

Chapter 2

Assessing the Political and Socio–Economic Impact of Corruption among Nations

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ABSTRACT

This research combined three distinctly unique and separate measures of corruption into one corruption factor, so as to yield a robust measurement approach to further understand the political and socioeconomic variables of corruption. The findings show that a strong significant variable in measuring corruption is the personal marginal-tax rate, especially in hierarchical based nations. The higher the tax rate is, the less corrupt the nation is. The authors found that hierarchical nations' public-sector employees place more emphasis on sociological determinants and tax rate contributions as factors contributing toward corruption.

1. INTRODUCTION

With the increase in globalization and the pressures put on management to maximize shareholders' wealth, corruption, bribery, and extortion have become an epidemic in the global business community. Svensson (2005) remarked that corruption "is an outcome—a reflection of the country's legal, economic, cultural and political institutions" (p. 20).

Even though research has shown that quantifying the true effects of corruption on a national or global scale remains a difficult task (Rose-Ackerman, 1999; Tanzi, 2002), the World Bank

estimates that the private, unlawful worldwide gains brought about by corruption (a) totaled \$2.6 trillion in 2008 or approximately 5% of global GDP; (b) added an additional 10% to the total cost of doing business globally; and (c) when a business moves from a country with a low level of corruption to countries with medium to high levels of corruption, the total costs attributed to corruption are equivalent to a 20% tax on the foreign business (World Bank Institute, 2011).

This research sets out to establish if there is a connection between a nation's personal disposable income levels for public employees, when measured by higher personal income-tax rates

and lower real adjusted-wage rates, and the level of public corruption found in these countries. By investigating which group of a nation's population is the main contributor to personal income-tax revenues and determining who the perpetrators of corruption are, one can verify that these might be strong factors contributing to corruption.

Previous research on corruption and its underlying determinants lacked the robustness of combining the different unique measures of corruption inherent in each measure and largely used one quantified measure that best fit the hypothesized model. This research combined the three distinctly unique and separate measures of corruption (Control of Corruption [CC], as measured by the World Bank, 2011b; Corruption Perception Index [CPI], as measured by Transparency International, 2009; and International Country Risk Guide [ICRG], as measured by Political Risk Services Group [PRS], 2007) into one corruption factor, so as to yield a robust measurement approach to further understand the political and socioeconomic variables of corruption and how they differ among nations.

The most interesting finding of this research is that a strong significant variable in measuring corruption for hierarchical religious-based nations is the personal marginal-tax rate. The higher the tax rate is in a hierarchical country, the less corrupt the nation is. This redistribution of fiscal tax revenue is a socioeconomic indicator that a higher functioning hierarchical nation may be using such revenues for social programs such as healthcare, education, and infrastructure, which the public-sector employee might view as beneficial. Public-sector employees and bureaucrats might also interpret that higher tax rates reflect an equitable redistribution of wealth as a result of efficient tax systems being in place.

2. LITERATURE REVIEW

Corruption has been defined in many ways over the years and by numerous researchers. The World

Bank (2011b) defined corruption as “the abuse of entrusted power for private gain... (which therefore) distorts markets, stifles economic growth, debases democracy and undermines the rule of law” (para.2), resulting in keeping foreign investors at bay, limiting sustainable economic and social development, and preventing job creation (World Bank Development Research Group, 2011b).

Tanzi (1995) claimed that a more neutral definition of corruption is “the intentional non-compliance with arm's length relationships aimed at deriving some advantage from this behavior for oneself or for the related individuals” (p. 161).

Svensson (2005) stated “public corruption is the misuse of public office for private gain. Misuse ... typically involves applying a legal standard. Corruption defined this way would capture, for example, the sale of government property by government officials, kickbacks in public procurement, bribery and embezzlement of government funds” (p. 20).

Despite the fact that there has been a global movement in the fight against corruption, the end results of corruption may contribute to facilitating faster economic growth (Kaufmann & Wei, 2000), effectively circumventing access regulations (Bardhan, 1997), and contributing to a political regime's ability to curtail conflicts and indirectly enhance economic growth (Huntington, 2002). Lui (1985) observed that investors may be able to work the system's bureaucratic red tape via corrupt acts such as bribery and thus be rewarded for market performance. Lui (1986) later determined that a country whose leadership maintains a growth-stifling central government can only benefit from corruption's growth-enhancing effects, thereby negating the government's negative effects.

Even though the results of the above research indicate that corruption may provide benefits, it still remains a deterrent to economic growth and fosters poverty. Kaufmann, Kraay, and Mastruzzi (2003) found that corruption has a direct impact on economic development by inhibiting growth in literacy, child-mortality rates, and per

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