Corruption in State Administration

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1. Introduction
Corruption can arise in any bureaucracy that has the authority to allocate benefits and impose costs. Program designers need to acknowledge and control such risks, but “best practice solutions” are seldom obvious. International development institutions propose long lists of anticorruption initiatives for state bureaucracies, hoping that at least some will be effective. But effective solutions in one context may be entirely ineffective in another.2

Nevertheless, general economic principles can help guide reform so long as they are interpreted in the light of each country’s particular situation. We turn for policy insight to models of bureaucratic behavior, especially the economic literature on asymmetric information and sanctions. In this literature, individuals are expected to make rational choices given their preferences and the limited information at their disposal. However, scholars often present these models abstractly without a discussion of how they interact with the law and with bureaucratic realities. We respond to that weakness by providing the intuitions behind the economic theories and discussing their practical value in anti-corruption policy design. We show how insights from economic theory can elucidate efforts to deter corruption in administrative hierarchies.

The chapter proceeds as follows. Section 2 shows how economic insights can contribute to understanding the nature and prevalence of corruption. Section 3 argues that economic principles can help reformers move from understanding to control of corruption. Section 4 discusses alternative policies to deter civil servants from engaging in corruption. Section 5 evaluates compliance regimes for state institutions and the available sanctions. A conclusion follows.

2. Explaining corruption
Economists sometimes distinguish between capture or collusive corruption (where the civil servant and the client secretly collude for their common benefit) and extortive corruption (where the client feels compelled to make a bribe payment).3 In practice, it is difficult to draw the line between cases of collusive corruption and extortive corruption, especially because most bribe-payers prefer to portray themselves as victims of corruption (regardless of the benefits they obtain). A more neutral perspective considers the allocation of bargaining

1 Jennifer Arlen, Paul Lagunes and Linda Gröning made very helpful comments on earlier drafts.
3 See Rose-Ackerman (2010) for a review.
powers between the parties involved in the corrupt deal. The more important a decision is for a client or the greater the power of the civil servant, the lower is the bargaining power of the client and the higher the share of the gains that a corrupt official can appropriate in the form of a bribe, everything else equal. The most extreme situation is one where the official is so powerful that he can threaten to harm the client through unlawful means unless paid off. Outside of such cases, however, corrupt deals tend to benefit both parties, typically at the cost of some government aim or function. These deals can range from pure extortion where the official behaves exactly as would an honest and competent official except that he is paid for his actions. At the opposite extreme, is a bribe paid to get a benefit to which one is clearly not entitled or to avoid a legitimate cost, as when a bidder bribes to obtain a government contract that should have been awarded to someone else.

We seek to explain what governments can do to deter corruption within their own ranks. To simplify and focus the discussion, we concentrate on a state institution with a hierarchy of employees who have the authority to allocate certain benefits to qualified clients. Although systemic corruption, of course, can penetrate state institutions, up to and including the top political level, we deal here with the intermediate case where top management level seeks to promote integrity. An honest higher level official has oversight responsibility—for example, a government minister who seeks efficiency and legality, consistent with publicly recognized goals. In this chapter, we concentrate on such bureaucracies, and we do not consider the background political environment or outside institutional checks. We also leave to one side the special case of publicly owned firms.4 Thus, we direct our contribution to high level-officials with a professional commitment to honest government who may gain insights from the economic analysis of reform alternatives. We emphasize two key loci of corruption—the allocation of scarce public benefits and the assessment of qualifications for receiving a benefit or for bearing a cost.5

2.1. Scarcity

State administrations allocate scarce resources according to given rules and standards ostensibly designed to serve the public interest. Scarcity may arise in public health services, in access to schools, in the number of ships able to enter a port, in the number of production licenses for some good, and so on. If the benefit cannot legally be sold to the high bidders, a corrupt “market” may operate where the balance between demand and supply determines the bribe-price. If no official has significant bargaining power, the corrupt system may operate like a competitive marketplace that excludes the honest and the poor. A uniform bribe-price is likely because anyone charged too high a bribe can approach another official for a better deal. Of course, even here the “market” is likely to diverge from the competitive model because of a lack of information about corrupt deals; they are kept secret not only from law enforcement

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4 Much of the material in this section and the next summarize arguments in Rose-Ackerman (1978, 1999). These sources also discuss some of the issues put to one side here.
5 A range of factors are relevant for understanding the individual propensity to engage in corruption. We have reviewed the literature in other publications, see Rose-Ackerman (1999), Rose-Ackerman and Palifka (2016), and Søreide (2016).
authorities but also from other demanders. Nevertheless, the main beneficiaries will be those with a high willingness to pay who cannot be extorted to pay more than the equilibrium price. In practice, other factors may influence the size of the bribe besides the underlying level of demand and supply. For example, honest officials and beneficiaries will not participate in corrupt transactions, shrinking the size of the corrupt market. In addition, lobbying and other forms of persuasion can also influence officials’ choices and can substitute for illegal payoffs.

If there is only one public official with de facto control over benefit allocation, he or she has monopoly power and might be able to negotiate bilaterally with each client with the bribes kept hidden from others. The official could then collect the clients’ whole “demand curve” – in the sense that those who obtain the benefits pay a bribe equal to their maximum willingness to pay. Those unable to pay enough, or unwilling to make illegal payments, do not obtain the benefit. There is no single, market-clearing bribe price. This result, of course, assumes—as in all analyses of price discrimination—that the benefit cannot be resold by the low bribers to those with high willingness-to-pay. The secrecy and illegality of payoffs is likely to mean that bribers have very poor information about the payoffs of others so that bribe-price discrimination can be stable.

In such a situation, the single official can create shortages even if the benefits are not scarce by law. For example, even if there is space in the port for all ships to offload their cargoes, the official controlling the port (or customs clearance) may restrict the shipping firms’ entry to maximize bribes, just as a private monopolist restricts supply (Shleifer and Vishny, 1993). Thus, the source of bribery is not scarcity in the underlying program, per se, but rather the official’s monopoly control over the allocation of the benefit. That control permits the official to extract payoffs from demanders in accord with their willingness to pay bribes.

2.2 Qualifications

Sometimes officials have discretion to judge who is qualified for a public benefit. Assume that anyone with certain qualifications should be able to obtain the benefit. Scarcity is not the problem, but bribery is possible because the allocation of the benefits is controlled by a gatekeeper who is able to deviate from the stipulated criteria without detection. The qualification criteria are stipulated formally by a directive or law. With corruption, the gatekeeper alters the criteria, so that informally, other criteria (such as bribe payments) apply.

Consider for example the award of drivers’ licenses – which clearly should depend on a candidate’s qualifications, assessed through an exam that tests the candidate’s driving skills.

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6 Lui (1985) presents a theory showing how paying bribes for a better position in a queue serves as an efficient auction-procedure. One problem with this result is that many public services are supposed to be free of charge. Corruption condoned because of efficiency concerns can easily undermine a program’s distributional goals (Rose-Ackerman, 1978:106). Second, public officials’ efforts to avoid detection and arrest may add to the social costs of corruption. Third, informal payments typically trigger undesired externalities – such as an adverse selection of the unscrupulous into the state administration and a higher inclination of individuals to offer bribes to induce officials to deviate from formal rules.

7 Monopoly control can arise not only when one official misuses of his or her authority, but also if several officials with similar or different responsibilities collude to share bribery receipts. For an illustrative case see Olken and Barron (2009) on corruption along trucking routes in Aceh, Indonesia.
and knowledge of traffic rules. With corruption, the exam becomes irrelevant and the payment of a bribe determines award of a license. This is exactly what Bertrand et al. (2006) found when they used a field experiment to study corruption in the award of driving licenses in New Delhi, India. According to their study, bribery puts unsafe drivers on the road. Those who obtained their licenses in exchange for a bribe had lower driving qualifications. Those who refused to pay bribes were often found ineligible for a license, regardless of their skills, and many of those who offered bribes did not even have to take a driving test to get a license.

Assessment of qualifications for benefits is a significant part of officials’ de facto discretionary authority. Building permit offices consider proposals in light of construction requirements, neighbors’ concerns, and urbanization plans. If the applicant pays a bribe, officials may set aside some criteria—possibly with the result that housing and city developments are not up to required standards and do not perform their expected functions. Similarly, teachers might allocate grades according to bribes paid instead of student qualifications. Safety inspections of industrial plants could be influenced by bribes, regardless of the actual safety level.

Public procurement contracts create corrupt incentives that mix scarcity and the determination of qualifications. The number of contracts is limited, and tendering firms are assessed, not only on the offered price-quality combinations, but also on their integrity. If suspected or found guilty of certain forms of crime, suppliers can be excluded from participating in tenders—often called debarment. However, if the procurement agent is corrupt, the opportunity to exclude firms on a discretionary basis implies that the debarment rules themselves, introduced to promote higher integrity, may add to the decisions that can be bought with a bribe. Payoffs might, for example, eliminate an annoying competitor—excluded with the more or less legitimate excuse of suspected corruption on the other side of the globe.

Bribes are also paid to induce civil servants to speed up the processing of requests or the issuance of licenses. Officials may strategically delay files as a device for extracting payoffs even if the applicant is clearly qualified. One way to delay allocations is to find fault with applications and to introduce trivial requirements. Sometimes the law itself helps the corrupt official by its very complexity. If access to the benefit is urgent for the client, the civil servant is obviously in a more powerful bargaining position to demand payoffs in return for speed.

Civil servants can also “sell” cost-cutting decisions. The civil servant has the authority to reduce a monetary burden—such as reducing the tax imposed on a category of clients or ignoring a client’s failure to pay a fine for some compliance failure. If corruption affects the performance of the judiciary, firms may avoid monetary penalties altogether. Other examples

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8 Peisakhin (2011) reviews field experiments on corruption, including the results from Bertrand et al. (2006). Banuri and Eckel (2012) present the insights and inconsistent results from lab experiments on corruption.

9 An official’s discretionary authority may follow de jure from the broad authority assigned to the specific position, or be the de facto consequence of the higher level lack of oversight of the official’s performance.

are firms offering bribes to cut health, safety, or environmental costs. This is very similar to the case of qualifying for a benefit. The firm or individual pays to avoid a cost rather than to obtain a benefit. Scarcity does not usually limit the discretion of officials unless he or she must collect a fixed quota of tax receipts. Rather, the bribe payer seeks an individual decision to limit his or her own costs.

The bribe is likely to be higher the closer the purchased decision is to a criminal offense. The consequences of discovery are higher here than for other corrupt transactions; hence, the official must demand a bribe that exceeds the expected cost of detection and punishment. Furthermore, the official will likely also be able to bargain for a larger share of the benefits if he or she can credibly threaten to report the bribe offer. We would expect, for example, that a bribe paid to induce public authorities to ignore life-threatening pollution that is treated as a criminal offense ought to be higher than a bribe paid to overlook less harmful pollution. Likewise, the customs official who allows the importation of illegal goods (such as weapons or human organs) may demand higher corrupt payments than one who exempts importers from tariffs on legal products. In short, when the expected cost of detection and punishment is high, the minimum bribe acceptable to officials must exceed that cost. The actual level of the bribe then will depend upon the bargaining range between the minimum bribe acceptable to the official and the profits of the offender, taking into account the risks of detection and punishment for both actors.

Those who are willing to pay bribes sometimes threaten violence to limit corrupt demands from officials—the famous choice between *plata o plomo* [silver or lead (bullets)]. Mafia organizations have used this combination of bribes and threats of violence to influence public institutions’ decisions in their favor or to avoid arrest and prosecution. The threat of violence reduces the civil servant’s bargaining power. In the extreme, organized crime pays no bribes but rather operates through intimidation and threats that extend beyond civil servants to include law enforcement and the judiciary.

Shelley (2014) explains that the most serious acts of terror since early the 2000s have used a mixture of threats and payoffs to obtain benefits. Without the necessary qualifications, terrorists have been given licenses, visas, bank accounts in false names, custom clearance for illegal goods, and access to areas with restricted entry. It is difficult to control this form of corruption with higher sanctions; both bribes and threats would simply increase to compensate for the added risk, and increased threats may be relatively inexpensive for criminal organizations. Corrupt officials have little bargaining power vis-à-vis such groups.

### 3. Forms of corruption control

The control of corruption depends on the underlying mechanisms that produce corrupt deals. Without an understanding of how anticorruption controls affect both public officials and private individuals and firms, reforms may simply shift the distribution of corrupt gains

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11 A government may reduce the incentives for such corruption by separately criminalizing the crime itself and the bribes paid to avoid detection—or to penalize bribe recipients more when their illegal conduct facilitates other criminal activity (Sanchirico 2006). However, this will not necessarily deter corruption if the criminal gains are very high or motivated by fanatic ideology.
between bribe payers and recipients, while corruption continues. With that in mind, we discuss the effect of controls on the supply and demand for bribes in a “competitive” corrupt market and next discuss how controls operate in collusive environments.

3.1. Reorganizing Service Delivery

Corruption can be controlled by increasing the expected cost of corruption— that is, the risk of detection and punishment multiplied by the penalty. However, the exact impact of various forms of control is often difficult to predict, especially because civil servants will often adapt their corruption to the form of oversight. In theory, an increase in the frequency and intensity of controls ought to reduce propensities for corruption. However, even if the number of corrupt deals falls, some clients who can obtain the given benefit only through corruption (for example, because they would not qualify for honest allocations), may be willing to pay a higher bribe that compensates the official for the higher risk of being detected and punished. Hence the official may be able to maintain a high level of corrupt receipts despite the decrease in the total number of corrupt allocations.

A simple illustration of this point is provided in Figure 1. Suppose that the underlying benefit is open to all who qualify, but that each applicant must bear a qualification cost, $c_i$, that might vary across applicants. This cost can reflect both measures taken to qualify, such as an educational credential for a person or the installation of safety measures in a firm, as well as the costs in time delays and fees of dealing with the state. In addition, willingness-to-pay can be a function of the risk of being caught times the penalty, which might vary with the size of the bribe. In the example, no one wants more than one unit of the public benefit, and applicants weigh the costs and benefits of corruption compared with qualifying honestly. For simplicity, assume that everyone could, in principle, qualify, but that some would have to bear very high costs to do so. Figure 1a then illustrates how clients’ demand (D) for corrupt decisions increases as the price (p = the bribe) decreases. The quantity associated with each bribe-price, $p$, is the number of applicants who prefer corruption, with its attendant risk, to using the honest qualification process or simply doing without.

The upward sloping supply curve, S, indicates that as the size of the bribe rises, more officials are willing to accept (or extort) payoffs. Even if expected penalties rise with the size of the bribe, the upward slope implies that in this case the net benefits of corruption increase with the size of the bribe. Alternatively, it is possible for costs to rise at a more rapid rate so that officials have a maximum bribe they are willing to accept. Now assume a “competitive” market for the service where a single bribe-price allocates the corrupt benefit because the

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12 Tyler (2006, 2017) warns this is a simplified assumption and explains that norms do not always accord with formal rules and depend on the rules’ source and how they are enforced. Nevertheless, in our discussion we claim that the net benefit is important, especially for those decision makers who “are on the margin” – in the sense that they are nearly indifferent between committing the crime and staying honest. Compared to other forms of crime, corrupt actors in many cases fit the profile of rational strategic planners who are disinclined to act on shortsighted impulses.

13 A number of empirical studies confirm this point. See for example Lagunes (2012) who finds that monitoring reduces the risk of bureaucratic corruption so long as detected corruption is followed by top-down sanctions. See also Sequeira (2013), who studies the impact of changes in tariff levels on tariff evasion in the context of clearing goods through international borders. A change of tariff levels reduced the risk of corruption, although it also resulted in other forms of tariff evasion. For the control of a completely different form of crime, see Ratcliffe et al. (2011), which find that foot patrols in violent crime hotspots can significantly reduce violent crime levels.
officials cannot collude. This structure pushes the bribe to the level that clears the “market”. If an official demands too high a bribe, the client can simply turn to a different official.

Increased controls on civil servants shift the supply curve to the left to $S_2$. The change of slope is determined by the corruption elasticity – that is, how sensitive civil servants are to a change in controls. A shift from $S_1$ to $S_2$ will reduce the quantity ($q$) of corrupt decisions at any bribe-price and raises the equilibrium bribe to $p_B$. The increased control has resulted in fewer corrupt decisions, but corruption is still a problem, and bribery revenues continue to reward civil servants for their corrupt behavior. In fact, those who remain in the corrupt column are likely to earn more than they did before the crackdown—the overall number of corrupt deals falls, but they are concentrated in the hands of those still willing or able to be corrupt.

Figure 1.b illustrates the case where controls are also placed on the clients who offer bribes in exchange for corrupt decisions. The demand curve shifts to the left from $D_1$ to $D_2$, and both the quantity demanded and bribe paid decrease. However, if combined with controls on the supply side, there is a combination of effects. Quantity falls but bribe-price could be above or below its level before the crackdown. In short, added controls may reduce the number of corrupt decisions as honesty becomes relatively more attractive, but the net benefits of corruption will still be positive for some participants who will continue to pay and receive bribes.

Figure 1

In both cases, there may be some honest officials and citizens or businesses. The figures represent the opportunistic actors who decide whether to accept or pay bribes on the basis of a profit and loss calculation. Those committed to honesty may complain about the corruption of the system but feel powerless to promote change. However, if a legal crackdown induces a new group of officials and citizens to shift into the honest camp, they may be especially likely to complain about others malfeasance. In figure 1 individuals only interact through exchanging bribe payments for benefits. If, instead, corruption leads to long delays

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14 Controls on the demand side that include a reward for self-reporting may also affect the supply side if self-reporting allows enforcement authorities to obtain evidence to charge the bribe recipient.
for the honest, this may be especially irksome for those who have decided to forgo bribery. If they can be granted an amnesty for past behavior, they can be potent allies in the anti-corruption campaign.

Government crackdowns against corruption are more effective if clients—both briber payers and those who refused to pay—are willing to complain and report corrupt offers or demands. In an ordinary competitive market, trades are impersonal interchanges, but in a corrupt market officials need to identify those who will make payoffs. The official’s risk of detection will depend, first, on his or her ability to distinguish between those who will pay informally and those who will not, and second, on the relationship between the delay experienced by the honest clients and the value of their time. Vicious and virtuous cycles can occur that our static equilibrium graphs cannot capture. For example, if those willing to pay and receive bribes cannot easily identify their counterparts, such dynamics may operate. As the share of bribe payers and recipients increases, there is a greater chance that a corrupt participant will interact with another dishonest one, making corruption less risky and inducing others to shift in the corrupt direction until all but an honest remnant are corrupt. Conversely, if few are corrupt, those willing to pay may find that it is too risky to offer or extort a bribe. Their shift to honesty induces even more to give up corruption in the next period, and so on until corruption becomes very rare.15

The analysis also suggests that if the benefit of corruption is access to a legal benefit, then competition for clients – between offices or between officers within a public office - will generally reduce the risk of corruption or at least lower the payoff levels compared to a case where individuals and firms are only allowed to interact with a single designated official who exercises a form of petty monopoly power (Rose-Ackerman 1978: 137-150). The best case is one where the bribe that applicants are willing to pay falls below the minimum willingness-to-accept of the officials. Then if service delivery performance is observable, compensation schemes can depend on honest or efficient performance.

Unfortunately, increased inter-official competition for clients is not always a viable option. A police officer will often be in a “monopoly situation” where his or her judgments and decisions go unchecked. In fact, because a police officer can initiate interactions with almost anyone, he or she is free to exploit situations of petty monopoly power, even if the police force attempts to limit corruption risks.16 A small local government may not have the financial capacity to have several staff involved in sector or program decisions. Even if several officials in an office are equally able to make a particular decision, they may, in

15 See Bardhan (1997), Rose-Ackerman (1999: 107-108, 124-125). These mechanisms depend on more than revenues and risk of detection. For some, ethnic belonging and loyalty may be more important than the risk of detection. Such aspects are parts of the broader set of costs and benefits associated with corruption and their effect may well be consistent with the assumption of (fairly) rational decision makers.

16 In a study of police corruption in Kenya, Andvig and Barasa (2014) found that rotation of police officials – introduced to reduce the risk of corruption -- had the opposite effect because officers could use their authority vis-à-vis strangers wherever they were located, and with the rotation, they could move on to new areas – easily avoiding the need to see their victims again. See also Fried et al. (2010) who study police officers’ opportunity to take bribes and how they take into account their victims’ social status when demanding bribes.
practice, consult with or defer to a colleague with more expertise or better political connections who may end up being able to monopolize the process.

In some situations, however, it may be possible to introduce an element of shared authority. Instead of allocating responsibility to individual public officials according to certain geographical areas, segments, age groups, or whatever classification of clients applies, it may be possible to introduce *overlapping jurisdictions* in order to permit clients to consult an alternative official. As discussed by Tirole (1994), competitive pressures can promote better service delivery in different ways, including for control purposes. For example, instead of asking one group of civil servants to investigate the various options prior to an important investment decision, different groups can be given the task of investigating different options and eventually “compete” with each other in defending their case. Assuming a transparent process, such competition can be expected to secure a more informed assessment of options before important decisions are made. In addition, corruption becomes more difficult to carry out because more officials must be bribed and observers cannot so easily be fooled.17

These proposals for restructuring service delivery highlight the shortcomings of common anticorruption strategies that concentrate on law enforcement against officials or firms or both. Anticorruption campaigns and integrity reforms occur all over the world, but unless one studies the causes of weak performance, these efforts will not get at the roots of corruption. For example, firing civil servants suspected of corruption will have a limited effect if it simply reduces the number of officials willing to accept bribes. The result may be fewer corrupt deals but higher payoffs per corrupt interaction. One might count the decline in corrupt transactions as a success, but the most important decisions are still for sale, but for a higher price. Similarly, a policy that limits those willing to pay (demanders of public benefits in figure 1) may have little effect if the government supply of benefits remains fixed. Bribe levels will indeed fall, but the quantity of the benefit allocated corruptly may not change.

### 3.2. Collusive environments

A key problem with competition between officials in the provision of public services is the risk of collusion by either those who pay or those who accept bribes. Public officials can create “a cartel” – where those who deviate might be informally sanctioned by its members. If so, the situation is similar to a monopoly setting: If every official demands a bribe, an increase in the number of public officials making the same type of decision will not help to reduce either the incidence or the level of corrupt payments. For example, if those who operate a port collude, regardless of complaints from clients, it will be difficult to solve the problem through reorganization alone. Clients who dislike the corruption have to use an alternative port and accept the associated extra expenses – as occurred in a study of ports in South Africa and Mozambique (Djankov and Sequeira 2010). Similarly, on the demand side, a reduction in the number of bidders for a contract may simply raise suppliers’ offering prices or facilitate

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17 Jean Tirole refers to the mechanism as *indirect reward* since those involved in providing information about options, performance or something else, are rewarded for the final decision, regardless of procedures, arguments or other forms of influence.
collusion between the remaining bidders. In the extreme, both those who pay and those who receive payoffs may collude to maximize their private gains at the government’s expense. Their relative bargaining power determines the division between payoffs and monopoly profits.

If only the corrupt officials collude, they will take care to interact only with those who are willing to pay. Rather than the single market-clearing bribe-price that prevails when officials compete, officials tailor their bribe demands to firms’ ability to pay. Thus Svensson (2003), using data on Uganda, found that firms’ “ability to pay” for regulatory decisions and their “refusal power” explained a large part of the variation in bribes across graft-reporting firms. The firms in his study differed in their profitability and choice of technology, and probably also in their views on corruption, and the regulatory authority appeared to extract bribes depending on the firms’ position—much as a monopolist would do.

In short, program designers need to ask if collusive behavior is likely to counteract the beneficial effects of competition. As Tirole (1986:182) points out, collusion (perhaps facilitated by existing clans or cliques) must be anticipated at the organization design stage, but it is difficult to detect and combat, especially because it will often distort attempts to tie compensation to performance. Hence, an efficient strategy against corruption requires one to understand the risk of collusion not only between civil servants and firms that bid on contracts but also between the firms themselves who act as a cartel.

For officials, the problem arises because officials at a given level of decision-making usually have an interest in exchanging favors (to solve tasks, help each other out, etc). A benefit that one provides creates an expectation of reciprocity. There are efficiency-enhancing benefits and efficiency-distorting benefits. An example of the latter is an official who ignores a colleague’s laziness or small-scale theft, or reports favorably on a colleague, regardless of how he or she performs. Another such benefit could be collaboration on the manipulation of performance reports or audit information—or to make sure complaints from clients disappear—in order to make it look as if the unit has performed better than it really has. The exchange of benefits is a form of trade, and the exchanges are “covert transfers”, usually non-monetary—and they are difficult to prove. A cartel-resembling deal on sharing the benefits of corruption can easily develop in such an environment. Coalitions can develop horizontally within the same category of decision-makers and vertically between controller and agent, and one official may collude with different parties depending on the issue.

The difficult question for reformers is how to encourage reliable information and honest decisions from those who know the informal power structures and make decisions. There is no clear way to discourage collusion and to encourage reliable, honest behavior. Tirole (1986) points to the importance of the corrupt relationship’s temporal length so that a pattern of reciprocal favors builds up. (Because coalitions take time to develop, old organizations will typically have more coalitions than new.)

19 Many authors propose partial solutions; see, among others, the review by Laffont and Rochet (1997).
It is possible to break up coalitions with new staff or staff rotation – or to use consultancy firms for certain tasks, and limit discretionary decision-making. These tools may also reduce efficiency-enhancing forms of collaboration, however, and, therefore, have other risks.

Rewards for reporting deviant performance can encourage staff to reveal collusion, but the benefits of such rewards depend on the system. Whistle-blowing programs help deter malfeasance in public institutions because they allow both staff and private individuals to protect themselves from retribution for revealing damaging practices. Civil servants retain their job security, and private individuals can reap large financial rewards if they have the stamina to stay with their allegations as they are investigated. Nevertheless, whistle-blowing in the workplace needs to be organized so that reports on colleagues’ under-performance does not create a hostile work environment where cooperation is discouraged.

To some extent a benevolent superior can detect coalitions by looking at information coming from his or her unit. Reports that reflect poorly on official A, while not on official B are typically reported by B, and suggest that the two are not in a coalition. Reports that reflect positively on both A and B cannot necessarily be trusted. A and B may be colluding to deceive the boss. However, negative reports on others can be a way of enhancing one’s own career prospects, so they too deserve some skepticism. One important intuition coming out of this research is that assessments of service delivery ought to involve clients and society; controls for corruption in state administration cannot be totally internal.20 Beneficiaries of state programs and society at large must have safe places to report inadequate service, perceived infringements, or clear-cut demands for bribes.

4. Sanctions against civil servants
So far we have treated punishment as a black box that is multiplied by the probability of detection and punishment to generate an expected cost of corruption. We turn now to consider the impact of alternative sanctions on corrupt incentives.

Although internal organization and the design of control mechanisms are obviously important, the penalties levied may matter decisively for the level of integrity in state administration. Figure 2 presents the correlation between the absence of corruption (vertical axis) and the likelihood that government misconduct is sanctioned when disclosed (horizontal axis). The further away from the North East corner a country is placed, the lower the sanctions levied on government corruption and the more problems with corruption are reported. This correlation, of course, is not sufficient to demonstrate causation. Severely dysfunctional governments can explain both the magnitude of corruption and the failure to sanction such crimes. Likewise, countries with low levels of corruption may have a culture and a political environment that are conducive to the promotion of integrity through many routes besides the level of penalties. The close relationship between estimated corruption

20 Beneficiaries of state programs and society at large must have safe places to report inadequate service, perceived infringements, or clear-cut demands for bribes.
control and the level of sanctions imposed on those found guilty of corruption, nevertheless, highlights the potential importance of the penalties imposed by the state.

Figure 2. Correlation between corruption control and the likelihood that government misconduct is sanctioned when disclosed. First presented in Søreide (2016). Source: World Justice Project (WJP) 2014 Rule of Law Index. The horizontal axis presents the WJP factor “Government officials are sanctioned for misconduct” (sub-factor 1.4 in the 2014 WJP Report). The vertical axis presents “Absence of corruption” (WJP factor 2 in the 2014 WJP Report). The correlation’s slope is 1.03. The WJP Rule of Law Index is constructed on the basis of survey information from 100,000 citizens and experts in 99 countries. The respondents answer a large number of questions referring to examples and cases, and these responses feed into an index consisting of nine main factors.21

4.1. Administrative and criminal sanctions
Corruption in state administrations can be sanctioned in many different ways. A reprimand, a letter criticizing an act, is among the milder sanctions against breach of duty. Nonetheless, being singled out as responsible for a more or less intended mistake may impose a significant cost on those who seek to maintain the image of an honest and committed civil servant. Relocation is used both formally, as a sanction for a certain breach of duty, or informally, without formal reference to a particular mistake. Relocation may mean that the civil servant loses his or her position or authority or is physically relocated to some remote area where few other colleagues would like to work.22

Serious acts of corruption are normally addressed by the criminal justice system. If that system functions adequately, individuals can be sanctioned with a fine or imprisonment, or they can be disqualified for work in government institutions or dismissed from a government position. A sanction can be imposed both by an oversight institution, for example a ministry overseeing the performance of state administrative entities, or formally by law enforcement bodies through the criminal or the civil law. Criminal law normally sends a clearer signal of wrongdoing and will often hit harder than other sanctions. From an economic

21 For details about the WJP Rule of Law Index, see their webpage: http://worldjusticeproject.org/rule-of-law-index. We thank Elias Braunfels who helped preparing the graph. Both axes are indices not cardinal measures. Thus the data are mostly interesting in showing a similarity in the relative ranking of countries in terms of these indices.
22 As an informal sanction, relocation is also used against honest civil servants who refuse to be part of a corrupt scheme.
perspective, however, what matters is that there is a clear risk of *some* predictable sanction that civil servants find severe, annoying and undesired.

If the identity of the wrongdoers is uncertain or even if there is a known individual, sanctions can target either the entire state institution or its top managers as individuals. The choice is not straightforward for institutions with severe problems. Sanctioning individuals only makes them scapegoats for deeper structural problems, but penalizing an institution may destroy its efficacy in a way that harms clients and those who have remained honest. Furthermore, a government that is responsible both for law enforcement institutions and for the performance of state institutions may not have the necessary independence or incentives to sanction parts of its own organization. How, then, can a government use sanctions on state institutions to provide incentives to comply with anticorruption legislation?

This section begins by discussing how economic sanctions can deter corruption among civil servants. Second, it asks whether sanctions can incentivize civil servants to report their own malfeasance. Section 5 addresses the sanctioning of state entities.

4.2. Deterring corruption through sanctions imposed on public officials
Sanctioning has multiple objectives including influencing the moral development of society, reducing the risk of private retribution which easily leads to an escalation of violence, and the general importance of protecting society against crime. Much weight is placed on the protection of offenders’ rights. Although some authors warn against using sanctions for the purpose of influencing *other* members of society, the deterrence of others is central to the economic analysis of crime.

The economic rationality assumption postulates that a civil servant will sell decisions for bribes if his or her expected benefits exceed expected costs (Becker 1968), including the risks of being detected, reputational costs, and moral obstacles to committing crime. As long as the individual’s cost-benefit trade-off includes the risk of a sanction, a government can influence the choice through the expected level of sanctions—that is both the chance of being caught and convicted and the level of sanctions if convicted. The sanctions will not “steer” the behavior of *all* the civil servants because most people will stay honest without even considering the benefits or costs of being involved in corruption. Expected penalties are intended to influence civil servants “on the margin”—that is, those who are close to indifferent between staying honest or accepting bribes.

The more responsive potential offenders are to the expected sanction, the more important it is to set a sanction high enough to deter corruption. At the same time, the sanction imposed on a citizen should not be set higher than necessary for the intended deterrent effect.

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24 The case for a utilitarian perspective on criminal law sanctions was early defended by Cesare Beccaria (*On Crimes and Punishments*, 1764), thereafter rephrased by Jeremy Bentham (*An Introduction to the Principles of Morals and Legislation*, first printed in 1823), and later examined analytically by Becker (1968) and others. Becker and Stigler (1974) apply the framework to corruption involving the civil service.
25 Indirectly, a criminal law regulation and sanctions may well have long-run effects on larger groups of civil servants’ moral concerns. Although such subtle effects are very important, we concentrate here on the direct effects.
There are three problems. First, if offenders cannot be induced to self-report their crime, the probability of detection for white-collar crimes, such as corruption, is likely to be low so that deterrence requires sanctions that far exceed the harm caused by any particular corrupt act. That is the only way to set expected penalties (that is, the sentence times the chance of detection and conviction) above the expected benefit ex ante. Second, police and the courts make mistakes so that the marginal deterrent effect of any sanction needs to take such errors into account in calculating the expected ex ante cost. Third, holding individuals in prison when they could instead contribute productively in society is inefficient going forward, even if it is defended as an effective deterrent ex ante. These problems, taken together create a paradox. The harsh penalties that seem needed to deter ex ante, may delegitimize the state when they are imposed, making it seem brutal and repressive. Corruption may then seem a justifiable response to the illegitimacy of the state. Very severe penalties may also demotivate both potential whistle-blowers from reacting against a colleague and juries from delivering a guilty verdict. They may easily feel empathy despite the person’s involvement in corruption. The basic problem is that the probabilities of arrest and punishment are far less than one for the crime of bribery. Thus, there is some tension between communicating the state’s respect for its citizens and using the criminal law to deter those who do make a rational calculation when deciding whether to demand or offer a bribe.

Intuitively, a criminal act will likely be deterred if the expected benefit to the offender is less than the sanction multiplied by the risk of being detected and convicted (assuming risk-neutral potential offenders). Some argue that the expected penalty should equal the expected harm to society so that potential offenders are then induced to take the consequences of their act into account before they commit the crime (Becker 1968). One obvious problem with this approach is the difficulty of determining the harm to society. Corruption will typically have direct and indirect effects, and especially the latter is difficult to quantify. A second concern is that a sanction set to match the level of harm may not have the intended effect on the offender’s trade-off behind a decision to commit a crime. This is particularly clear in cases of corruption – because the briber and bribee can inflate the price (i.e. the bribe) as the sanction rises, while the decision in question is still illegally traded. Instead, to affect potential offenders’ decision-making process, it is necessary for the sanction to match or exceed the benefit obtained by the briber. The expected sanction for bribery should be tied to the value obtained by buying a civil servant’s decision. In other words, it should take account of the estimated risk of detection. The penalty levied on conviction should be a multiple of the corrupt benefit. For the civil servant the benefit obtained is reflected in the size of the bribe. These values multiplied by the risk of detection should determine the level of sanctions for those involved. If observers complain that the expected sanction is too high relative to the social harm, then the state ought to rethink what it places in the criminal category.

The link between deterrence and expected sanctions outlined here relies on an extreme simplification of actual decision-making processes. Many important factors determining an

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27 Rose-Ackerman (2010) provides a broader review and discussion of efficient sanctions for individuals involved in corruption.
individual’s choice to accept or pay bribes are not known—possibly not even to the individuals involved. The economic logic generalizes about human behavior and motivation, while in real life individuals differ, including in their perceptions of the consequences of sanctions and their own ability to avoid detection. Even if the underlying simple assumptions are met, however, it is still difficult to set a sanction that is neither too harsh nor too mild for deterrence. In cases of corruption, the deterrent effect may be very different for different sanctions. For a wealthy corrupt decision-maker, the payment of a fine may be a way of bribing one’s way out of the problem and not be seen or perceived as a real criminal penalty.

A further concern is the need to adjust the sanctions’ level to achieve marginal deterrence. Thus, governments should impose small punishments for small offences because they need room to levy additional sanctions for large violations. Even if a decision-maker is not fully deterred by the level of sanctions, he or she may still modify his or her conduct to avoid serious penalties. Therefore, sanctions should be scaled, so that more harmful crimes are punished more severely than less harmful crimes. That strategy could, however, reduce very harmful corruption while low-level corruption remains undeterred or even increases as law-breakers shift from high- to low-sanction offenses. In principle, one could find a pattern of expected sanctions to deter both, but that may be difficult in practice, given limited law enforcement resources. If crimes with low social costs also provide low benefits to the corrupt—a plausible assumption, sanctioning systems can set expected punishments, that is, chance of detection times the punishment, to match the gain for those involved. If some very harmful crimes provide few benefits to offenders, rational criminals can be diverted to other lines of criminal activity. Of course, not all potential criminals react to economic incentives, but it seems plausible that most of those engaging in “grand” corruption are making profit and loss calculations.

The deterrent effect on repeat offenders is another difficulty. From an economic perspective, it makes sense to let sanctions depend on the civil servant’s offence history – clearly, a higher penalty is needed to deter these offenders, while for society, these civil servants are more important to deter, given the confirmed risk of repeated crime. For many forms of crime, such as violent crime, this concern may justify incarceration. In cases of corrupt civil servants, however, the need for protecting society will largely be met simply by excluding corrupt civil servants from government positions. The opportunity to disqualify civil servants from certain positions may deter some officials, but a comprehensive strategy still requires tougher reactions, including imprisonment, for some of the corrupt.

4.3. Incentives for self-reporting
Economists have studied white-collar crime prevention, not only for the purpose of deterring potential offenders, but also, to stimulate them to report their own crime after it has occurred (Arlen and Kraakman 1997). However, expecting civil servants to report their personal involvement appears inconsistent with the assumption that the crime is the result of rational choice, rather than accident or negligence. Civil servants work in bureaucracies that generally have formal monitoring mechanisms and seek to impart professional norms of honesty.
However, corruption still occurs, and the economic literature can be of help here in suggesting ways to improve the effect of integrity systems in controlling corruption.

Going beyond static rationality assumptions, it is possible that civil servants who engage in corruption feel such deep regret ex post that they want to report the incident. A reduced sanction for those who report their own crime, or an extra penalty for those who do not, will encourage these civil servants to disclose their wrongdoing. Those who self-report can also be rewarded for helping to locate other corrupt officials and private bribe payers (Kaplow and Shavell 1994).

However, the offender should not be fully excused because otherwise an official could take bribes without risk as long as he or she reports them (Arlen and Kraakman 1997). Self-reporting is more likely, the higher the reward for doing so, and it reduces enforcement costs substantially. There is a tension between incentivizing honesty and incentivizing self-reporting once bribery has occurred. From an economic perspective, there are at least two ways out of this dilemma. The first solution is to impose different penalties on those who report and on those who hide their crime but are detected by controls. Civil servants who fail to report may be found unqualified for positions of trust, leading to dismissal and loss of their pensions; those who report may keep their jobs but face fines, relocation, or extra controls on their actions.

The second solution exploits the fact that there are two parties involved in corruption (sometimes more), and law enforcement officials can intensify the incentives to report by promising complete leniency to the party who reports the case first, while the other is punished. The parties will rarely trust each other 100 per cent, and a little bit of doubt may be sufficient to trigger a race in which each party tries to be the first to reach the prosecutor’s office. Several authors have discussed the effect of offering leniency in return for admitted corruption, but so far, the debate has circled around the bribe payer as the relevant party to reward with a reduced sanction. Basu et al. (2014) argue for excusing citizens who report their bribe payments in cases where they are legally qualified for the benefit obtained through a payoff. Under their proposal, not only is the briber not punished, but, in addition, he or she is given back the bribe payment. This scheme gives bribers a strong incentive to reveal corruption, and thus the crime will more easily be deterred. As the authors point out, however, the result depends on certain aspects of bureaucratic and legal institutions. The scheme will not work if the oversight institutions collude with the official who takes bribes. Moreover, the scheme is more likely to be effective for one-shot encounters and not for repeated interactions where, over time, official and citizen develop a trusting corrupt relationship from repeat play.

28 This is a common strategy in antitrust and relevant also for corruption cases where players collude (Buccirossi and Spagnolo 2006).

29 Basu claims that the leniency arrangement is primarily effective for “harassment bribes”, i.e. where the civil servant holds monopoly power or colludes with colleagues. In contrast, Dufwenberg and Spagnolo (2015) argue that the efficiency of a self-reporting program is higher for cases with larger bribes. They take into account the enforcement cost of verifying corruption, and this cost is high in an environment with high levels of corruption. They argue that for Basu’s suggestion to be efficient in the societies where the corruption problem is widespread, it will require “a wider reform package that also fosters independence and accountability of the legal system.”
Furthermore, the incentives to report can also apply to those who accept payoffs. The aim in both cases is to introduce a heightened risk of detection that will deter payoffs in the first place. That effect will operate if either of the two parties has an incentive to report the case. The situation is similar to cartel cases and investigations of organized crime, where the cartel member or Mafioso who reports first may avoid harsh sanctions, while the remaining participants are punished. In cases of corruption it does not matter which party is deterred, as long as one of them makes a report. In state administration with one monopoly decision-maker and many clients, however, it will often be more efficient to invest in efforts to deter the decision-maker, compared to convincing each of the clients (or firms).

5. Sanctions against state institutions
Some state institutions are permeated with systemic corruption that goes beyond the presence of individual bad actors. Here, one can draw lessons from the regulation of corporate criminal liability. This section begins with a discussion of duty-based sanctions applied to state administrative entities. Then, we consider institutional sanctions against agencies that fail to comply with rules against corruption and self-dealing.

5.1. Insights from the regulation of corporate crime
Many government jurisdictions are beginning to draw lessons from law enforcement efforts to encourage self-reporting and self-monitoring in the private sector. Such borrowing occurs most prominently in the United States, but other countries are now following suit.

In the private sector, enforcement priorities increasingly give incentives to firms to report corruption and other crimes and to monitor their employees. If under suspicion, firms bear a large part of the expense associated with internal investigations of their business practices and employees’ behavior. Jennifer Arlen (2012) explains how to stimulate such incentives, given various law enforcement trade-offs and constraints. One strategy is to negotiate a deferred prosecution agreement with a firm instead of seeking a conviction and to reduce sanctions if the firm’s management or board reports malfeasance (Arlen 2012). This strategy of “duty-based” corporate liability (Arlen and Kraakman 1997) has two parts. First, it places an expectation—or duty—on firms to assist enforcement authorities by adopting effective compliance programs, self-reporting, investigating, and cooperating. Second, the form and extent of criminal liability depends upon satisfying these duties. This strategy can both limit the expected benefit of bribery and ensure that the firm has adequate incentives to implement an effective compliance program. The individuals responsible for corrupt acts must also face sanctions (Arlen 2012).

Duty-based sanction regimes encourage owners and top management to take steps to secure compliance because their organizations can largely escape criminal sanctions if they

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30 Oded (2013) provides a rich overview of the legal-historical development of compliance regimes and current solutions.
31 Problems arise when corporate liability is disconnected from individual liability, either because the responsible individual cannot be identified or because he is outside enforcement authorities’ jurisdiction.
have a satisfactory compliance program in place. The duties must be listed explicitly – with details on self-reporting strategies for self-policing and a whistle-blower system, and failure to comply with any one of them could trigger a sanction.

However, according to Arlen and Kraakman (1997) if a case of corruption is disclosed by the firm, despite an apparently well-functioning compliance system, the firm still should face some form of sanction. This sanction – which they call strict residual liability – will strengthen firms’ motivation to undertake other prevention measures that are designed to deter misconduct, such as reforming compensation and promotion policy to remove excessive incentives to seek profits or sales at all costs.

Given a combination of duty-based and residual liability sanctions, firms with strong compliance systems will only face the latter sanction. They are rewarded for having a good system in place but still bear a residual sanction that encourages them to do better. The impact of this regime is uncertain; some firms will have incentives to enact meaningless compliance systems that are mere window dressing, while they continue to profit from well-hidden bribery. However, once even a nominal compliance system is in place, it becomes more difficult for managers to avoid responsibility if cases are revealed. Hence, a compliance system can have a crime-deterrent effect even for those who intend to use it only for window-dressing so long as there is a risk that the firm’s corruption will be revealed by other means.

To what extent can these elements from the criminal law regulation of firms apply to state administrations? Similar to firm managers and board members in the private sector, public sector managers are better placed than public law enforcers to know their institution-specific risks of corruption. They can more readily intervene if corrupt deals are being negotiated, and they are better able to identify those involved and react if cases come to light. In addition, like private sector leaders, public sector managers will be able to provide the evidence necessary for a court case or settlement at a much lower cost than public law enforcers. For these reasons, governments may be able to draw lessons from duty-based corporate liability regimes in the private sector.

But would anti-corruption incentive schemes for civil servants threaten public sector values? Public organizations should design compliance regimes that do not distort the way state institutions carry out their assignments, determine or meet their goals, or adapt to political signals. Instead, the regimes should promote compliance with the law, encourage well-functioning whistle-blower-systems, establish efforts to monitor the risk of corruption in the institution, and provide incentives to report cases once they are discovered, even if they involve top management. Most governments already encourage these integrity-initiatives. The duty-based liability regime adds a clear anti-corruption responsibility for the leaders of the public agency. The individuals most responsible for its functioning will see both that the agency faces penalties and that the leaders, themselves, will face predictable sanctions upon failure to comply with the regime. Sanctions are imposed regardless of what the top-leader knew, giving him or her an incentive to monitor others’ behavior and making it more difficult for corrupt leaders to cover up their own personal benefits.
These effects are largely consistent with an honest government’s goals for effective state administration. In various degrees, across countries and sectors, similar mechanisms are already in place. If corruption is revealed, there will often be an internal investigation and a reaction against the organization and those involved. If individual civil servants as well as top leaders are criminally liable, they can be prosecuted and sanctioned so long as independent prosecutors and judges exist. A duty-based compliance regime will emphasize managers’ responsibilities and the consequences of failing to fulfill them. It will add incentives for leaders to have a whistle-blower program in place and to encourage their employees to use it. There will be a firmer push for maintaining integrity systems more generally, in accord with government’s anticorruption aims.

Compared to the regulation of the private sector, however, a duty-based sanctions regime faces some distinctive challenges. Unclear and multiple performance targets combined with the discretion needed for civil servants to perform effectively, can permit collusive corruption to hide behind the façade of a compliance system. In the private sector the drive for profits and the benefits of paying bribes simplify the mapping of incentives, even if ambiguities arise in actual practice. In public institutions, high expectations, combined with ad hoc voter-friendly politics, often lead to multiple, vaguely defined objectives and performance criteria. With unclear performance targets, it becomes difficult to know if an organization is performing well or poorly. If the incentives and goals are blurred and in conflict, corrupt managers can deflect blame by claiming that neither they nor the government as a whole sought corrupt advantage and did what they could to prevent it. Furthermore, rights-based service delivery and non-monetary values make it difficult for public institutions to develop efficiency-enhancing initiatives that could be triggered upon indicators of low performance, including corruption. At the same time, because public agencies and departments are responsible for implementing and enforcing political decisions, they do not have the same autonomy as private firms. They are exposed to popular pressures or unexpected budget constraints. A further essential difference between the public and the private is that firms may reach their business objectives faster if their employees pay bribes to get procurement contracts or circumvent regulations and taxes, the acceptance of bribes by public officials usually distorts service delivery.

For these reasons, a duty-based sanctions regime, introduced to promote compliance, may have a weaker effect in the public sector, compared to the private sector. Its impact on integrity will be stronger the clearer the state institution’s mandate. Because of the limits of integrity systems in the public sector, they should not entirely replace external controls. The two must operate together.

5.2. Sanctions for state institutions and their staff
Sanctions for corrupt acts should match the offenders’ gains so that they deter future crime, and they should not being harsher than necessary to accomplish that goal. Sanctions are supposed to target those who cynically assess the expected gain from crime. At the same time, they signal to society that the state is determined to limit corrupt acts and to encourage norms
of compliance with the law. Although the principles associated with duty-based sanctions in the private sector are also relevant for state institutions, the particular sanctions imposed on the private sector are not always appropriate for state institutions.

As mentioned, levying a huge fine on a state institution makes little sense if the fine primarily harms the users of social services. However, the purpose of the sanction – that is, to raise the costs for those who ignore, accept, or are directly involved in corruption—may be achievable through alternative penalties, as we describe below. The effect of sanctions on decision-making is difficult to foresee for both private and public entities. In either case, the principles associated with a duty-based sanction regime can be pragmatically implemented using penalties that need not be tied to the criminal law. As long as the specific compliance regime is clearly stipulated, implemented in the organizations, and enforced by an external control body, penalties will have their intended integrity-promoting effects if they are sufficiently severe, fairly predictable in their form, and imposed with a certain level of probability.

However, sanctions should not be so severe that they harm the administrative unit’s service provision responsibilities. An across-the-board cut in the compensation level for a state institution’s employees ought not substitute for ordinary fines targeted at venal individuals. Although monetary rewards for honest behavior may well have an encouraging effect, a general wage cut for a state institution involved in corruption may lead the employees to compensate for their loss by demanding more bribes. If corruption is pervasive, sanctions should avoid singling out scapegoats, who may just be the most junior hires or those who are politically suspect. Conversely, however, treating everyone as innocent because the “system: made them do it” will also be ineffective. There should be some combination of penalties against the organization as a whole and sanctions imposed on the responsible individuals in order to encourage law compliance.

Given these various concerns and conditions, and the low applicability of standard criminal law sanctions on corporations; what are the applicable sanctions for state institutions? Relevant sanctions for managers include both the criminal law (for individuals) and the milder penalties listed above in Part 4.1. For state administrative entities, where corruption is known to be entrenched but the identities of the individual offenders are not known, it makes sense to impose institutional reforms rather than to impose monetary fines.

What might these sanctions be? In addition to the possible embarrassment associated with an investigation and blame-placing process, a number of sanctions are relevant for corrupt public institutions. First, intensified monitoring, as applied to private corporations, can be imposed as a reasonable sanction with external controllers investigating not only acts

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32 To some extent, this argument applies also to shareholders who innocently bear the cost when a huge fine is imposed on the company they own. However, a crucial difference between these private sector shareholders and the citizens and clients using public sector services is that shareholders receive higher returns when the firm is involved in profit-generating corruption. Their incentives are therefore more aligned with the incentives of the company management. When it comes to corruption in the public sector, corruption typically is damaging for citizens and clients – regardless of whether it is detected or not; a huge fine simply adds to the costs of corruption.

33 Banabou and Tirole (2003) explain why economists need to take into account the way positive rewards affect decisions differently than do payment cuts. (These changes will not necessarily have “clean inverse/opposite effects” on decisions.)
in the past but also overseeing the institution’s daily work – a penalty found annoying by many top managers and expensive for the government, yet reasonable given the gravity of the problems. More hard-hitting penalties are necessary in more serious cases. Strict sanctions may include reorganization of the relevant part of the bureaucracy, removing leaders from their positions, taking away responsibilities from the entity in question, disqualifying leaders who have completely failed to comply with the duties stipulated by the sanctions regime, and replacing a significant share of the staff. Victim compensation ought to be considered, but for a budget-constrained agency it cannot be integrated into the institutional sanction. The institution can, however, be requested to identify the victims of corruption and may be able to find ways of redressing their prior maladministration.

The basic challenge is to both deter corruption and improve agency performance going forward. Thus, an outside monitor must not only seek to root out corruption but also find ways to help the agency serve its clients and its public goals better. Anti-corruption reforms that simply scare officials and make them overly cautious about taking action can be counter-productive.

Hence, it is possible to impose sanctions on agencies without relying on monetary fines and in ways that improve their performance. Given explicit guidance and sanction principles, a sanctions ladder reflecting the degree of negligence can make the law enforcement actions more predictable and serve as corruption deterrents while unmistakably signaling expected compliance. The principle of residual liability is applicable as well – meaning that the organization will face sanctions under any circumstance where corruption is known to have occurred and where the liability goes beyond those who are knowingly involved. Predictable enforcement combined with a certain risk of detection is a clear signal that the government expects compliance with the law.

6. Conclusion
Anticorruption strategies for a state administrative institution should build on careful analyses of the underlying causes and consequences of corruption. Many integrity mechanisms are likely to have a corruption-controlling effect. Under resource constraints and given the risks of missteps that make the situation worse, reformers should be cautious about initiatives whose effects are highly uncertain or not understood. This chapter has presented an economic understanding of corruption as a trade in decisions that should not be for sale, where the size of the bribe and the consequences of corruption are functions of the bargaining powers of those involved. We suggested ways to re-organize decision-making procedures to reduce the risks of corruption but stressed the difficulty of breaking up entrenched collusive environments.

Although proven corrupt acts should lead to criminal or administrative sanctions, the range of available penalties is not so obvious when it comes to public institutions and their staff. Compared to private organizations, state institutions have inherently different functions, and governments will often lack the distance needed for independent control and sanctioning.
We ask if principles applied to the regulation of corporate liability are relevant for state institutions. Here it is important to distinguish between cases involving individuals found guilty of corruption, and cases where an institution “is corrupt”. Because common criminal law sanctions applied to private sector entities are less applicable to state institutions, we propose more appropriate penalties, including intensified external monitoring, reorganization of authority, disqualification of leaders, and removal of service provision responsibilities. Oversight institutions can impose these sanctions. However, in cases of criminal law violations, internal administrative sanctions should normally be imposed in combination or collaboration with prosecuting authorities.34

We recognize that the corruption of some public entities is so pervasive that there are no reformers able to initiate change. Nevertheless, both history and contemporary experience suggests that such reformers do exist over time and space and that some end up in positions with the power to effectuate change. How to cultivate and support such leaders is an important topic for another day. In this essay we have rather sought to provide some guidance to those who do face reform opportunities and need to think through what might be both feasible and efficacious.

References


34 Recanatini (2011) describes experiences and challenges for government anticorruption agencies around the world.


