STRUCTURAL CORRUPTION AND ITS INFLUENCE ON THE BUSINESS ENVIRONMENT

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Abstract

In modern countries, corruption is still a major problem in business environments. According to the World Bank, corruption is synonymous with abusing public office for private gain. The level of corruption is defined by the amount of the fee paid for operating a certain business. Corruption appears in different forms. This is the relationship between corruption and bureaucracy. Corrupt behavior may ensue in countries, where the line between the market and the state is not clear and is not even properly regulated; where distinctions between what is public and what is private are obscure. In the same way, regulations invite economic agents to find new ways, including bribing public officials, to secure favorable interpretations.

The aim of the article is to show what is structural corruption and how does it effect the business environment; to give examples from the less corrupted countries and to compare the strengths and weaknesses of different methods of combating corruption.

Keywords: structural corruption, bribery, business environment, government.

JEL Classification: F23, K42

Introduction

Corruption is not a new phenomenon and it appears in different forms. For example, politicians are making decisions that appeal to the companies that fund them, not for common good.

Corruption can be also seen in many other forms along with bribery. Even though not all are as clear as bribery, they have a great influence in the business environment. For example, many big organizations are co-operating with or owning a large sports team or affiliated organizations. Using that power, they make sure the affiliated organization would benefit from their business actions. One of the features of the structural corruption is the use of your relations with someone to get what you want. But it is not that simple - structural corruption is just a method evolved from bribery. High levels of corruption push entrepreneurs underground and this is one of the main factors of the increasing role of the shadow economy in all countries.

Scandinavian countries are one of the less corrupt countries. Still, the business environment there has been affected by corruption. Corruption is a very powerful tool when a person wants to pursue his/her own interests, so sometimes it just is the best or easiest way to make sure that the person gets what (s)he wants. Although there are lots of regulations trying to prevent corruption, the world is in continually changing and big companies are getting even bigger. Global companies are pursuing their own interests and countries are depending on the taxes those companies pay and the employment they provide.

The business environment has changed and organizations are becoming larger than countries, they do not depend on their native countries anymore, but the countries now depend of them. In the end, corruption shakes the economical stability of a country, decreases the productivity of a country’s infrastructure, reduces tax revenues and finally prevents the government from keeping public expenditures under control.

Corruption influences the business environment, but its impact is decreasing continuously and the main reason behind this is the change in peoples’ attitude and saturation to ethically questionable actions. Any realistic strategy must be based on the principle that there are always two sides in a process. It means that supply and demand also exist in the case of corruption. It can be pointed out that the war against corruption often involves reforms. Therefore, corruption will decrease only in those countries, where governments are willing to substantially reduce some of their functions.

Overview of related literature

There are different causes of corruption and they can be classified into three main areas – environmental, individual, and firm related. Aidt (2003, p. 633) made a distinction between four different analytic approaches to corruption (for alternative categorizations see, for example, Rose-Ackerman, 1999) which highlight two important considerations in the theoretical analysis of corruption: (a) the degree of benevolence of the government official in charge of implementing policies and designing institutions; (b) the role of institutions versus history as a determinant of corruption levels. These categories are:
Efficient corruption: corruption arises to facilitate beneficial trade between agents, which would not otherwise have been possible. There are two specific channels through which corruption can enhance allocative efficiency: (a) corruption speeds up bureaucratic procedures (“greases the wheels”); (b) corruption introduces competition for scarce government resources. It is also argued that “in the context of pervasive and cumbersome regulations in developing countries, corruption may actually improve efficiency and help growth” (Bardhan 1997, 1322; see also Saha 2001, Shleifer & Vishny 1994). This statement is based on the “second-best” argument (when distortions exist, additional distortions in the form of black-marketeering, bribes etc. may actually improve welfare) or on the “speed money” argument (corruption may reduce delays in moving files in administrative offices and speed up moving in queues for public services).

Corruption with a benevolent principle: corruption arises when a benevolent principle delegates decision-making power to a non-benevolent agent; the level of corruption depends on the costs and benefits of designing optimal institutions. Whenever authority is delegated to a bureaucracy, the potential for corruption is created. The actual level of corruption is determined by how well the institutions governing the bureaucracy are designed. The key theoretical question is: Is it optimal for a benevolent principle to design a corruption-free bureaucracy? And if not, corruption can be viewed as an integrated part of optimally designed institutions (see the classical study of Becker and Stigler 1974, also for example, Rijkseghem & Weder 2001, Laffont 2000, Acemoglu & Verdier 2000, 2003).

Corruption with a non-benevolent principle: Corruption arises because non-benevolent government officials introduce inefficient policies in order to extract rents from the private sector. The level of corruption depends on the incentives embodied in existing institutions. This approach starts from the premise that all agents (bureaucrats as well as politicians) are corruptible. “The grabbing hand model” developed by Shleifer & Vishnny (1993, 1998) describes the idea that all government officials can be expected to seek rents. Empirical evidences in the framework of this approach are reported by Leite & Weidemann 2002, De Mello & Barenstein 2002, Gupta et al. 2001, Bardhan and Mookherjee 2000, Ades & Di Telia 1999, Shleifer and Vishny 1993).

Self-reinforcing corruption: the reward of corruption depends on the incidence of corruption due to strategic complementarily. The level of corruption depends on history (for given institutions). There are different mechanisms which have the potential to make corruption self-reinforcing: (a) it is hard to audit corrupt officials in societies where corruption is more prevalent; (b) corrupt individuals want to interact with other corrupt individuals; (3) the reward to rent-seeking relative to entrepreneurship is high in societies where the most individuals seek rents and accept bribes (Aidt 2003, 647, see also Acemoglu 1995).

Among organizations that fight corruption, Transparency International (TI) is the most prominent. It has influenced public perception and its corruption perception index, rating countries has received much publicity. Transparency International (TI) has ranked 180 countries by Corruption Perceptions Index (CPI) in 2008 and 1780 countries in 2010. CPI is a composite index. Because the index is based on polls, the final results are subjective and to some extend are less reliable for countries with fewer sources. Also there are differences between countries: for example, a matter viewed as acceptable tipping in one country may be considered as bribery in another. Therefore, the poll results are supposed to be understood very specifically, measuring mostly public perception, rather than presenting an objective measure of corruption. The scores range from 10 (squeaky clean) to 0 (highly corrupt). A score 5.0 is the number TI that considers the borderline figure distinguishing countries, which other have or do not have serious corruption problems. Illustration of this can be seen in the Table 1.

In 2008, Estonia stood ranked 27th among 180 countries by the Transparency International’s CPI (6.6 points) and in 2010, the situation has improved a little bit, with Estonia ranking 26th, but among 178 countries (6.5 points). Our neighbor country, Finland (9.0 points), was ranked as a least corrupt country, the 5th position in 2008, and in 2010 the 4th position (9.2 points). Russia was on the 147th position in the ranking list by CPI (2.1 points) in 2008 and during last year has dropped from this position and became 154th with the same score (2.1 points). Lithuania took the 58th place (4.6 points) and Latvia 52nd place (5.0 points) in 2008. Lithuania has improved the position in 2010 and ranked 46th with the score 5.0 points, but Latvia has lost its positions and became the 59th (4.3 points). Sweden has lost its position during these years, being on the 1st place with 9.3 points in 2008 and has moved to the 4th position with 9.2 points. the During the last two years (2008 to 2010) almost all countries presented in Tab.1 more or less have the stable position of CPI. Sweden, Finland and Denmark are usually ranked among the least corrupted countries from year to year. The explanation given for this phenomenon is that the named countries have a well-functioning political system and a relatively efficient bureaucracy, also they are characterized by a well-working legal system and high
levels of trust between citizens. Also it might be a genetic characteristic trait or the educational systems in these countries that make the people of these countries the cleanest in the world.

Table 1. The Corruption Perceptions Index for the countries of the Baltic Sea Area, Ukraine and Belarus

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<td>Finland</td>
<td>9.0</td>
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<td>Denmark</td>
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<td>Sweden</td>
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<td>14/180</td>
<td>8.6</td>
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<td>52/180</td>
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<td>Poland</td>
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<td>5.3</td>
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<td>Belarus</td>
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<td>151/180</td>
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<td>147/180</td>
<td>2.1</td>
<td>154/178</td>
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<td>Ukraine</td>
<td>2.5</td>
<td>134/180</td>
<td>2.4</td>
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Source: The 2008; 2010 Transparency International Corruption Perceptions Index

Transparency International has found that developing countries suffer from structural corruption. 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. 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. Corruption in some of these countries is so pervasive that it is hardly surprising to learn of corruption among its senior administrators and political leaders.

Structural corruption’s influence to the environment in Scandinavian companies

Although Scandinavian countries are one of the least corrupt countries, the business environment has still been affected by corruption. Corruption is powerful when you want to watch your own interest, so sometimes it just is the best or easiest way to make sure that the right things from your point of view will happen. Although there are lots of regulations trying to prevent corruption, the world is in continuing to change and big companies are getting even bigger. Global companies are watching their own interest and countries are depending on the taxes and employment that those companies are providing. The business environment has changed and organizations are becoming bigger than countries, they are not depending on their native countries anymore, but the countries are depending of them. Corruption can help companies grow and at the same time help countries to develop their economy. Nowadays, politicians are watching companies’ assets. For example, in Finland, the government made a law called “Lex Nokia” where organizations can read their workers’ emails to avoid corporate spying (YLE, 2009).

Now, in Scandinavian countries, corruption appears only a little bit as we can see on the table 1. That’s mainly because the countries have achieved the status of welfare state and at that point the small corruption becomes useless, because no one is ready to risk their careers to get a small sum of money. So, in a welfare state, it is much more difficult for a small company to become a big one, because they have to go through official channels. We might say that the base of the business environment in Scandinavia is fair, but it has been affected by corruption and nowadays, the corruption in Scandinavia is well hidden into the social structure.

It is quite clear that bribery doesn’t play a large role in Scandinavian countries. As shown in this research, there are other ways of corruption also and the term that will unite those is structural corruption and it is the biggest problem in Scandinavia. So basically, structural corruption is when you use your relations with some person to get what you want. But it is not that simple: structural corruption is just a method evolved from bribery. In Finland, 1970s and 1980s were the decades where every problem was solved with bribery and Nokia’s ex-director Harry Míldh has his utterance: there is no man so insignificant that he was...
not worthwhile to bribe. From those times, this old chap community has been developing, where people are using their relationships to drive their own assets. This is very usual in more developed countries.

Other corruption trend in Finland has been that companies co-found organizations and give support to the politicians trough them. Finland’s politicians have to publically announce everyone that supports them more than 1700€. One of these organizations was Kehittyvien Maakuntien Suomi Ry. They gave more than 100 000€ to support a politician in election campaigns only one and half year after founding the organization (Talous Sanomat, 2008). The organization’s structure was blurry and when the media started to examine them, it was noticed that the organization was really controlled by many of Finland’s biggest businessmen. Of course businessmen can support politicians, but when it is done like this it raises questions. Especially when one of the politicians that had money from them was Finland’s ex-prime minister Matti Vanhanen, who at the same time was accused of taking bribes. Finland’s national TV station YLE accused Mr. Vanhanen of getting construction materials from a company who got many jobs from the institution in which Mr. Vanhanen used to be the chairman (YLE 2009).

Also, in Finland, the government-owned Gun Company Patria has been suspected of bribing officials in Slovenia. Patria sold 136 transport wagons in the year 2006 to Slovenia and in has been suspected that Patria’s affiliated agent bribed the officials in Slovenia (Niemi, 2008). When the Corruption law is not strict, organizations try to find new loopholes such as using affiliate companies and agents to do the dirty work for them. In Finland, as shown earlier in this research, structural corruption is a big problem. There have been politicians from Prime Minister to many other politicians under suspicion of doubtful decisions. All of this is working in a grey area - there are no regulations forbidding a person to be in the city council and in confidential posts in some company same time. Also, it is very often that directors from big companies are used as experts in government organizations, but is it ethically correct that they are making decisions about donations to their own employer. This kind of behavior bed the competition in the business environment and, in my opinion, this fulfills every aspect of corruption. The present community has gotten so used to this kind of activity that many don’t even consider that this kind of actions might be somehow dubious. Old chap mentality has become so normal that knowing right persons is more important than the idea or your skills. The European Commission published a research, where 33% of Finns believed corruption to exist in the city level and 36 in the governmental level (European Commission, 2008). I think that this research shows us that most of the Finns do not consider structural corruption as corruption, because everyone is used to this old chap mentality.

How companies prevent corruption inside their organization

Although there is an old chap community in Scandinavia, there are also many good examples of ethical organizations and ways to prevent corruption in their organizations. In this research we are using two examples, one from Sweden - Hennes & Mauritz (H&M) and one from Finland - Stockmann. Both of these organizations are well known for their uncorrupt ion policies and both of them have many similarities on how to prevent corruption in their organizations. In H&M and Stockmann, the fight against corruption starts with the salesperson and goes all the way up to the directors, both of them have a clear and strict code of ethics and they make sure that everybody follows those codes. In Stockmann it is strictly forbidden to give free samples suppliers or discounts for customers.

Also, Stockmann has been in tough positions when expanding their business activities into Russia. Stockmann has continuously refused to give bribes, although native officials delayed the construction of their Store in St. Petersburg. (Lassila, 2007; 2008).

H&M is one of the biggest clothing corporations in the world and is very often suspected of using child labor etc. But they have strict ethical codes that everyone has to follow and they even have their own corporate social responsibility team that follows the actions of their workers and subcontractors. The code of ethics for all workers in H&M reads:

“H&M’s Code of Ethics contains guidelines on how we, as H&M employees, are expected to act in various situations when we represent the Company in a business context.

H&M has a zero tolerance policy on bribery and corruption, and this applies to all the Company’s business dealings and transactions in all the countries in which the Company or its subsidiaries and business partners operate.

As an employee of H&M, you must not accept bribes in any circumstances. In addition, you must not offer bribes on behalf of the Company to any person, whether privately employed or in the public sector, or any organization. The laws of each country regulate what is regarded as a bribe.” (Hennes & Mauriz, 2009).
This kind of policy prevents many problems that could appear because of different culture, but when a global organization has common rules, it prevents problems that might occur because of cultural differences.

There are many neutral organizations that are helping companies to conquer corruption. For example, the United Nations Global Compact program is a program where companies have to agree on certain policies to be a part of the program. These kind of mutual agreements are very powerful and there are two main reasons why these are working. Firstly, there is a third party inspecting organizations so that all requirements are fulfilled. And the second reasons, perhaps the biggest reason, is that customers are getting more and more aware and they are more willing to buy products from organizations that are more socially responsible.

Many global organizations have understood that people are more aware and they have to change their ways of doing business. It can be seen from the above Fig.1. Global Compact signatories have rapidly grown during the last years, so the pressure from normal people drives companies to act more responsibly.

Concluding Remarks

In developed countries and especially in Scandinavia, corruption still plays a role in the business environment, though the role is not as dominating as it’s been a couple of decades ago. The forms of corruption have evolved from bribery to modern structural corruption, because of the unrestrictive legislation.

Corruption is still a major problem and it bends the competition in many business areas. The one dominating form of corruption is the old chap community where your own personal relations affect your decisions.

But many global organizations like Hennes & Mauriz has started to fight against corruption in cooperation with organizations like the United Nations. The main factor of this change is the increased awareness of people and their demand for equality.

Corruption has major influence on the business environment, but its impact is decreasing continuously and the main reason behind this change is the change in people’s attitude and saturation to ethically questionable actions.

The contacts between less corrupt and more corrupt countries have intensified in the last decade. All indications show 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 more importantly, because, over the years, the reporting of corruption and monitoring of corrupt practices has improved tremendously. In order to reduce worldwide corruption that affects businesses, there has to be a concrete and well-coordinated effort on the part of all concerned. The parties that must take an active role in this effort are:

- Individual countries’ governments
- International organizations
- International firms
It is quite evident 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, but not impossible.

References