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CROSS BORDER CORRUPTION: POINTS OF VULNERABILITY AND CHALLENGES FOR REFORM

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Introduction

The same globalisation of markets and developmental inequalities that have helped draw renewed attention to problems of corruption in recent years also confront us with the dilemma of cross-border corruption. Cross-border corruption involving international interests, actors, capital and economic processes (both licit and illicit) is a potentially serious problem in affluent and developing countries alike, and raises important questions for both analysts and would-be reformers. Monitoring, oversight and the gathering of reliable data are difficult enough with respect to legitimate international trade. For cases of domestic corruption, such challenges are even greater. But cross-border corruption occurs within and among many jurisdictions, each of which may experience only a part of a much more complicated process. A world in which capital, people, information and enterprises move freely and rapidly from place to place offers new development opportunities of many sorts, but also makes accountability more difficult: because the agents of cross-border corruption are capable of doing business almost everywhere, it is difficult to hold them accountable anywhere. Even when domestic governments or international organisations decide to confront the problem, the result can be a mismatch: governments of developing states, and international organisations with their finite resources and limited mandates, may be no match politically or economically for powerful interests, often working in secret, that hold the leverage underlying cross-border corruption.

Nonetheless, the issue must be confronted. Evidence is growing that corruption slows economic growth (Ades and di Tella, 1994; Mauro, 1995, 1997; Murphy, Shleifer and Vishny, 1993; Rose-Ackerman, 1996, 1997; Rose-Ackerman and Stone, 1996; World Bank, 1997) and serves as a heavy tax upon investment (Wei, 1997). Similarly, corruption undermines political development, is linked to poor-quality national institutions (Knack and Keefer, 1995) and weakens the political will needed for effective reform. As economies and markets become more interdependent, corrupt agents and dealings can quickly gain a foothold in countries far from their own. New technology means that they need not be physically
present in a country to do their business, manipulate their assets (and those of others) and work their influence; it also means that direct evidence of corrupt activities may be difficult to come by. Cross-border corruption can facilitate, and be sustained by, illegal trafficking in money, drugs, technology, arms and human beings. In such a setting, corruption in one nation can quickly become a regional or global development and law-enforcement issue. With its negative effects upon political and economic development, it can impede the development efforts of aid donors and international organisations, reduce the effectiveness of externally-funded projects (IMF, 1995; Isham, Kaufmann, and Pritchett, 1995, 1996; Rauch, 1995) and further reduce political support for aid programmes within donor countries. Countries suffering from cross-border corruption cannot make the best use of their human and natural resources, or implement effective development strategies of their own; instead, they will more likely remain dangerously vulnerable to, and dependent upon, outside interests, technology and market trends. General domestic policy and the legitimacy of leaders and institutions are likely to be undermined where cross-border corruption is most serious, often in societies where sustainable development is most desperately needed.

International Influences upon Domestic Corruption

While cross-border corruption is a serious concern in its own right, it is also worth our attention because of its potential to interact with domestic corruption, often with the effect of intensifying both and making reform more difficult. In its causes as well as in its consequences, cross-border corruption has much in common with domestic varieties; countries that have serious internal corruption problems are likely to be particularly vulnerable to cross-border forms as well. Thus, strategies for reform must be carefully integrated; while it is increasingly futile to attempt to fight corruption only within national economies and political boundaries, the inverse will be true as well. Efforts to control cross-border corruption will meet with little success unless they are supported by, and co-ordinated with, effective action against domestic abuses.¹

In many cases the connections between cross-border and domestic corruption are simple and direct: practitioners of cross-border corruption will almost always require the co-operation of local officials to carry out and conceal their schemes. That, after all, is usually the whole point of the practice: if local authority were not available for “rent”, or if officials did not have the power to aid or impede rent-paying interests in the first place, cross-border corruption would not take place. But where rent-seeking officials (or the conditions that encourage and protect them) do exist, in many cases they will be available to both domestic and international clients. Particularly where poverty keeps official salaries low, the temptations to tap into external flows of capital may be irresistible.

Other connections are longer-term and systemic. If economic interests employ cross-border corruption to gain unfair advantages over competitors both international and domestic, economic inefficiency is likely to result (Rose-Ackerman, 1996, 1997). Particularly in developing countries, domestic competitors will operate at a severe disadvantage or be driven out of business altogether. Economic development will be impaired as a result, in terms of both aggregate growth and greater difficulty of sustaining balanced development within a country. Legitimate economic opportunities will be few and often tightly controlled; many people and firms may have few alternatives to dealing with corrupt interests, and thus domestic corruption grows. On the political side, officials who enrich

¹ I thank Daniel Kaufmann for emphasising this point.
themselves by facilitating cross-border corruption will not surrender their positions of advantage willingilly; they may thus short-circuit political competition through intimidation, electoral fraud, extensive patronage and the like. This in turn weakens effective opposition to corruption, and political pressures for accountability. And where the political and economic realms meet — at the boundaries between state and society, or between politics and the bureaucratic and judicial institutions that implement policies and interpret the laws — orderly boundaries and channels of access (Johnston and Hao, 1995) are likely to break down. More corruption will be the likely short-term result, and a shortage of opportunities to resist the longer-term consequence. This combination of forces — reduced political and economic competition, and compromised institutional boundaries and linkages between those realms — can enable both domestic and cross-border corruption to become entrenched (Johnston, 1997) and thwart sustainable political and economic development.

Varieties of Practices and Problems

If one thing is apparent in the current international corruption situation it is the variety of cross-border corruption problems. In some cases, international influence is exercised in dubious, and at times overtly corrupt, ways through established political processes. Donations to political campaigns from foreign sources have become controversial issues in recent years in the United States, where such donations are illegal, and in the United Kingdom, where (at the moment) they are not, to name two prominent examples. Such donations can become matters of intense partisan dispute, and occasionally of public outcry; but the fact that they are channelled into orderly electoral competition between established political parties, and that news media and opposition forces are free to decry such practices, suggest that they are unlikely to do major political or economic damage. This political connection also works the other way: for many years, major powers channelled money into foreign electoral processes more or less covertly, generally seeking to maintain ideologically sympathetic forces in power (or to keep others out) rather than in pursuit of detailed influence over policy. The effects of such efforts will probably never be fully known, but they probably did little to help institutionalise fair, open political competition, and may have made it easier for other practitioners of international influence to gain entry.

Other states open themselves up to cross-border corruption through their policy choices. Tolerating or encouraging extensive banking secrecy, offshore banking operations and informal markets; running loose border and customs controls; basing growth upon the transhipment of goods or upon the creation of tax havens; and offering lax or bogus regulatory regimes may all invite extensive flows of funds and goods of dubious origins. These states can become vulnerable to the influence of interests (some of them primarily engaged in legitimate business, but others more sinister in nature) seeking to conceal or “launder” illicit money and goods, and to protect their assets from taxation, disclosure, regulation or seizure. The boundaries between licit and illicit enterprise, and between legitimate growth strategies versus those aimed at capitalising upon shadowy activities, are difficult to define. In the best such cases, the economic and political costs of corruption partially cancel out the dividends that may come from operating a wide-open economy. In the worst cases, corrupt interests may gain considerable power within a country, and use its leaders and institutions for their own ends. This situation will not necessarily lead to a general collapse; indeed, it can be quite a profitable one for entrenched interests,
and can enable them to see off potential political and economic competitors (Johnston, 1997). Such a state of affairs seems unlikely, however, to foster sustainable political and economic development.

The Most Serious Cases

“Source” Countries. Two types of cases seem especially worrisome. First are those countries that are sources (as well as targets, in many cases) of cross-border corruption. Countries that are home to powerful mafias or drug cartels might be the leading examples; so might those harbouring “outlaw” enterprises. These groups can extend their corrupt influence into faraway countries, in the course of running and protecting illicit businesses. Even a small share of their “take” can be enough to buy legal and political protection, at home and abroad. This of course intensifies domestic corruption in both source and host countries. But another major source-country issue is foreign bribery by otherwise legitimate businesses. Countries with major arms- and technology-exporting industries or international construction-contracting firms, for example, might well re-examine their policies of tolerating (and even granting tax-deductibility to) bribes and “commissions” paid abroad. These concern us not only because of the direct incidence of cross-border corruption, with its negative implications for developing societies. To the extent that they contribute to weak, ineffective governance and slower, uneven development abroad, they can also weaken their home countries’ legitimate export markets, penalise the international investments of other firms and waste the resources their home countries devote to international development aid. As I will suggest below, for these reasons cross-border corruption can be a truly global problem, requiring co-operative initiatives. “Source” countries that regard international bribery as irrelevant – or even as helpful – to their own economic health might reach very different conclusions once they consider the big picture.

Vulnerable States. The second serious kind of case is that in which countries experience severe cross-border corruption because of their political and economic vulnerability. Extensive domestic corruption (as noted), poverty, small size, political and administrative weaknesses and dependence upon external markets and technology can all facilitate such abuses; once in place cross-border corruption helps keep a country poor and politically weak. Cross-border abuses, aided by local officials with a share in the corrupt deals, will impede the growth of sound market institutions and of reliable basic economic rights (Knack and Keefer, 1995). The result can be further entrenchment of domestic corruption, delayed and distorted economic development, and diversion of talent and investment from productive enterprise and human-capital — creating public services into rent-producing activities (Rose-Ackerman, 1997; Murphy, Shleifer, and Vishny, 1993) — hardly a promising road to sustained development.

Points of Vulnerability

Under what conditions are international interests most likely to find it worthwhile to exercise corrupt influence in a country, and under what conditions are they most likely to be able to do so? How many of those sources of corruption are open to basic change, or at least to amelioration?

From this point onwards I propose to focus primarily upon cross-border corruption involving
legitimate (or largely legitimate) international businesses and flows of capital and goods, rather than that perpetrated by criminal syndicates and outlaw firms that happen to operate internationally. This distinction is admittedly not always precise, and the latter groups are plainly important problems. But legitimate businesses and markets are central to strategies for sustainable development, and thus open, transparent, and efficient relationships with them are going to have to be worked out sooner or later. Their activities are central to international trade policy, and are more easily monitored by the international organisations making and implementing that policy. Illicit syndicates also are linked to a wide range of law-enforcement problems, in both their home countries and internationally, that are beyond the reach of reformers in “target” countries and clearly exceed the scope of this paper. In any event, some of the possible remedies to be discussed below may also help countries contain the influence of international criminal interests.

Another caveat: I do not wish to imply that strategies for dealing with cross-border corruption are separable from those aimed at domestic corruption. A country with high levels of one is likely to have a great deal of the other, as already noted; they can feed upon each other, as in the all-too-familiar cases of dictators who make personal corrupt deals with multinational economic interests, and then export their wealth to numbered bank accounts in other countries. Many contributing causes, such as poor monitoring of financial institutions, a lack of transparency in economic policy and its implementation, and, in domestic tax and expenditure policy, weak institutions and basic economic rights, and poorly-developed economic and political competition, are common to both cross-border corruption and home-grown varieties. Poor people and intimidated opposition groups exploited by a corrupt official establishment are unlikely to distinguish between local corruption and that of foreign origin. Nonetheless, we can identify some of the major points of vulnerability that can contribute to cross-border corruption problems, and in so doing identify possible strategies for reform. To the extent that possible remedies are common to the two syndromes, it will be possible to attack both at once.

**Institutional Vulnerability Points**

As with domestic corruption, weak and poorly run institutions increase vulnerability to cross-border corruption. Some of these have to do with international borders as geographical facts: where customs inspectors are poorly paid and trained, corruption is likely; this is all the more true when their superiors have been drawn into corruption too, and have built vertically organised systems of collective bribery and shared payments, with discipline enforced by the threat of dismissal or violence. Other military and law-enforcement agencies with border-control duties are points of risk too: “protection” may be bought and sold for the smuggling of goods and funds, for a tolerant attitude toward criminal or terrorist groups operating in neighbouring countries, and for the illegal, unlicensed or excessive extraction of natural resources. The range of possible practices is wide indeed. They have in common, though, the fact that the power to maintain a country’s borders and geographical integrity affects the movement of goods, capital and enterprises, and thus can be put out for rent – thus making the legitimate monitoring of imports and exports, and at times the protection of a nation’s citizens and territorial integrity, more difficult and expensive.

International borders also exist in the form of administrative procedures and policy processes, and these too can attract substantial rents. Import and export licenses, taxes, currency exchange at favourable rates, policies regulating inward investment and joint ventures, labour and environmental regulations, treaty obligations and a variety of other requirements and processes can become issues when economic
interests seek entry to a country, or when its own enterprises do business abroad. These rules and requirements may reflect valid policy goals and processes, but they can also be bought, sold and abused. A country may be well-advised to reassess its trade, taxation and regulatory policies, both as regards the opportunities for corruption created at its own legal or geographical frontiers, and in terms of their place in overall development strategies. Legitimate, productive policies must be supported by effective personnel, organisational and institutional reforms (for a fuller discussion, see Rose-Ackerman, 1978; Klitgaard, 1988); those that are outmoded, ambiguous, open to abuse or counterproductive because of the corruption they encourage may be in need of basic revision, or of repeal.

Institutions with domestic missions also enter into the picture: a weak judiciary and corrupted law-enforcement agencies are unlikely to enforce laws effectively once corrupt interests have set up shop in a country, and an ill-paid, demoralised, poorly organised bureaucracy practically invites rent-seeking and -paying activities by civil servants and entrepreneurs. These particular sources of cross-border corruption differ little from those of domestic varieties, but they are of concern because they make cross-border corruption easier to institutionalise within a country and considerably more difficult to eradicate.

Points of Political Vulnerability

Anyone intending to resist cross-border corruption from within will be taking on powerful enemies, both in government and in the economy. Reformers will thus need political resources and the opportunities to use them. Where those opportunities are scarce – whether because of a general lack of civil liberties and political freedoms within a country, or because officials have become collaborators in corruption with external interests – reform will be all the more difficult. Low levels of political competition mean that corrupt officials face few threats to their ability to deliver on their end of corrupt deals, and have little risk of losing power because of their abuses. Low competition also reduces incentives to respect the independence of courts and judges, and to exercise careful oversight over the domestic bureaucracy and border-maintenance agencies. Indeed, political and bureaucratic corruption can become entrenched (Johnston, 1997), with corrupt leverage and incentives being shared within and between the political and bureaucratic structures. In such a setting, would-be reformers are intimidated or frozen out of influence, and existing anti-corruption rules and agencies become empty shells.

Politically insecure officials – those whose hold on power is fundamentally uncertain – can be just as damaging as an entrenched elite facing no competition. Officials who do not know how long their power is likely to last have strong incentives to steal as much as they can, as quickly they can take it (Scott, 1972; Knack and Keefer, 1995), and to make sure they store as much of the take as they can in safe havens abroad. Moreover, when they do lose power they may have to flee the country lest they lose their assets, their freedom or their lives. Thus they are likely to be all the more accommodating to corrupting foreign interests that might be in a position to give them, and their money, new homes on short notice. Here too, a poorly integrated political process can open the door to substantial cross-border, as well as domestic, corruption.

A weak civil society is another source of vulnerability. Strong business, trade and professional associations can help discipline their members in their dealings with international interests, with governments and officials in other countries, and with each other. An active self-organising social sector is more likely to form and enforce strong social norms (Cooter, 1997) that might help officials and business people resist the blandishments of
foreign corrupt interests and insist upon reform at home. People and groups in a viable civil society may enjoy some support and protection when they criticize corruption in government. A strong civil society is essential for the structured political competition that can remedy the political problems discussed just above, and that can reinforce the political will needed for reform. Similarly, an active civil society depends upon, and in turn can help sustain, an open and competitive economy. None of these advantages, by itself, will be decisive in the fight against cross-border corruption, and all of these problems are interconnected with others. Without a broad-based understanding of factors making for serious corruption, however, success will be unlikely.

**Economic Vulnerabilities**

Finally, economic policies and realities can also encourage cross-border corruption. Any law, regulation or procedure blocking, delaying or raising the cost of the movements of goods, information and capital across international borders is a potential “squeeze point” for corrupt bureaucrats or focus for bribery from economic interests. As noted above, these procedures may well be a part of essential policies; moreover, completely unimpeded movement across borders may pose real economic, social and health and safety threats for a nation’s citizens. But the rent-attracting potential of any such policy must be factored into the assessment of its importance and effectiveness, and while some should be retained and enforced with vigilance, others may not be worth the costs — in corruption terms and otherwise — that they incur. Multiple exchange rates and systems of price control, for example, encourage the growth of unofficial markets and extensive corruption. Excessively open economies, as noted above, may become havens for corrupt interests. Conversely, preferences granted to some enterprises or trade partners but withheld from others can encourage bribery. Even legitimate, widely accepted rules, if they are unevenly enforced, poorly drafted, ambiguous or needlessly complex, can attract rents and create opportunities for official abuses. In our increasingly global and interdependent trade environment, countries will find it important to review their policies closely and to ask whether, as well as how, many of them should be maintained and enforced.

The nature of the domestic economy is an important variable as well. A country that is dependent upon technology and expertise from abroad, or upon the selling of extracted natural resources upon global markets, is vulnerable to the leverage of outside speculators and middlemen. Weak internal economic competition, or the exclusion of various regions and segments of the population from the mainstream economy, can open up opportunities for exploitation by international interests, and can render whole societies or segments of them unable to resist because of poverty, dependency and a lack of economic alternatives. Such a situation is also likely to weaken civil society and political competition, two problems discussed above.

The state of a country's market processes and economic rights is also an important concern. Where property rights and the sanctity of contracts are uncertain, international firms and investors will look for other, at times illicit, means to protect their interests. Or, they may keep their capital and enterprises as mobile as possible, ready to be withdrawn if the situation becomes threatening. Keefer (1996) has argued persuasively that uncertain legal rights, and the potential for capricious or abusive state policies (often conditions accompanying serious corruption), lead entrepreneurs to insist on quick profits rather than to invest for the long run. From officials' point of view, the uncertain future prospects thus created may increase the short-term incentives to engage in corruption. Where banking systems, currencies, equity markets and similar institutions are open to manipulation or arbitrary political interference, investors are
again likely to seek extralegal protections and guarantees, and/or to stay perpetually prepared for a quick exit — that is, if they choose to do business in a country at all. These issues overlap with institutional points of vulnerability, and reform requires a sound, independent judiciary and bureaucracy as well as political will from the top. Moreover, these interlocking problems not only increase the opportunities and temptations for corrupt deals between international interests and domestic officials; they also are a poor prescription for sustainable development, and may thus help maintain a country in a state of economic dependency and vulnerability.

What Can Be Done?

At one level, the possible remedies for cross-border corruption are very similar to those for domestic varieties. Aggressive, but honest and accountable, law enforcement; careful political oversight of the bureaucracy; judicial and bureaucratic institutions that are independent of political abuse, and open and accountable to society at large; transparency in government and business dealings; proper training and realistic salaries for civil servants; the active involvement of the citizenry; and (perhaps above all) the cultivation of sustained political will and leadership from the top, are all essential parts of the mix. These anti-corruption strategies — aimed primarily upon controlling the intersections between wealth and power — while very important, are familiar to us from our efforts against domestic corruption, and thus need not be discussed at length here.

Instead, I will put more emphasis upon dimensions of the fight against cross-border corruption that may be less well-known, and that are peculiar to this problem. In the former category is the need for significant, structured competition in both the economic and political realms. Where officials stand to win, or to lose, significant power through orderly political competition, pressure can be placed upon them to address cross-border corruption issues, and those who are found to be involved can be sacked and punished. Political competition can place a check upon arbitrary political interference in the bureaucracy, encouraging genuine oversight in its place, and can maintain healthy opposition to political attempts to compromise judiciary and regulatory agencies. Where economic competition is sufficient to maintain strong pressures for efficiency, and orderly enough that firms and investors can look beyond immediate circumstances to longer-term costs and benefits, corruption begins to look less like a useful form of influence, or an acceptable overhead cost of doing business, and more like an unreliable, inefficient and very costly way of doing business. Corrupt officials, after all, do not always stay “bought”, and bribes once paid do not necessarily clear away obstacles for all time. Indeed, once officials know that payments can be had, they may well contrive ways to extract more; once a person or firm has paid up, it has given corrupt officials evidence that can be used against them, and has effectively forfeited recourse to the law. Without significant, structured political and economic competition the opportunities and reasons to resist corruption may be few; with it, those who may now be participants in corruption can be enlisted as anti-corruption forces, and the lasting incentives that motivate them and guide their choices can sustain support for reform.

Economic and political competition can scarcely solve all problems; its benefits depend upon the free flow of information (and thus upon civil liberties and a relatively free press), a lack of pervasive violence in everyday life, a viable civil society, credible guarantees of basic economic rights and political will and determination.
among government and opposition leaders alike. Indeed, it can create opportunities of its own for certain kinds of cross-border corruption, as suggested by the controversies over foreign political donations and interference noted above. Thus, with political competition the struggle against cross-border corruption may be risky and difficult; but without it, the task will be even tougher, particularly in any country larger and more complex than a city-state.

Transparency in the economic and state realms makes corruption more difficult to conceal, and can help people resist dealing with corrupt interests on their terms and thus being exploited. Transparency strategies, however, depend upon civil liberties, a free press and a strong civil society: transparency means little if there is no one to look in, or if no one can act on the knowledge thus obtained. In this connection, streamlining trade policies is also worth consideration. Where transparency prevails, bottlenecks and squeeze points are more difficult to conceal and exploit, procedures move more rapidly and rent-extraction is more difficult. As noted, such basic policy revisions will have to take into account many considerations other than corruption problems, and reform will require considerable resources: raising bureaucratic salaries may well prove to be a necessary (if not sufficient) step. But where political will is strong, it should be possible to increase public scrutiny and official accountability, substantially reducing officials’ opportunities to create petty (or major) monopolies, and/or to exercise discretion in self-serving ways (Klitgaard, 1988). When this has been done, corruption at a country's geographical and administrative frontiers is likely to decline.

Many of the foregoing statements apply not just to cross-border corruption but to corrupt dealings in general. Cross-border corruption, however, may demand regional and international responses unique to its particular dynamics. Regional co-operation in customs and law-enforcement may raise the costs or cut the rewards of illicit movements of people, goods and capital, and make it more difficult to conceal corrupt deals and illicit enterprises. Harmonisation of laws regarding contraband and forbidden substances might similarly help individual countries reduce dangers along their own borders. Regional economic co-operation that opens up borders and reduces the administrative costs of trade can reduce opportunities for rent-seeking; similar policies that pursue broad-based regional economic development may, over time, help a group of countries become less dependent upon single resources or exports, and upon outside markets, investment and technology. Regionally based economic development may also increase overall economic (and perhaps indirectly, political) competition. Like any other strategies, regional responses have their risks: regional customs unions or law-enforcement consortia will only be as strong as their weakest links, and once inside, corrupt interests may find large regional markets and easy internal movement very much to their liking. But to the extent that small countries and those overly dependent upon single resources or markets can pool their strengths, their chances of resisting cross-border corruption may improve.

Finally, the more affluent nations and major international organisations must take important initiatives. The American Foreign Corrupt Practices Act, enacted in the late 1970s, remains unique a generation later. A full assessment of its impact is beyond the scope of this discussion, but it does seem to have reduced bribery by American corporations to a significant extent, and at times is invoked by the corporations themselves as a way of resisting extortion. Views on its implications for economic competitiveness vary; but if all or most of the major exporting nations were to adopt and enforce similar legislation, comparative disadvantages would cease to be a major issue and important incentives to cross-border corruption might dry up. The OECD’s initiative to end the tax-deductibility of bribes...
is an equally important and promising initiative, as is the recent commitment by the Organisation of American States to criminalise bribery in the Western Hemisphere. Such reform strategies will take a long time to bear fruit, and raise major questions about content and implementation. But to the extent that countries that are home to sources of cross-border corruption begin to move against the problem, major progress and widely shared economic benefits begin to seem a real possibility. Further opportunities exist for international organisations. Technical assistance programmes, and surveys of best practices and their effects (in routine administrative services such as customs processes, as well as in the field of anti-corruption reforms) could be of great value to reformers in many nations. Substantive policy reviews to eliminate rent-seeking opportunities, such as those arising in the course of shipping agricultural commodities among the nations of the European Union, should also be a high priority.

There is no single recipe for eliminating cross-border corruption. Practices, the interests and countries involved, and the policies that do and do not apply to relationships among them, vary so widely and are so complex that in this discussion I have only been able to discuss the problem in general terms. What is clear, however, is that fighting corruption only within the boundaries of individuals nation-states is an enterprise that is doomed to failure; equally, efforts to combat cross-border corruption must dovetail with domestic reforms. International and regional co-operation offer real opportunities for reform, particularly in the current climate of globalisation and regional integration of markets, and of renewed concern over corruption in general. The substantial political, economic and developmental costs of cross-border corruption demand that those opportunities not be lost.

References


