheeler prior to the project, and an indicator variable for whether the individual had ever driven a four-wheeler prior to the project. For ease of interpretation, the comparison group mean of the dependent variable is listed in the first row. The last two rows report the Fstat and pvalue for a test of the joint significance of the bonus and lesson group indicator variables.
 3. The sample in Column 1 includes all individuals whose final license status was ascertained by the program staff. Columns 2-8 include all individuals who both whose final license status was ascertained and who completed all relevant surveys.
 4. All standard errors are robust. Significance at 10% level is represented by a *, at the 5% level by a ** and at the 1% level by ***.

Policy implications: Transparency International



Let's look at Transparency International (TI).

International NGO founded in Berlin in 1993.

Today, prescribing three types of tools:

1. Integrity Pacts: for preventing corruption in public contracting, typically followed by TI local chapters.
2. Corruption Fighters' Toolkits: for activists/civil society (e.g., anti-corruption kit for young activists)
3. Business Principles for Countering Bribery: private sector.



Summary

Defining corruption is a normative exercise; importantly, corruption is not bad for social welfare by definition.

Measurement of corruption: perceptions (macro), missing money (e.g., PETS), or direct observation.

Corruption is correlated with poorer settings (PETS).

(In)efficiency of corruption:

1. (Macro) Clear negative correlation with investment and growth.
2. (Micro) In the allocation of driving licenses in India corruption 'greases the wheels' but decreases social welfare (experiment).

Solutions: challenging but possible! Olken (JPE 2007), Indonesian village infrastructure – audits and grass-root participation.

Thanks for your attention and contributions!