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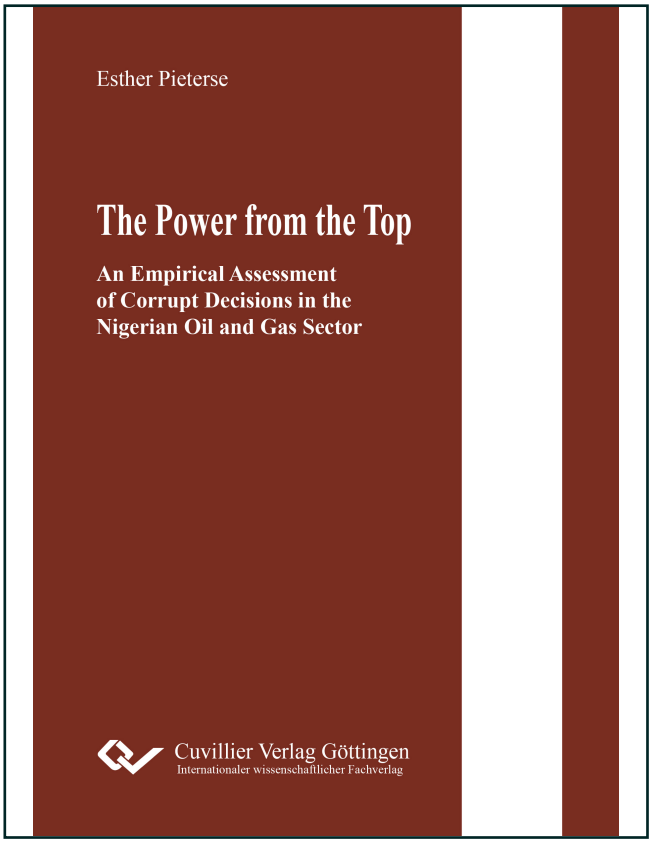
The Power from the Top

An Empirical Assessment of Corrupt Decisions in the Nigerian Oil and Gas Sector



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"I suppose that's one of the ironies of life doing the wrong thing at the right moment."
(Charlie Chaplin)

1 Introduction

The Bonny Case

In late November 1994, a couple of Western business representatives and high-ranking Nigerian officials met to discuss a deal that would result in four of the six major breaches of the United States Foreign Corrupt Practices Act (FCPA). The Western business representatives were members of a steering committee that run the joint venture 'TKSJ' formed by the companies Technip, Kellogg (today Kellogg, Brown & Root), Snamprogetti and Japanese Gas Corporation. Amongst the participants of the meeting was also the British lawyer Jeffry Tesler who would become one of the key players in ensuring the transfer of bribes from TKSJ to the Nigerian officials through a shell company on Gibraltar (United States District Court Southern District of Texas Houston Division, 2008, pp. 2, 4-5; Department of Justice (DOJ), 2009a).

After the November meeting, the chief executive officer (CEO) of Kellogg and leading member of the TKSJ steering committee, Albert Jackson Stanley, approved the agreement to pay Jeffry Tesler $60 million, with the understanding that a substantial portion of this money would be funnelled to Nigerian officials. A few weeks later, the company Nigeria Liquefied Natural Gas (NLNG), which was controlled by the Nigerian government, selected TKSJ as its "preferred contractor" for a construction project on Bonny Island, Nigeria. The contract worth US$2.2 billion was consequently awarded to TKSJ in 1995 (United States District Court Southern District of Texas Houston Division, 2008, p. 5).

After the first construction project was finished in 2000, a number of follow-up construction contracts for LNG projects on Bonny Island were awarded to TKSJ. The value of contracts that TKSJ received to construct the LNG facilities during 1995 and 2004 amounted to a total of US$6 billion (DOJ, 2008; Cassin, 2008). Jeffry Tesler and a second, Japanese agent who was later engaged to facilitate the transfer of bribes to lower-ranking Nigerian officials received over US$182 million to be transferred as bribes (Cassin, 2008).

The bribery scheme between TKSJ, the shell companies, the Nigerian officials and responsible persons at Nigeria LNG might have still been a secret if not for the former Director General of Technip, Georges Krammer, who was one of the partners in the TKSJ bribery scheme (Offodile, 2012). Initially Krammer was accused by French authorities for

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another unrelated corrupt practice, which Krammer sought to defend with the company policy of Technip. Technip Management, however, disputed Krammer's claims and left him to face the charges as an individual crime. This triggered Krammer' reaction in telling the French investigating judge Renaud Van Ruymbeke how Technip's commission payment system worked in Indonesia, Thailand and on the LNG Project in Nigeria. Thus began, in 2002, the French investigation of the Nigeria LNG project leading to investigations of French and Swiss authorities. In 2004, the investigations of the United States Department of Justice (DOJ) and Securities and Exchange Commission (SEC) followed suit (Hill & Jones, 2009, p. C101; Offodile, 2012; Wrage, 2007, p. 77).

Albert Jackson Stanley was the first to plead guilty in 2008 for his participation in the bribery scheme (DOJ, 2008). A few years later, he was sentenced to two and a half years in prison and a payment of US$ 10.8 million (Cassin, 2012; Calkins, 2012). Jeffrey Tesler, the middleman, was indicted on February 17, 2009 and at the request of the United States, arrested by the London Metropolitan Police on March 5, 2009 (DOJ, 2009a). On the same day of Albert Stanley's trial, Jeffrey Tesler was sentenced to 21 months in prison and had to pay US $149 million, the biggest individual forfeiture in FCPA history (Cassin, 2012; Calkins, 2012).

The companies involved in the TKSJ bribery scheme were also convicted before various jurisdictions and had to pay hundreds of millions of US dollars as criminal penalty in the US only[1]*. Four of the six major cases in FCPA history involve charges towards companies related to the Bonny Island bribery scheme (Cassin, 2011).*

1.1 Context and Motivation

The Bonny case is a remarkable and often-cited corruption case (e.g. Hill & Jones, 2008; Wrage, 2007). It underlines various arguments that can be overheard in (anti-) corruption discussions like "FCPA enforcement has become more rigorous", "corrupt deals involve complex networks" or "corrupt actions are facilitated by off-shore havens". However, it also demonstrates a fact that has long been ignored in anti-corruption literature and practice, recently leading to a new perspective being taken on the problem of corruption, especially in developing countries.

The fact referred to is that the private sector, as the supply side of corruption, plays a major role in perpetuating the problem of corruption (Burke & Cooper, 2009; Fleming &

[1] Kellogg Brown & Roots: $ 420 million (DOJ, 2009b); Technip: $338 million (DOJ, 2010a); Snamprogetti: $240 million (DOJ, 2010b); JPC Corporation: $218.8 million (DOJ, 2011).

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Zyglidopoulos, 2009; Gebhardt & Müller-Seitz, 2011; Transparency International, 2009a). In the Bonny Island bribery scheme multinational companies were involved that are based in industrialized countries with reportedly low levels of corruption. In fact, they took a very active part and for many years were heavily responsible for feeding the deceptive practices of the Nigerian government and the Nigerian oil sector. The presence of the corrupt TKSJ joint venture in the construction projects on Bonny Island endured the regimes of dictator Sani Abacha (-1998), the interim military leader Abdulsalami Abubakar ('98-'99), and the ostensibly corruption-fighting president Olusegun Obasanjo (1999-2007). Although it is unlikely that the representative officials of each of the governments needed substantial persuasion to accept the Bonny Island bribes, the involvement of the various regimes highlights the proactive engagement of TKSJ to be on "good terms" with relevant officials.

The dominant role of the multinationals in the Bonny case stands in a stark contrast to the long upheld argument that companies do not wish to engage in corruption but that in many countries they are more or less forced by public officials in order to do business (Heimann, 1997, p. 149; Rügemer, 1996; The Economist, 2002). It also shows that the previous focus on corruption as a problem of a weak public sector in developing countries (Rose-Ackerman, 1997, 1999; Doig & Riley, 1998; Krueger, 2002) represents a rather incomplete picture.

In this respect, it is not surprising that in the aftermath of the Bonny case transnational organisations issued a bulk of guidelines, codes and principles for anti-corruption programmes (also referred to as compliance programme) in the private sector (among others: International Centre of Commerce (ICC), 2011; United Nations Office for Drugs and Crime (UNODC), 2013; World Economic Forum (WEF), 2009). Today, all four companies that were involved in the Bonny case have implemented such an anti-corruption programme. In 2010, the United Kingdom (UK) passed a new Bribery Act, which makes companies liable for employees who engage in bribery if the company cannot prove that there are "adequate" anti-bribery measures (Transparency International UK, 2010, p. 4). In short, through scandals like the Bonny case anti-corruption programmes in companies have become *en vogue*.

Anti-corruption programmes involve the implementation of various measures such as internal controls, anti-corruption training for employees or the production of a code of ethics. The recommendations made by the variety of guidelines are quite similar[2]. One prominent anti-corruption measure that is often stated as the "basis" or "fundamental

[2] For a comprehensive comparison see: OECD, UNODC & World Bank (2013)

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requirement" for an effective programme is the 'tone from the top'. A strong tone from the top refers to a visible and strong endorsement of the companies' anti-corruption programme by top management. This endorsement not only relates to the provision of resources to establish an anti-corruption programme but also to an active representation and promotion of a company's ethical values and normative behaviour (Ashforth & Anand, 2003, p. 7).

The importance of the tone from the top for an effective corporate anti-corruption programme implies the assumption that individual employees regard top management as a role model for their own behaviour and decisions (Rich, 1997). With respect to corruption, it means that the motivation of individual employees to engage in corruption is influenced by the tone from the top.

The cherished relevance of the tone from the top in current anti-corruption guidelines for the private sector is puzzling from an academic point of view because the relationship between the perception of top management and corrupt behaviour of employees has not been thoroughly elaborated in corruption literature. The importance that is attributed to the tone from the top lacks a theoretical and empirical foundation. However, if tone from the top is a fundamental precondition for an effective anti-corruption programme, it seems to be worthwhile to scientifically explore the influence of the tone from the top on corrupt decision-making.

1.2 Research Question and Goals

In order to better understand the relevance of tone from the top as an anti-corruption measure, this research seeks to find out how and to which extent the tone from the top can help to prevent corruption in companies. Previous literature indicates that top management influences moral judgments of employees as well as social norms existing in organizations (Lasthuizen, 2008; Ashforth & Anand, 2003). Therefore, this study seeks to investigate how tone from the top relates to moral and social motivations in the employees' decision-making concerning corruption. Further, it explores whether motivations to engage in corruption differ in individual and collective decision-making.

By answering these research questions, this study seeks to make two contributions to better adapt anti-corruption programmes in multinational companies. First, this research seeks to develop an understanding of how top management as well as the moral and social setting may influence an individual in deciding whether to engage in corruption. Although there have been a few studies that examine the influence of non-rational motivations on corrupt decision-making, these studies all bear the limitation of being tested in industrialized countries and mostly involve students as subjects. This research therefore aims to test the

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proposed model with middle managers of companies that operate in the Nigerian oil and gas sector. The results of this research contribute to the understanding of the setting of the Nigerian oil and gas sector and how this setting influences the individuals in their decision whether to engage in corruption. This enables the formulation of anti-corruption measures and recommendations for companies that specifically suit the Nigerian context.

Second, the study seeks to advance the methodological possibilities of empirically investigating the effectiveness of corporate anti-corruption programmes. An innovative method is developed to test the theoretical model presented in this study. The method involves a tool, the "Drill Bit Business Simulation" which companies may apply in future to better understand the decision-making of their employees. Whereas the method is applied in this context to conduct an empirical analysis, its application represents a test run of a tool for companies, which can be applied in other sectors and countries. It consequently enables companies to adapt their anti-corruption strategies to the perceptions and mind-set of their employees in the variety of their contexts of operations. Also, it can be applied to test the effectiveness of certain anti-corruption measures that have been previously implemented.

1.3 Structure

The present work is organized into seven chapters, which follow the classical linear format starting with a review of existing research, a theoretical part, continuing with an empirical part, and concluding with a discussion of results and implications. This should help the reader to follow the deduction of the research question and the research hypotheses, to understand the development of the theoretical model and to be able to relate to the methods and analyses used to come up with results that have theoretical and practical implications. A short description of each chapter's content is provided in the following.

Chapter 1 introduces the work by providing the context, motivation as well as the research interest and focus.

Chapter 2 seeks to legitimize this study by showing the lack of scientific insight concerning the relevance of the tone from the top for the creation of integrity and compliance in companies. It first introduces the topic of corruption by outlining its development during the last few decades as an acknowledged problem in academia and practice. In the second part of chapter 2, the insights from previous research on the causes of corruption are regarded from the perspective of an individual employee. It stresses the need for more insight on the effects of tone from the top as well as on the role of moral and social motivations. Since

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moral and social motivations are culture-sensitive it is argued that more research is needed in regions that are the recipients of consequent anti-corruption measures.

Chapter 3 first discusses the variety of definitions, forms and types of corruption to clarify the subject of research more precisely. Next, the chapter presents the theoretical framework and the research hypotheses. After deducing the research question, the research model is developed. Three theoretic models have been used to synthesise the proposed model of corrupt decision-making. The chapter subsequently describes the proposed model of corrupt decision-making, which seeks to explain, which social and moral motivations influence an individual employee when facing a corruption-related decision.

Chapter 4 introduces the empirical method used for testing the model of corrupt decision-making derived in Chapter 3. First, the area of research is presented. Nigeria, as a country where corruption is omnipresent, is selected as a country where effective anti-corruption measures could make a strong impact on the social, economic and environmental state. The importance of the oil sector is presented as leverage to improve the lives of many Nigerians on the one hand, and on the other hand as a sector where corrupt practices are pervasive.

Following the discussion of challenges to empirically investigate corruption, the research design is outlined. It is explained how the method for empirical analysis "Drill Bit Business Simulation" realistically mimics the interactions in the Nigerian oil and gas sector and outlines the procedures that were taken for data collection. Relevant quality criteria are also discussed in this respect.

Chapter 5 presents the results of the study. First, the results on the model of corrupt decision-making and its evaluation are described. Further, explorative results on socio-demographic factors and the increased cost of corruption are presented.

Chapter 6 discusses the empirical results in the light of the theoretical implications and provides a number of recommendations for anti-corruption practice. Limitations of the study and avenues for future research are also discussed.

Chapter 7 gives an overall summary and emphasises the contribution of this research.

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"When water chokes you, what do you take to wash it down?"
(Aristoteles)

2 Literature Review

During the last decades, corruption has become a prominent topic of research in various academic disciplines (Andvig et al., 2001, p. 4; Pinto et al., 2008, p. 686; Rabl, 2008, p. 23). This rising academic interest has been accompanied by the growing acknowledgment of civil society organizations, media and policy makers that corruption is a serious political, economical and social problem, which is not confined to developing countries (Dimant, 2013, p. 2; Heimann; 1997, p. 147). As an introduction into the state of the art of corruption research, the first part of this chapter outlines how growing public awareness concerning corruption has fuelled corruption research and vice versa. This overview highlights the strong interaction of academic literature on corruption with anti-corruption practice. It further helps to understand why certain fields of corruption research have been more focused on than others.

Subsequently, a review on existing literature concerning the relevance of top management in preventing corruption in organizations is provided. Top management has been argued to be an important factor in preventing corruption in companies. However, little research exists that outlines the impact on employees' motivations concerning corrupt decisions. Therefore, the third part of this chapter presents existing corruption literature that helps to explain motivations of employees to engage in corruption. Finally, this chapter elaborates on the (non-) existing contributions on the differences in individual and group decisions concerning corruption.

2.1 The Development of Corruption as a Matter of Interest in Academia and Practice

Corruption has been a steadfast companion of human history (Dreher & Herzfeld, 2005, p. 2; Jain, 1998a, p. 1; Pinto et al., 2008, p. 685; Serra, 2009, p. 127). Numerous authors have highlighted the long history of corruption by referring to the early reports on corrupt behaviour in ancient Egypt (Kreitel, 2004, p. 149; Lipset & Lenz, 2000, p. 112) and ancient Rome (Bannenberg & Schaupensteiner, 2004, p. 24; Lipset & Lenz, 2000, p. 112). Others refer to the ancient book *Arthashastra* that discusses corruption and was written by an Indian prime minister in the fourth century BC (Bardhan, 1997, p. 1320; Klitgaard & Klitgaard, 1988, p. 23; Tanzi, 1998b, p. 4). Hence, corruption has always existed and has merely changed its forms and types in different eras of history (Bardhan, 1997, p. 1320).

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For a long time, corruption has been considered to be a serious problem of developing countries with weak governmental structures and low standards of public morality (Bayley; 1966; p. 719; Nye, p. 1967, p. 418). However, the corruption scandals unveiled in the previous decades showed that corruption prevails in every country (Bannenberg & Schaupensteiner, 2004, p. 25; Glynn et al., 1997, p. 7). Also, corruption scandals like the Bonny case (see chapter 1), demonstrate that corruption can be regarded a trans-national problem, involving international financial transactions and actors from all over the globe (Glynn et al., 1997, p. 12).

The historic and geographical omnipresence of corruption bares two puzzles. First, if corruption has always existed, is it possible to eradicate corruption once and for all? Literature provides rather pessimistic answers in this respect. Rose-Ackerman states that "the total elimination of corruption will never be worthwhile, but steps can be taken to limit its reach and reduce the harms it causes" (Rose-Ackerman, 1999, p. 4). A similar perspective is reflected in the a speech of former United Stats (US) trade representative Mickey Kantor stating that though it is unlikely that the world will ever be corruption-free, the US has a legal, moral and economic and political responsibility to pursue this problem in every possible forum and with every tool at our disposal (1996). Apparently, this seems to be the view that is widely shared by leaders in business and politics (Geetz & Volkema, 2001, p. 8).

If the aim of curbing corruption is not its total elimination but rather its control, research of corruption consequently needs to focus on the forms and types of corruption that are most harmful. Also, research should prioritize areas where corruption has the greatest negative effects. Acknowledging that corruption will always persist and that corruption research merely helps to identify measures that help to control corruption also implies that a reduction of corruption levels should be regarded critically. In order to determine whether anti-corruption is effective, the type of corruption that is reduced and its negative effect should be accounted for.

The second puzzle relates to the contrast of the long history of corruption to the brief history of corruption research. In fact, corruption as a designated subject of research has been investigated for only a few decades. It suddenly gained momentum with an exploding interest in a vast range of different academic fields. Almost over night, corruption became a major term when discussing the politics and economic growth in Africa (Matei & Matei, 2011, p. 23), good governance (e.g. Huther & Shah, 1998; Williams, 2010), democracy (e.g.

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Phongpaichit & Piriyarangsan, 1994; Rose-Ackerman, 1996) and the social responsibility of companies (e.g. Rodriguez et al., 2006).

The sudden development of corruption as a much-debated issue can be explained with the model of '*social maturity states'* (Zadek, 2004, p. 4). The model explains how a 'social issue' develops through four states: the latent, emerging, consolidating and institutionalized state. In the *latent state*, there is there is only a weak scientific basis and main drivers of the social issue are activist communities (Zadek, 2004, p. 4). In the second, *emerging state*, there is a higher level of societal awareness characterized by a certain level of media coverage and political interest. Although hard evidence and data may still be weak, there is an emerging body of research (ibid.). In the *consolidating*, third stage, academic insights are translated in practice such as sector-wide, voluntary standards and collective initiatives. Also, there is litigation and an increasing support for legislation. In the *institutionalized state,* there are legislation and norms established (ibid.).

The model of social maturity states can be used to explain the increasing interest in corruption as a research subject. Also, it helps to understand that trends in corruption research are embedded in the development of corruption as a social issue. This development is characterized by a continuous reinforcement of public awareness, academic research and anti-corruption practice (figure 1), driving the topic of corruption through the four states of social issue maturity.

Figure 1: Development Cycle of Corruption as a Social Issue

The following subsections outline the development of academic research on corruption during the last decades and put it in the context of the rising public awareness and development of anti-corruption practice. By structuring this development along the four social issue maturity states (latent, emerging, consolidating and institutionalized) it is

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described how corruption has become a research subject that today has captured the interest of a variety of sciences and is one of the most debated topics worldwide (Rabl, 2008, p. 16).

2.1.1 Latent State of Corruption as a Social Issue

Often, problems only become recognized and openly discussed if they have amounted to a serious crisis (Senge, 1990). For instance, the obvious need for financial regulation became topic of political debate after the global financial crisis of 2008 (Lo, 2009, p. 2). After the catastrophe in the Fukushima Diichi power plant in 2011, various countries saw massive demonstrations against nuclear energy (Bloomberg Businessweek, 2011; Dickie, 2012). Although problems may have existed for a long time, it is the crisis that raises the awareness of the public, motivates trends in academic research and triggers political and/or legal action.

In this regard, it is perhaps no coincidence that Rose-Ackerman's article on 'the economics of corruption' (1975), the first contribution on corruption receiving wide attention (Ades & Di Tella, 1997, p. 496), was published one year after the resignation of the President of the US, Richard Nixon, in 1974 due to the Watergate scandal[3]. This was about the same time in which the bribery scheme of Lockheed, a company that produced military aircrafts, became public.

Drawing upon Gary S. Becker's theory of crime (1968), Rose-Ackerman (1975) developed a theoretic model that explained the relationship between market structures and the occurrence of corruption in government contracting. The model explains corruption as a decision-making problem of civil servants and firms competing for government contracts. Like Becker's theory of crime, Rose-Ackerman's model incorporated the expected penalty and the probability of conviction as variables in the preference functions of the public official and the bribing firm.

[3] The Watergate scandal occurred during the presidency of Richard Nixon; it resulted in the indictment of several of Nixon's advisors and his resignation on 9 August 1974. The scandal takes its name from the Watergate complex in Washington, D.C., the site of a 17 June 1972 break-in into the Democratic National Committee headquarters. The break-in was one of several illegal activities authorized and carried out by Nixon's staff. Other illegal activities included campaign fraud, political espionage and sabotage, illegal break-ins, improper tax audits, illegal wiretapping, and a "laundered" slush fund used to pay those who conducted these operations. For more insights and information on the Watergate scandal, the author recommends the movie by Alan J. Pakula "All the president's men" (1976).

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In spite of Rose-Ackerman's important theoretical contribution, which advocated a change in the US legal statue, corruption did not become a much-debated topic in academic literature until the 1990's (Tanzi, 1998b, p. 559). Corruption was generally discussed in the context of economic growth in developing countries (Bayley, 1966, p. 719; Nye, 1967, p. 418; Quah, 1988, p. 80). For instance, Bayley (1966) explicitly discussed the effects of corruption in a developing nation. Gould and Amaro-Reyes (1983) outlined different forms of corruption in various developing countries and the classic of Klitgaard and Klitgaard (1988) proposed various remedies for political reforms in developing countries.

According to the model of social issue maturity, the limited public and academic interest for corruption in this period can be explained with the lack of evidence on the negative political, economic and social effects of corruption. In fact, most contributions on corruption between 1960 and 1990 revolved around the question whether corruption is to be seen as harmful practice (Pieth, 1997, p. 120). In 1982, Gould and Amaro-Reyes pointed out that one of the difficulties in conducting research on corruption is the disagreement over the effects of corruption (1983, p. 3).

The two opponent views that discussed corruption can be termed as the 'moralists' and the 'revisionists' arguments (Ney, 1967; Waldman, 1973; Johnston, 1986). The 'moralists' (a name that was attributed by the opponents of the latter) saw that corruption is harmful for societies and governments because it erodes legitimacy and economic development (Johnston, 1986, p. 459; Ney, 1967, p. 418). One of the classics in this respect is the book "Controlling Corruption" by Klitgaard and Klitgaard (1988), which provides a theoretic account for various negative effects of corruption on an economic, political and social level.

'Revisionists' in contrast, argued that corruption may have positive effects since it could speed up cumbersome bureaucratic processes, buy political access for the excluded and perhaps even de facto produce policies more effective than those through legitimate channels (Johnston, 1986, p. 459). In this respect, Nathaniel H. Leff (1964, p. 11) argued: "If the government has erred in its decision, the course made possible by corruption may well be the better one." An alternative statement which exemplifies the tone in this strand of literature is that of Samuel P. Huntington (1968, p. 386)[4]: "In terms of economic growth, the only thing worse than a society with a rigid, over-centralized, *dishonest* bureaucracy is one with a rigid, over-centralized, *honest* bureaucracy". Hence, revisionists suggested that corruption –under certain political conditions– might have possible benefits like the increase of efficiency (e.g. Lui, 1985; Beck & Maher, 1986; Lien, 1986).

[4] Highlights set by author.

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A striking feature of the early academic contributions on corruption was that the discussion of the possible harm of corruption was confined to theoretic argumentation (Ades & DiTella, 1997). This limitation was due to the lack of data for empirical examination of corruption. Basically, the little empirical data that existed was based on case studies but not on comparative data (Sandholtz & Koetzle, 2000, p. 33). The lack of comparative data impeded any conclusions on the effects of corruption. Consequently, researchers on corruption found it difficult to provide clear and coherent policy recommendations (Ades & Di Tella, 1997).

Although academic research on corruption was still somewhat restricted in the 1970's, the Watergate scandal triggered public awareness concerning the questionable conduct of the political elite in developed countries like the US (Posadas, 1999, p. 348; Weaver et al., 1975). It also led to the first legal initiative that was taken by the US with the passing of the Foreign Corrupt Practices Act (FCPA) in 1977 (Pieth, 1997, p. 122; Posadas, 1999, pp. 350-353). Among others, the FCPA prohibits the bribery of foreign officials and applies to any company that trades on the US security market (Pines, 1994, p. 189; Posadas, 1999, p. 360). Although the FCPA was a truly innovative step, for it was the first national legislation that prohibited bribery of foreign officials, it was not enforced very rigorously. From 1977 until 1990, the Securities and Exchange Commission (SEC) only filed six FCPA cases (SEC, 2014). Since the US was the only country to prohibit foreign bribery, many US companies complained about the competitive disadvantage that the FCPA caused them (Elliott, 1997, p. 200; Pines, 1994, p. 190). In Germany for instance, bribes paid to foreign officials were even deductible from the corporate tax (Glynn et al., 1997, p. 22; Schilling, 2004, p. 22). The strong opposition against the FCPA consequently led to an amendment of the latter in 1988, relaxing a number of clauses (Posadas, 1999, p. 359; Pieth, 1997, p. 122).

Summary of the latent state: The latent state of corruption as a social issue is characterized by a low level of public awareness of corruption as a serious and global problem. This can be explained by the very limited amount of research on corruption, which was confined to a theoretic discussion of the negative aspects of corruption. Consequently, the latent state also saw a limited legal engagement to curb corruption.

2.1.2 Emerging State of Corruption as a Social Issue

The 1990's can be regarded as the period where corruption emerged as a social issue or as Ades and Di Tella coined it a "hot issue" (1997, p. 496). In 1998b, Tanzi states, that the "degree of attention paid to corruption in recent years is unprecedented. For example, in its

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end-of-year editorial on December 31, 1995, The Financial Times characterized 1995 as the year of corruption" (p. 560). Glynn, Kobrin and Nyn state in 1997 that they believe the world to have reached "an historical turning point in humanity's long wrestle with corruption" (p. 8).

A number of authors have explained the "eruption" of interest for corruption with a battery of reasons (Nyn, 1995; Glynn et al., 1997; Tanzi, 1998b). First, the heightened interest can be explained by the unveiling of a series of corruption scandals like the Elf-Aquatine scandal in France and the Tangentopoli scandal in Italy, which demonstrated the vast scope and extent of corrupt practices. Also, the rising awareness of corruption as an explanation for other economic, social and political problems was driven by the Non-Governmental Organization (NGO) 'Transparency International', which was founded in 1992 and would have a major impact on the development of anti-corruption worldwide (Tanzi, 1998b; Glynn et al., 1997).

Tanzi (1998b, pp. 560-562) explains the rise of attention towards corruption in the 1990's with a number of geopolitical and economic changes. The end of the Cold War led policy makers to stop ignoring the political corruption that existed in particular countries just because the latter were in the right political camp (ibid.; Rose-Ackerman, 1999). Further, Tanzi refers to increasing number of democratic governments and free and active media that allowed a discussion of corruption. Globalization is argued to have brought individuals from countries with little corruption into frequent contact with those from countries where corruption is endemic. These contacts have increased the international attention paid to corruption (Tanzi, 1998b, p. 561). Although Tanzi's list of possible reasons for the growing interest in corruption may not be comprehensive, the collection of possible explanations indicate that the geopolitical and economic changes of the 1990's contributed to the rising awareness of more people towards the problem of corruption.

The emerging state also saw an exponential growth of academic corruption literature. A fundamental basis for the growing amount of empirical studies was provided by indices that aimed to measure levels of corruption across various countries[5]. The general recognition that the arguments justifying corruption on grounds of a gain in efficiency only apply as a "second-best" solution (Bardhan, 1997; Jain, 2001) began to dominate the discussion on the effects of corruption. On a conceptual and empirical basis, Kaufmann (1997) strongly criticized the literature that portrayed corruption as a "grease-the-wheels" solution. Also

[5] Indices were available for instance from International Country Risk Guide (ICRG), Business International (BI) index, Transparency International (see chapter 4.2.2).

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Ades and Di Tella (1997) argued against the "grease-the-wheels" literature by referring to corruption as being rather the "sand-in-the-machine".

Yet, evidence of the negative effects of corruption was still weak as there were only a handful of studies that estimated the costs of corruption (e.g. Krueger, 1974; Bhagwati, 1982). Hence, the focus of academic research in the 90's became the empirical investigations of effects and consequences of corruption on a cross-national basis (Lambsdorff, 1999a).

Until today, the most-cited empirical contribution on the negative impact of corruption is the work by Paolo Mauro (1995). He was the first scholar to investigate the effect of corruption on economic performance on a cross-country basis (Ades & DiTella, 1997, p. 500; Lambsdorff, 1999a, p. 5). In a sample of 67 countries, Mauro finds a negative correlation between corruption and the ratio of investment to Gross Domestic Product (GDP). A one-standard-deviation improvement in the corruption index is estimated to be associated with an increase in the investment rate by about 3% of GDP (even after controlling for some other determinants of the latter, and correcting for a possible endogenous bias in the data). The negative relation seems to hold even in subsamples of countries where bureaucratic regulations are reported to be cumbersome, indicating that corruption, as a way of bypassing these regulations may not have been very beneficial (Mauro, 1995, p. 704).

In response to Mauro's findings, a number of scholars used different corruption measures and a different selection of countries to conclude that their results support Mauro's findings. For instance, Knack and Keefer (1995) incorporated corruption among other explanatory variables into one single index of 'institutional quality' and found a negative correlation between the latter and the levels of corruption. Brunetti, Kisunko and Weder (1997) used a corruption index of the World Bank to reinforce Mauro's results as they concluded that corruption significantly reduces the ratio of investment to GDP. Mauro (1997) provided further backing for his results by presenting a larger sample of 94 countries and by also making use of another corruption data set. Brunetti and Weder (1998) used the same source to show in a sample of 60 countries that corruption has a significant negative impact on the ratio of investment to GDP. Elliot (1997) used Transparency International's Corruption Perception Index and presents similar results.

Next to the effects of corruption on investment, the 90's also saw scholars who examined other consequences of corruption that could influence the economic development of a country. Tanzi and Davoodi (1998) for instance, examined the impact of corruption on the

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volume of public expenditure and efficiency of allocation. The quality of investments plays an important role in the productivity of capital and, hence, GDP. The authors suggested that corruption lowers the quality of the infrastructure as measured by the condition of paved roads and power outages. They concluded that corruption reduces growth by increasing public investment while reducing its productivity because of higher levels of government consumption and because of the reduced quality of existing infrastructure and by lowering government revenue (p. 20).

Another prominent contribution is that of Wei (2000), who showed that corruption influences foreign direct investment. His database includes bilateral capital flows between 14 source and 45 host countries in 1990 and 1991. Controlling for other factors such as GDP per capita, Wei demonstrated that the impact of corruption in isolation on foreign direct investment (FDI) is no different in East Asia to that of other countries. His general conclusion was that corruption has a significant negative impact on FDI. For instance, he found that an increase in the corruption level from that of Singapore to that of Mexico has an equivalent effect on FDI as when raising the tax rate by over twenty percentage points.

Furthermore, Phongpaicht & Piriyarangasan (1994) showed empirically that corruption causes losses of public funds due to the inflation of project cost from 20-40% and by decreasing growth through the motivation it gives firms to operate in the unofficial sector. Gray and Kaufmann (1998) show that firms have greater capital costs when operating in countries with higher levels of bribery.

Next to the negative economic effects of corruption, some scholars examined the political effects of corruption. It was argued that extensive public sector regulations are the result of a deliberate strategy by civil servants to increase their clients' willingness to pay bribes (Rose-Ackerman, 1999; Tanzi, 1998a). Assuming that bureaucrats are driven by rational, self-serving motives, the logical presumption is that they will seek even more ways to create bribe-producing delays. This line of reasoning explained the observed resistance from bureaucrats for public sector reforms.

In this regard, Winters (1996, p. 166) asserted that the strongest resistance to tax reforms in Indonesia came from the tax officials themselves, since they had the most to lose from the depersonalisation and simplification of the tax system. Flatters and Macleod (1995, p. 409), also referring to Indonesia, stated that tax collectors actively opposed simplifications in property tax administration, income tax laws and tariff structures.

Corruption has some particularly "important political repercussions in that it has a direct effect on the rules of the political game and the operating rules of the political system"

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