

International Business Corruption: A Framework of Causes, Effects, and Prescriptions

James P. Neelankavil
Professor of International Business
Zarb School of Business
Hofstra University
Telephone # 516 463 5336
E-mail: mktjpn@hofstra.edu

International Business Corruption: A Framework of Causes, Effects, and Prescriptions

Abstract

International business corruption affects adversely national economies as well as the international business environment. Some attempts have been made in the last two decades to resolve this complex problem. Though some success has been achieved, the problem is far from being totally eradicated. By identifying the key participants of corruption and by tracing the root causes of the problem, a set of prescriptive measures are suggested. These prescriptions are built on the works of other researchers who have investigated this area in the last twenty to thirty years. It is recognized that worldwide corruption is endemic and cannot be easily eradicated. But, can it be reduced to make the international business operations more efficient?

Introduction

Corruption is not a new phenomenon. It is centuries old. There have been recorded incidences of bribing and seeking illicit favors in early Chinese, Egyptian, Greek, and Indian civilizations. Mankind with its proclivity for power and wealth has always succumbed to corruption in one form or another.

Corruption is found in all walks of life. Naturally, it is endemic to the business world too. Internationally, it is even more pervasive, and it affects many aspects of business from cost of operations to business relationships and even to government-to-government relationships. Since international business transcends many countries and cultures, understanding and studying corruption is even harder. How should international companies with one set of rules and codes of conduct in their home country operate in countries that may have a different set of rules, especially if the host country rules are less stringent than the ones in their home country?

Traditionally, corruption has been accepted as no more than a “cost of doing business” in many countries. Corruption takes place in industrialized countries, developing countries and less developed countries. The degree of corruption may vary from one group to another. Countries are classified as ‘high-level corruption’ (for example, Bangladesh with a corruption perception index of 0.4 - on a 10 point scale, where 10 is least corrupt and 0 is most corrupt) and low-level corruption’ (for example, Finland with a corruption perception index of 9.9). Corruption issues have gained prominence as the contacts between less corrupt and more corrupt countries have intensified due to the globalization of markets.

The recent revelations of corporate scandals among American companies have sent shock waves within the global business community. The down fall of Enron in late 2001 followed by the problems at Tyco International, Qwest communications, WorldCom, and ImClone Systems can all be traced to corrupt acts by senior executives. These misdeeds have resulted in huge losses for these companies. And in the case of Enron and WorldCom, they sent the two companies to bankruptcy. In each instance, one or more of

the senior executives misappropriated funds, were accused of accounting irregularities, or of insider trading. These executives, misused their powers for personal gains and in so doing destroyed the wealth of many of the shareholders, brought losses to pension funds, and also cost the jobs of innocent employees.

The United States, with its arguably superior financial transparency rules, an auditing system though self-regulated that is known to have a core of well trained and diligent auditors, vigilant Securities and Exchange Commission (SEC), corporate executives with integrity, and a very inquisitive press was considered a system that was least likely to be a haven for corrupt behavior in its corporate executive ranks. But, apparently, the financial reporting after all was not that transparent; the accounting firms were less than diligent, the SEC was not that vigilant, the corporate executive not that honest, and the press were not that inquisitive.

The question in the minds of the policy makers in some of the international organizations like the UN, World Bank, Transparency International (TI) etc. is, if the United States, with all its zeal, power, and dominance cannot overcome corruption, what chances do the small developing countries, with less vibrant economies, little capital, and vague laws and lax enforcement have in curbing corruption?

Types of corruption

Corruption involves many types of crimes. The extent to which people abuse their position for personal gains is limitless. Research has shown that there are different types of corruption. At one end of the spectrum we have a local low-level official taking small sums of money to expedite routine approvals or transactions - *petty corruption*, next we have defense contractors paying billions of dollars to lawmakers for awarding major defense or transportation projects – *grand corruption*, at the other end of the spectrum are the huge campaign contributions to politicians or the contributions to government leaders – *influence peddling* (Elliot, 1997). Corruption can also be classified as business corruption and political corruption. Table 1 presents the different types of corruption and some examples of each type.

Table 1
Types of Corruption

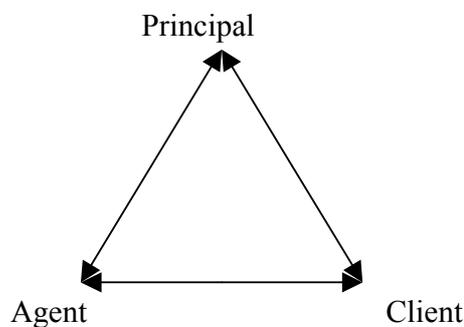
#	Type of Corruption	Examples	Predominantly Found in:
1	Business corruption	<ul style="list-style-type: none"> * Bribing officials * Accounting irregularities * Tax evasion * Insider trading * Money laundering * Embezzlement * Falsifying documents (research data) 	Most countries
2	Political corruption	<ul style="list-style-type: none"> * Voting irregularities * Holding on to power against the will of the people * Nepotism and cronyism * Rule of the few 	Mostly in developing and less developed countries

Definition of corruption

The difficulty with understanding corruption lies in the fact it not only covers many different types, but also has a divergent number of definitions that have been put forth by different agencies and researchers. Corruption implies “some form of illicit and criminal behavior for personal enrichment.” Though the above statement appears straightforward and simple, the interpretations and hidden meanings encompass quite a spectrum of activities and issues. As stated in Table 1, corruption could be associated with many different activities. Most current definitions are full of ambiguities and subjective statements. There is a need for a comprehensive definition for operationilizing the issue and at the same time be used to develop effective prescriptions to prevent corruptive practices. The definition and discussion of corruption for this paper is solely centered on ‘international business corruption’.

Any definition of ‘corruption’ starts with the premise of “abuse of power.” In the context of corruption in the international business field, there are three main actors. The *principal*, the entity that has the authority to grant and approve projects – a government agency such as the ministry of industry; the *agent*, is the intermediary who represents the principal and is actually responsible for granting the permission on behalf of the principal – a civil servant; and the *client*, a company or an individual who seeks a grant or permit for projects or investments – a business entity (Klitgaard, 1991). See Figure 1.

Figure 1
Key Actors in International Business Corruption



In this model, corruption occurs when the agent betrays the interests of the principal and accepts gifts and or monies from the client to grant a favor to the client without any thought for the fairness of such a favor. Corruption could also stem from the principal going directly to the client. Therefore, in defining corruption all the three actors that form this triumvirate should be included. Similarly, in addressing the causes and remedies of corruption, effort has to be made to focus on each element of the triangle individually as well as collectively.

Interestingly, the most commonly used definitions of corruption mention the three main actors, that is, definitions assign equal importance to ‘*offering*’, ‘*receiving*’, and

‘soliciting’ of gifts or bribes. Unfortunately, in the discussion of solutions to corruption, harmonizing the code of conduct for businesses has been the most difficult to accomplish. Table 2 presents the five most commonly used definitions of corruption and the name of the agencies that define it (Claros, 2002).

Table 2
Definition of Corruption as defined a Particular International Organization

#	International Organization That defines it	<u>Definition of Corruption</u>
1	The United Nations (UN)	“Commission or Omission of an act in the performance of or in connection with one’s duties, in response to gifts, promises or incentives demanded or accepted, or the wrongful receipt of these once the act has been committed or omitted”.
2	Organization for Economic Cooperation and Development (OECD)	“The offering, giving, receiving, or soliciting of any thing of value to influence the action of a public official in the procurement process or in contract execution”.
3	Transparency International (TI)	“The misuse of entrusted power for private gain”. Transparency International further differentiates corruption “according to rule’ or “against the rule”. In the first instance, the definition covers all the areas in which the receiver is required by law to receive some form of compensation (bribe), and in the second instance, the receiver is prohibited from providing some of these services and therefore is not entitled to any compensation (bribe).
4	World Bank and Asian Development Bank (ADB)	“Corruption involves behavior on the part of officials in the public and private sectors, in which they improperly and unlawfully enrich themselves and/or those close to them, or induce others to do so, by misusing the position in which they are placed”.
5	Law Library’s Lexicon	“An act done with an intent to give some advantage inconsistent with official duty and the rights of others. It includes bribery, but is more comprehensive; because an act may be corruptly done, though the advantage to be derived from it be not offered by another”.
6	Summarized definition based on the above	“When a public agent or person in power uses his or her position to gain for themselves and/or those close to them by acting improperly or misusing their given powers and thereby compromising the trust that is entrusted in them and in so doing gives an unfair advantage to the person or persons who initiated the gift or provided the said gains”.

Causes of corruption

It is very hard to pinpoint all the causes of corruption. It is even harder to associate corruption with a single factor. Many attempts have been made to find correlations between factors that may contribute to excessive International business corruption. These attempts generally fail to isolate the variables. The number of factors that lead to corrupt practices and the interrelationships between the factors may be one of the reasons that researchers find it difficult to identify causes of corruption. Therefore the literature dealing with corruption often states a general framework of causes.

There is confusion as to whether corruption flourishes because of a country's cultural traits, its economic development stage, its economic system, its political structure, poverty levels, social patterns, faith and belief (trust) in its religious institutions, moral apathy, the prevailing attitudes of the people or the unethical behavior of the international companies and their executives. It has been noted that corruption is widespread in countries where the administrative powers are concentrated among few individuals and when the laws of the land are not transparent (Tanzi, 1998; LaPalombara, 1994).

But, how guilty are the international companies themselves? Do the international companies follow a rigid code of conduct that discourages them from bribing officials? In understanding the causes of corruption, one must not overlook the interconnected relationship between the *principal*, *agent*, and *client*.

Causes of corruption can be classified into three main areas – environmental, individual, and firm related. Environmental factors are those that exist within the country and are outside the control of a single individual.

In order to develop a systematic approach to the causes of corruption, some researchers have identified the key environmental variables in which corruption may thrive (Tanzi, 1998; Novartis Foundation, 1998; Alam, 1995; LaPalombara, 1994, and Macrae, 1982). The most commonly cited environmental variables leading to corruption are:

a. Environmental variables

- Lack of a clear distinction between what is considered 'public' and what is considered 'private. This leaves the door open to appropriate public resources for private gains.
- Excessive administrative and discretionary power concentrated among a few. Since these leaders have supreme powers, their actions are never questioned and those who do raise questions are summarily dismissed or severely punished.
- Lack of transparency in the handling of public finances. There are no clear mechanisms of check and balances; hence it is easy to misuse funds.
- Lack of independent control agencies. Since there is no oversight, corruption goes unabashed.
- Absence of dependable legal machinery for preventing arbitrary application of regulations and laws. When the legal system fails, it becomes a hot bed for

- corruption, as there are no penalties for misuse of funds and at the same time the ones who loose out do not have any recourse for appeals.
- Weak public institutions. Because there is no free press, many misdeeds go unreported.
 - Over regulations. When there are too many requirements to get projects approved, it breeds inefficiencies that are then circumvented through bribing officials.
 - Unclear regulations. When laws can be misunderstood or misinterpreted it leads to confusion and a few individuals who can operate in this set up can become targets of bribery.
 - Lack of economic development. When a country has not reached its economic potential, many of the common people do not have employment opportunities leading them to resort to corruption or other illegal activities.
 - Lack of competition. In countries where many of the industries have just one or two firms competing for markets it creates an informal barrier for other firms to enter. In order to perpetuate this equation, these firms resist others entry and win contracts through illegal means.
 - Income inequalities. When just a few members of the population live lavishly leaving the rest to barely manage, it can lead to corruption by necessity.
- b. Individual variables
- Greed – individual greed, whether it be of an official, government leader, or a company executive all lead to actions that may be corrupt.
 - Integrity/honesty – some individuals are dishonest by nature and are more prone to acting illegally than others.
 - Wages and salaries – in some poorer countries the salaries of government employees are so low that they cannot take care of the needs of their families. In desperation and by necessity these individuals take bribes to augment their incomes.
 - To maintain power – some leaders of autocratic governments resort to taking bribes in order to continue their rule and maintain their ostentatious lifestyle. The bribes, provides funds to pay off a few political allies and some key loyal officials who then support the rule of the individual.
- c. International firm variables
- Market expansion – international companies participate in corruption to assist themselves in their market expansion strategies. By bribing a few officials, these companies are able to establish operations and achieve their goals. If not for these bribes, these companies would not have received the necessary permits to set up operations.
 - Profit maximization – by selecting those countries with potentially a large expanding market with very little competition, some of the international companies choose to bribe officials to enter these markets and reach their profit targets.

- Supply of resources – by entering some of the countries through corrupt practices, international companies are able to secure a continuous source of resources such as materials, components, etc.
- Low cost labor – some of the most significant cases of corruption has occurred when international companies have gotten permission to establish operations to tap into the inexpensive and abundant labor that is available in these countries.

Generally, confusing bureaucratic rules, weak enforcement of existing laws, top-level corruption, and multi-level corruption are all factors that contribute a great deal to illegal business activities and bribes. This is especially true among developing countries as they are often beset by many of these forces. Transparency International has found that developing countries suffer from ‘systematic’ corruption. It is like an epidemic and it infects every aspect of governance. This may be the reason that in most studies on corruption, developing countries tend to be the most corrupt from a business point of view. Corruption in some of these countries is so pervasive that the populace is hardly surprised to learn of corruption among its senior administrators and political leaders.

The ten most corrupt countries in the world according Transparency International’s ‘Corruption Perception Index’ (CPI) for 2001 are presented in Table 3 (list includes only 91 countries). The CPI is a ‘poll of polls’ and has been prepared using seven sources. The sources of the CPI include World Competitiveness Yearbook, Gallup International, and DRI/McGraw-Hill Global Risk Service. Because these sources provide similar assessments, they may be considered an indicator of a real world phenomenon. Over the years, TI has successfully publicized the problem of international business corruption. Hence, more and more people are aware this issue.

Table 3
Ten Most Corrupt Countries of the World

Rank	Country	Corruption Perception Index (CPI) (Scale; 10 = Clean and 0 = Corrupt)
91	Bangladesh	0.4
90	Nigeria	1.0
88	Uganda	1.9
	Indonesia	1.9
84	Kenya	2.0
	Cameroon	2.0
	Bolivia	2.0
	Azerbaijan	2.0
83	Ukraine	2.1
82	Tanzania	2.2

In reviewing these countries, it is apparent that many of the aforementioned factors that lead to corruption are found to exist in most of these countries. For example, Nigeria has had its share of dictatorial regimes, ineffective judicial system, lack of a free press, lack

of transparency in handling public finances, and a large percentage of its population living without basic necessities. In addition, many of these countries have large populations (between 8 million and 210 million, with an average population of 59.8 million people per country). The large population combined with high levels of poverty, high unemployment, uneven income distribution, and low literacy levels all seem to foster corruption. Interestingly, five of the most corrupt countries according to the CPI are African countries. In fact, a large number of African countries are among the most corrupt in the world. Consequently, many of these countries remain economically poor, have not grown for decades, and receive very little FDI.

A factor that is not on the above list of variables contributing to corruption or acting as deterrent to corruption and appears to be a strong contributor to corruption is 'greed'. Selling junk bonds and the savings and loan debacle of the 1980's in the U.S. can be attributed to the greed of few individuals (Useem, 2000). Greed is what makes rulers of countries, bureaucrats, politicians, and government officials take bribes. Greed to amass wealth, live a lavish life, covet material goods, own assets, and gain power by exerting authority. Take for example, the recent scandals in the United States, a country with many of the positive variables that hinder corruption, but it is the greed of a few individuals at the top of these companies that brought these companies down. This means, that the environments can be markedly different and work to either promote or hinder corruption, but environment in itself may not be the only contributing factor to corruption. No wonder, that corruption is much more pervasive in the world even if the conditions that contribute to corruption does not exist, there are some people in every society who are greedy.

Is greed a cultural trait? Can greed of a society be measured? Can we train people to be less greedy? These are all important questions that researchers should be addressing in combating corruption.

It is easy to pinpoint the environmental variables and greed as the two factors that lead to high-levels of corruption. But, what is missing here is the role of international companies? Whereas politicians and government officials are the recipients of the bribe, it is the international business community that offers these bribes. Therefore, in isolating the factors that cause corruption, the responsibility of the international companies should not be omitted. If these companies did not offer gifts and bribes to government officials would there be corruption at all? Some countries and industry groups have tried to address this very issue. For example, the United States Congress passed the "Foreign Corrupt Practices Act" (FCPA) motivated by the highly publicized cases of bribery by U.S. Multinationals to governments and or government agents (Exxon was accused of paying bribes of over \$78 million during the 60's and 70's. Similarly, Lockheed paid over \$30 million in bribes to maintain its business overseas). Although the FCPA was successful in curbing corruption by U.S. companies, it appears that they may have lost a few opportunities in some of the countries because of bribery by international companies from other countries. Mainly, due to the efforts of the U.S. government, the Organization of Economic Cooperation and Development (OECD) has instituted guidelines for corporate behavior that is ratified by 35 member countries. More needs to be done by the

industry groups to curb corruption. Therefore, in any discussion of causes of corruption the individual or groups that bribe must be considered in the equation.

As there are factors that contribute to high-level of corruption, researchers have been able to identify variables that deter corruption. As one may surmise, some of these variables are just the opposite of those that are identified as contributing to corruption. The types of variables that hinders corruption (transparent systems) are:

- Relatively efficient bureaucracy. Efficient bureaucracy negates the need to bribe officials and therefore deters corruption.
- Free and open democratic system of governance.
- Well functioning political system
- Access to public records
- A well functioning legal system
- High level of trust between citizens and their elected officials
- Low level of tolerance towards corruption

Countries like Finland and Denmark that rank very high on the CPI list as the cleanest countries has a relatively stable political system, very efficient government agencies, a very high level of trust between politicians and the populace, and the society as a whole values ‘integrity’. Table 4 lists the top ten countries that are the cleanest as ranked by Transparency International.

Table 4
The Ten Least Corrupt Countries of the World

Rank	Country	Corruption Perception Index (CPI) (Scale; 10 = Clean and 0 = Corrupt)
1	Finland	9.9
2	Denmark	9.5
3	New Zealand	9.4
4	Iceland	9.2
	Singapore	9.2
6	Sweden	9.0
7	Canada	8.9
8	Netherlands	8.8
9	Luxembourg	8.7
10	Norway	8.6

Each one of the top ten countries that are least corrupt are all industrialized and economically developed countries. There are a few other key characteristics common to these countries. All the ten counties have very stable governments, have a political system that is open and participatory, people are well educated (literacy rate well over 90%), and have small population (except for Canada and the Netherlands all the others are under 9 million with an average for the group at 8.16 million). Surprisingly, 3 out of the top ten countries are Scandinavian countries and Finland lies next to the Scandinavian

countries. There must be a genetic character trait and or the educational systems in these countries that make the people of these four countries the cleanest in the world.

Effects of corruption

A corrupt economy does not provide a fair market opportunity to all the firms that would like to participate in it. The effects of corruption are felt in monetary terms from a business point of view as well as in social and political costs. Focus of this paper will be more on the monetary effects of corruption.

1. Monetary costs of corruption – economic effects

- As mentioned earlier, a corrupt system does not provide open and equal market opportunity to all the firms. Payments and or bribes do not have a market value, and hence, raise the overall cost of operations. This would not be the case if the opportunity to compete were available for all the firms interested in this market.
- Generally speaking, high level of corruption effects economic development and economic growth (Rose-Ackerman, 1975; Shleifer and Vishny, 1993). Corruption acts as a hindrance to growth by not allowing free markets to operate and hence creating inefficiencies that lead lower outputs. Besides its impact on economic growth, corruption also has been shown to worsen poverty (Gupta, Davodi, and Alonso-Terne, 1998).
- Habib and Zurawicki (2002) in their study of corruption and foreign direct investment (FDI) concluded that corruption is a serious obstacle for investment and may result in reduced flow of FDI's (Wei, 2000). This problem is compounded for developing countries. These countries need FDI to produce industrial goods, to receive technology, to increase employment, and for obtaining badly needed capital.
- Due to the reduction in flow of capital, corruption effects GDP growth. Between 1995 and 2025, countries such as China, Indonesia, India, and Nigeria are projected to contribute more than half of the world GDP growth (World Bank, 1997). But, these four countries are also among the most corrupt in the world, resulting in an inefficient world economy.
- Price and quality of finished goods are also affected in countries where there is high-level of corruption. Since bribery takes place in secret, access to market is artificially set and therefore it excludes competitive forces that could have put pressure for setting competitive quality and price.
- Many international companies have started including CPI as yet another variable along with economic risk and political risk in evaluating countries for investing. Therefore, international companies bypass countries that have a high-level of corruption. Hence, these countries lose out on valuable inflow of foreign capital. In fact, studies have shown that FDI to a country increased when investors believed that the government would curb corruption (Busse et al., 1996).
- Lack of foreign investments flow to a country increases financing costs for both private and public projects. The limited capital within the country forces local investors to pay higher rates for borrowings. For example, in a study done by the

Milken Institute (Hall and Yago, 1999), it was observed that in comparing sovereign bond issues, countries with higher corruption index had to pay much higher premiums than those with lower corruption index. As see in Table 5 below, in comparing Sweden and Brazil with approximately similar amount of bond issuance for 1997 and 1998 (23 billion dollars versus 22 billion dollars), Brazil's financing costs are about 25 times greater than that of Brazil (38,157 billion dollars versus 1,531 billion dollars) because of graft and corruption.

Table 5
Comparison of National Bond Rates for High-level and low-level Corruption Country

Country	Debt Issued (000,000) 1997+1998	Institutional Premium	Corruption Premium	Graft Premium	Financing Costs (000,000)
Brazil	21,959	1.23	6.00	2.07	38,157
Sweden	23,916	0.33	0.50	0.04	1,531

- There is no doubt that corruption has an adverse effect on countries that are not able to curb this problem. As an example, the Asian Development Bank (1998) in a study of corruption and monetary effects reported that:
 - a) The Philippines has lost \$48 billion over the last 20 years to graft.
 - b) In Africa, at least \$30 billion in stolen aid money ended up in foreign bank accounts.
 - c) Corruption in Italy inflated its national debt by \$200 billion.
- According to The U.S. Commerce Department estimates foreign firms paid approximately \$80 billion to officials in other countries during the years 1995 to 1998. These costs would somehow trickle into the consumer market either in the form of increased price or inferior product quality (Wilhelm, 2002).
- Corruption also leads to other negative impacts including reduction in tax revenues. There are no specific studies to indicate the exact amount of losses, but most researchers agree that it could be in the millions of US dollars per country.

2. Social costs of corruption

Besides the monetary costs, corruption leads to some social costs that could be detrimental to a country's overall economic growth. Some of the social costs associated with higher corruption levels are seen in the areas of health, education, and hygiene. Governments that spend a higher percentage of their GDP on education, health, and other public services normally are those that have a fully developed economy. It has also been suggested by the World Bank, that countries wanting to reach developed economic status should spend more on education and health. Every country needs a well-educated and healthy population to be productive and improve its economic condition. It has been observed, that in countries where high-levels of corruption exists, the amount spent on public services is considerably lower to other comparable countries with lower corruption levels (Buscaglia, 2001). Using regression analysis Paulo Mauro (1995) demonstrated that a country that improves its CPI by 2 points ends up increasing its education budget at least by 1% of its GDP.

Corruption also leads to poor health services as funds are channeled to individuals and or projects that are favored by the leaders of the country. The consequences for those countries poor health or inadequate services are high infant mortality rates, low life expectancy, and poor quality of life.

3. Political costs of corruption

Politically, corruption leads to government leaders who are self-serving, amass wealth for themselves, allocate very little funds for projects that could benefit the country and its economic growth, perpetuate the rule of a few, and suppress the rights and voices of the majority of the population. To continue in power, these leaders need funds and this most often comes from bribes and also from the government budget. In developing countries, where budgets are inadequate to begin with, very little of the appropriated funds actually go to fund projects. Projects such as building of roads, power plants, telecommunication systems, and education are all essential to attain economic growth. But, the little funds that are allocated end up in the hands of the country's leaders who then would use them for their own well being as well as to manipulate the political system to continue their rule.

Prescription to end or reduce international business corruption

Efforts to curb corruption in the past three decades have had somewhat less than stellar results. There have been some improvements due to the actions of individual governments (U.S.), international organizations (OECD and TI), and individual companies (codes of ethics adopted by the Fortune 1000 companies, Weaver et al., 1999). Because of the globalization of markets there are many more companies with operations in many foreign countries compared to 20 years ago. As mentioned earlier, the contacts between less corrupt and more corrupt countries have intensified in the last decade. All indications are that the number of cases of corruption is on the rise. This may be due to the involvement of many more companies in international business or because of the larger number of countries that are now open to these companies, or yet, because over the years the reporting on corruption and monitoring of corrupt practices has improved tremendously.

In order to reduce worldwide corruption that affects businesses, there has to be a concerted and well-coordinated effort on the part of all concerned. The parties that must take an active role in this effort are:

- Individual country governments
- International organizations
- International firms

The task of these three groups would be to:

- Set standards and codes of conduct

- Undertake monitoring of corrupt practices
- Set up a judicial system to hear cases of corruption and meet out justice

a. At the country level

Any attempt to curb corruption has to start at the country level. Governments in some of the most corrupt countries have to have programs to root out corruption in increments, as it is impossible to completely root out systematic corruption in one sweep. Since, most of the countries that have high-level of corruption are economically underdeveloped, the incentives for these countries to get rid of corruption must be economic. Through greater foreign direct investments, transfer of technology from industrialized countries, and reduction in unemployment, these countries can attain an unprecedented level of economic growth. Entry of foreign firms will increase competition, which along with reduction in government subsidies that are quite common in the developing countries has been found to decrease corruption (Ades and Di Tella, 1999).

Some of the specific steps that countries with high-level of corruption should undertake to curb corruption are:

- Enact anti-corruption regulations – most of the countries with high-level of corruption either do not have anti-corruption laws or have them but do not enforce them. These countries do not have to reinvent the wheel. They could easily adapt anti-corruption regulations or the enforcement procedures that are practiced in some of the low-level corruption countries to suit their particular environment. The cornerstone of any anti-corruption law has to be the problem definition. That is, what constitutes corruption? Corruption activities and their boundaries must be clearly spelled out in order to establish anti-corruption laws.
- Setup monitoring systems – laws and regulations will be observed only if there is a mechanism to monitor and enforce it. Government agencies need to be established that will have the responsibility of tracking corruption and reporting it.
- Penalties – anti-corruption laws will not be followed unless there are severe penalties meted out to law-breakers. Penalties have to correspond to the degree of corruption. A government clerk taking a small amount of bribe could get a warning or suspended from his job, but, the Defense Minister taking a million dollars need to be tried and sent to jail if guilty.
- Codes of conduct for government employees – it is imperative that codes of conduct for government employees be developed and then enforced. These codes should include what constitutes corruption, what is permitted, and what the consequences for not observing these codes are.
- Incentive systems for government employees – most social scientist agree that to make individuals obey rules it must be reinforced with a system of punishment as well as reward. By rewarding employees who are honest and obey the codes of conduct established by the government, the lure to take bribes will be considerably reduced.
- Better salary structure for government employees – in many developing countries taking bribes is more of a necessity for some government employees because of

poor wages. In order to sustain the family needs some of these workers take bribes and gifts to augment their meager wages. Therefore, to make these employees less dependent on bribes, governments should introduce wages that guarantee a reasonable living standard.

- Establish democracy – in many developing countries where the rate of corruption is very high, the country is ruled by a few with all the power centered around one individual. Since there is no resistance, these individuals rule without opposition for many years and are free to act as they wish including taking bribes, fostering nepotism, and cronyism. To perpetuate their rule, these leaders buy the loyalty of some of the key government agencies including the military.

The aforementioned prescriptions are not easy to implement, especially for developing countries. Most of the steps outlined above require funds, training, and changes in attitude at many levels. It is in this area that international agencies such as World Bank and IMF, and the international business community could be of great help. By providing the necessary funds, training, mechanisms to establish codes of conduct, and setting up local monitoring systems the international agencies could reduce the corruption that is rampant throughout the world. To be successful, the effort should start with just a few carefully selected countries as test cases and then once the program is successful it could be rolled out to other countries. This approach has three benefits, first, the smaller number of countries would mean lower costs, second, it is easier to implement, and thirdly, flexibility to make changes to the program if something does go wrong.

b. At the International organization level

It is obvious that any attempt to eradicate corruption at the country level is not going to succeed without some external help. The countries where corruption is systematic, the will to change is not there, the knowledge to understand the problem is not there, and the funds required to set up an anti-corruption program is not there. To assist the countries in curbing corruption, some of the international agencies must get involved with necessary financing and training. Corruption is a worldwide problem that funnels productive funds out of the economic system to the hands of a few who then use it for personal gains without contributing to the development efforts of the country.

Some of the specific steps that these agencies could undertake are:

- Provide knowledge and training – as mentioned earlier, many of the countries with high-levels of corruption do not have anti-corruption laws or if they have it are not properly enforced. Organizations such as the World Bank, IMF, Transparency International, and the United Nations could provide technical help to these countries to formulate laws, codes of conduct for government employees, and help set up monitoring systems to track the corruption code breakers. With experiences gained from other less corrupt countries, these agencies are well positioned to provide the necessary technical help. In a similar vein, these organizations could also undertake training programs to assist these countries in

- having a knowledgeable group of people who could administer these rules and monitor the observance of the corruption laws and rules.
- Provide funding – what is very badly needed in curbing corruption in developing countries are funds to carry out some of the prescriptions/steps outlined earlier. The countries with highest level of corruption are those that are poor with very low economic growth levels. These countries do not have the finances necessary to implement rules and regulations. Therefore, it is imperative that some of the international organizations that have developmental funds at their disposal like the IMF and Asian Development Bank provide some of these funds (International businesses could also come to the assistance of these countries, this is discussed under a separate heading). The justification for these allocations would be from an economic standpoint.
 - Harmonize the codes – at present each country (especially the industrialized countries) has their own set of codes for business behavior and also for the government staff. The process of curbing corruption would go a long way, if these codes could be standardized so that there is no confusion, especially when an international firm operating in two different countries has to follow two different set of rule.

c. International firms

One of the key participants in the corruption process are the international firms who try to use influence, gifts, and bribes to get better deals from host nations. So the argument goes, “if all international firms did not take part in bribing officials, there would not be any business corruption.” This is too simplistic a solution. Businesses always look for competitive advantages and securing markets with fees paid (legally or illegally) is just another expense that has to be incurred. On the other hand, gaining advantage through illegal means makes the competitive environment imperfect which in turn changes the dynamics of the marketplace. In this scenario, goods become more expensive, products will be of poorer quality, and service will suffer. It is imperative that international firms collectively follow uniform codes of conduct in dealing with host countries for the benefit of the consumers, economic growth of the country in question, and for their own profit objectives.

Specifically, international firms should implement the following:

- Internal codes of conduct – many international firms have their own internal of codes of conduct for conducting business with host nations and vendors. For example, in many companies, the specific amount of gift that one can accept from vendors is limited to a very small amount. Similarly, there are written rules banning bribes to host country officials and also an explanation of what constitutes bribes. Even with written rules, it has been observed that many company executives do bribe foreign officials, especially if the stakes are high. Therefore, the issue is of compliance, that is, rules and codes of conduct should be followed and those who break the rules must be penalized. Unfortunately, many companies are unwilling to enforce the rules as they see it as a competitive disadvantage. A case in point is the Foreign Corrupt Practices Act passed (FCPA)

- by the US, everyone concerned with the act, now feels that the United States International firms may have lost out on many foreign deals and market opportunities because of the FCPA.
- Employee training – employees need to understand the rationale for the rules and why they should follow these rules. This could be achieved through employee training programs. These programs are held in house with both internal and external lecturers. Better the understanding of the rules and codes of conduct higher is the compliance by the employees.
 - Adhere to rules – company executives should be aware of all the rules and regulations that affect their operations, including corruption laws in all the countries the firm is in. This knowledge should be used to understand the variances between the various regulations that the company encounters. By knowing these laws, company executives can direct and coordinate the activities of their subsidiaries in terms of corrupt practices.
 - Provide funding – for the worldwide anti-corruption program to succeed, it needs developmental funds that could be used at the country level for establishing these programs. The countries themselves are poor and do not have the funds to set up anti-corruption programs. Some of the international organization may provide some funding, but it appears that this is not adequate. To augment the existing budgets, international firms could step in and fill the need. The funds that are provided by the international firms should not go individual countries, but to the international agencies who then can distribute these funds. It is not the role of international firms to meddle directly in country affairs and therefore, using the international agencies as intermediaries the task could be accomplished with little or no repercussions.

Conclusion

International business corruption is a worldwide phenomenon with no end in sight. On the other hand, its effects on local economies are very damaging. Some efforts are being made to curb corruption by some of the industrialized countries, the OECD, and Transparency International. They have succeeded to some extent in publicizing the problem. They developed individual country codes of conduct and also attempted to standardize the codes. Even with these efforts, the number of cases of corruption has not abated. There are more corruption cases reported each year.

This paper attempted to define the problem, determine its causes, map out its effects, and finally develop some programs to fight corruption. It is quite evident from the discussion that the problem of corruption is very complex. The number of entities involved, the underlying causes of it, and the territorial context under which corruption takes place makes understanding the problem quite difficult, if not impossible.

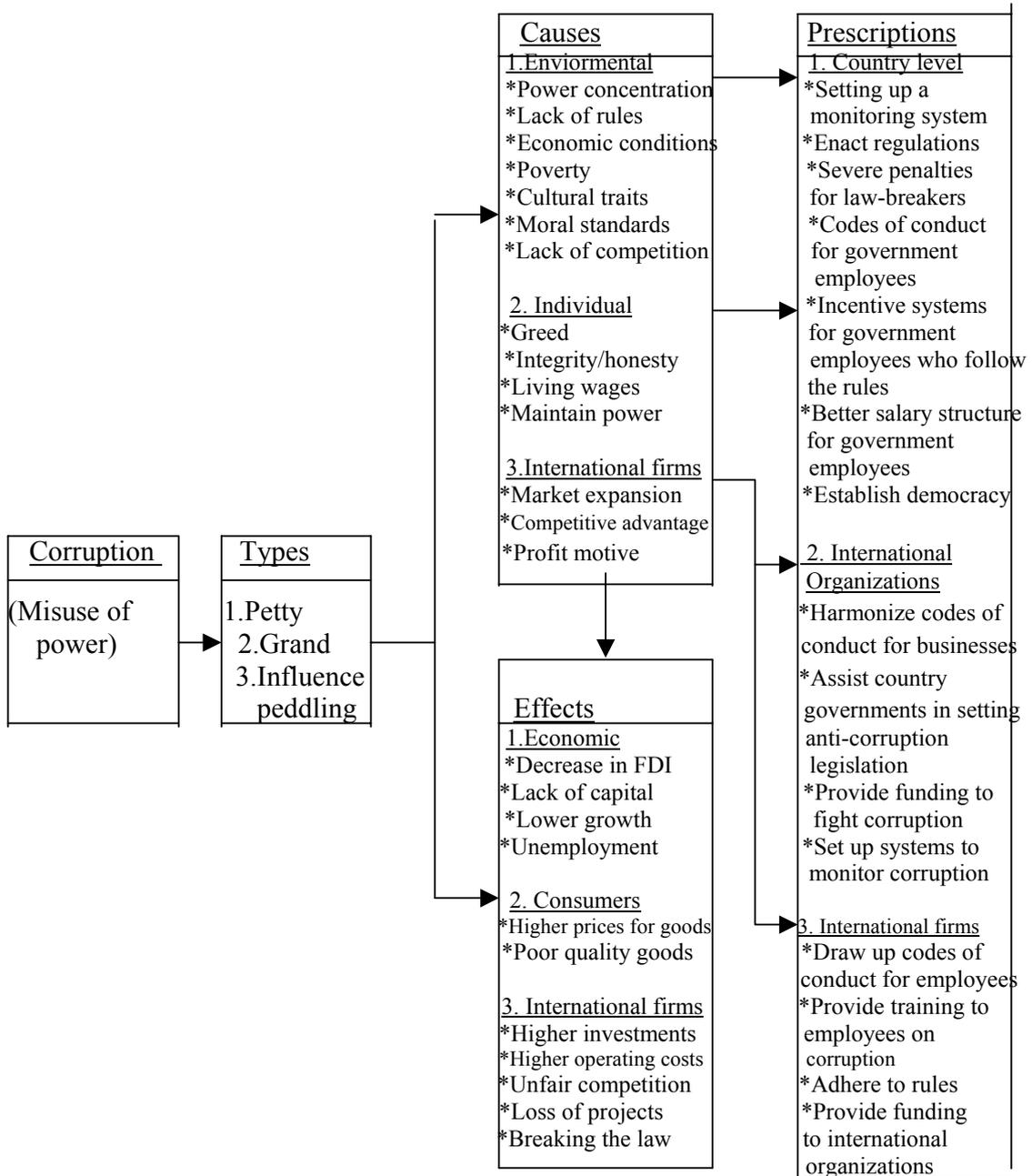
The three main actors in the corruption equation are: the *principal*, the *agent*, and the *client*. Any attempt to curb corruption has to bring order into all the three parties. Solving the problem from one entity alone will definitely fail. The prescriptions stated here curb corruption takes this unique mix into account. It is suggested that to reduce corruption,

the efforts of the countries involved, the international firms who participate in corruption (may be forced to participate due to competitive reasons), and international organizations have all to work together. The main focus of their efforts has to be in:

- Developing codes
- Harmonizing the codes
- Providing training
- Establishing monitoring and tracking systems
- Setting up a judicial process to hear corruption cases

To be successful, it is suggested that: 1. To start the program with just a few carefully selected countries. 2. International organizations should provide technical and financial help. 3. The funding should partly come from international firms. Figure 2 summarizes the overall framework of the corruption issue and the prescriptions for partly solving the problem.

Figure 2
Framework of Corruption



References

1. Ades, Alberto and Rafael Di Tella, (2001), "Corruption in International Business (A)-Case Study," *Harvard Business School Publishing*, March 29, pp: 1-10.
2. – (1999), "Rents, Competition, and Corruption," *American Economic Review*, vol. 89 (4), pp: 982-994.
3. Alam, M, (1995), "A Theory of Limits on Corruption and Some Applications," *Kyklos*, 48, pp: 419-435.
4. "Anticorruption Policy Paper," Asian Development Bank, (1998), Manila, Philippines.
5. Buscaglia, Edgardo, (2001), "An Analysis of Judicial Corruption and its Causes: An Objective Governing-based Approach," *International Review of Law and Economics*, vol. 21 (2) pp: 233-249.
6. Busse, Laurence, Noboru Ishikawa, Morgan Mitra, David Primmer, Kenneth Surjadinata, and Tolga Yaveroglu, (1996), "The Perception of Corruption: A Market Discipline Approach," *Working Paper*, Emory University, Atlanta, GA.
7. Claros, Andres, M., (2002), "Corruption in International Business," Unpublished Honors Essay, Hofstra University, NY, pp: 6 - 10
8. Elliott, Kimberly, (1997), "Corruption as an International Policy Problem: Overview and Recommendations," in Kimberly Elliot (ed.), *Corruption and the Global Economy*, Institute for International Economics, p: 177.
9. Gupta, Sanjeev, Hamid Davoodi, and Roso Alonso-Terne, (1998), "Does Corruption Affect Income Inequality and Poverty?" *IMF Working Paper*, International Monetary Fund, Washington D.C.
10. Habib, Mohsin, and Leon Zurwaicki, (2002), "Corruption and Foreign Direct Investment," *Journal of International Business Studies*, 33 (2), pp: 291-307.
11. Hall, Tom and Glenn Yago, (1999), "Policy Briefing", Milken Institute, Washington D.C., pp: 1 –10.
12. Klitgaard, Robert (1991), *Controlling Corruption*, Bekley, CA. University of California Press.
13. LaPalombara, Joseph, (1994), "Structural and Institutional Aspects of Corruption," *Social Research*, 61 (2), pp: 325-350.
14. Macrae, John, (1982), "Underdevelopment and the Economics of Corruption: A Game Theory Approach," *World Development*, 10 (8), pp: 677-687.
15. Mauro, Paul, (1995), "Corruption and Growth," *The Quarterly Journal of Economics*, August, pp: 681-712.
16. "Multinational Corporations, Governing Deficits, and Corruption: Discussing a Complex Issue from the Perspective of Business Ethics." <http://www.foundation.Novaritis.Com>.
17. Rose-Ackerman, Susan, (1975), "The Economics of Corruption," *Journal of Public Economics*, 4, pp: 187-203.
18. Shleifer, Andrei and Robert Vishny, (1993), "Corruption," *Quarterly Journal of Economics*, 108 (3), pp: 599-617.

19. Tanzi, Vito, (1998), "Corruption Around the World: Causes, Consequences, Scope, and Curses," *IMF Working Paper WP/98/63, International Monetary Fund*, Washington, D.C.
20. Transparency International, (2001), "Corruption Perception Index," <http://www.transparency.org/cpi/2001/cpi2001.html>.
21. Useem, Jerry, (2000), "New Ethics or No Ethics?" *Fortune*, Education Collection, March 20, p: 1.
22. Weaver, G. R., L. K. Trevino, and P.L. Cochran, (1999), "Corporate Ethics Practices in the mid 1990's: An Empirical Study of the fortune 1000," *Journal of Business Ethics*, vol. 18 (2), pp: 283-294.
23. Wei, Shang-Jin, (2000), "How Taxing is Corruption on International Investors?" *The Review of Economics and Statistics*, vol. 82 (1), pp: 1-11.
24. Wilhelm, G. Paul, (2002), "International Validation of the Corruption Perception Index: Implications for Business Ethics and Entrepreneurship Education," *Journal of Business Ethics*, 35 (3), pp: 177-189.
25. World Bank, (1997), *Global Economic Prospects and the Developing Countries*, Washington D.C., p: 23.