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Controlling Corruption: A Key to Development-Oriented Trade

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The mission of the World Trade Organization (WTO) rests on the credo that barriers to trade are barriers to development. I share this belief. And yet, like other civil society organizations worldwide, Transparency International is intensely concerned about the WTO's single-minded concentration on the removal of trade barriers and its inattention to development-obstructing phenomena that accompany trade liberalization.

Trade liberalization can unleash global market forces, which if unchecked can in turn lead to the exploitation of labor, deepen poverty, and fuel

of its major and immediate responsibilities.

The purpose of the WTO is to liberalize trade, but trade is not an end in itself. Even the staunchest proponent of neoliberal economics would agree that the goal of trade liberalization is to contribute to economic and human development. Yet while the WTO has succeeded in increasing the volume of international trade, not all participants have realized welfare gains. Instead, liberalization has extended opportunities for unfettered competitive practices while substantially increasing harmful trade-related corruption. If the WTO is to ensure that global

Transparency International urges the WTO to recognize the fight against cross-border corruption as one of its major and immediate responsibilities.

conflict. Strong, responsive governments that strive to prevent such outcomes are essential if liberalization is to foster sustainable development. For this reason, Transparency International is particularly concerned about cross-border trade corruption, whose corrosive effects on the integrity of governments severely weaken the correlation between trade growth and societal well-being. Transparency International therefore urges the WTO to recognize the fight against cross-border corruption as one

trade fosters development, or at the very least that corruption does not seriously impede it, then it must part with the mistaken assumption that liberalization automatically bolsters development and join other international institutions in designing strategies to fight corruption.

The Effects of Corruption

Competition may be defined as the struggle for resources that are inadequate to meet everyone's

SUMMARY

The economic and social costs of corruption-induced market distortions are widely recognized. In response, civil society groups, governments, and international institutions all are taking steps to put a stop to corruption's corrosive effects on development. As a necessary complement to these emerging anticorruption initiatives, the WTO must now join this effort and devise trade-focused mechanisms to prevent corruption. A key opportunity in this regard is the potential WTO agreement on transparency in government procurement. Resistance to its inclusion as part of the WTO Doha Ministerial was strongest from developing nations—precisely those countries that could realize the greatest benefits from anticorruption reform. Beyond this stalemate, WTO members must make a commitment to fight cross-border corruption while building trust and collaboration between industrial and developing countries to achieve broader WTO institutional reform.

ABOUT THE AUTHOR

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needs. Behind the WTO's drive for the removal of trade barriers lies the assumption that free trade fosters competition and thus more efficient production of goods and services for the benefit of *all*. It goes without saying that well-designed policies and corresponding institutions are essential for effective competition. Where the political will and the institutions for promoting competition are weak, corruption can flourish.

Corruption engenders bad choices, encouraging competition in bribery rather than in quality or price. By inhibiting the development of a healthy marketplace and fostering mismanagement in public institutions, corruption distorts and undermines development. Ultimately, it denies a better quality of life to the most vulnerable members of society.

In the context of international trade, corruption too often means that the world's poorest people must pay through higher prices not only for the corruption of their own officials but also for that of export companies based in industrial countries. Once a pattern of bribery is institutionalized, it invariably breeds a culture of illegality, fosters market inefficiencies, and destroys development opportunities. If corruption is not contained, it will grow. Its costs are evident in the economic distortions triggered by bribery and in weakened governing institutions.

Although corruption is as old as it is widespread, it is neither natural nor unavoidable. Though hard evidence on the incidence and magnitude of corruption is difficult to find, surveys indicate that the problem varies widely across countries and business sectors. Moreover, even within countries, surveys show that some public agencies—for example, those dealing with customs and taxes—are more prone to corruption than others. This suggests that remedies are possible. But before considering efforts to contain corruption, let us examine the evidence for it.

Empirical Evidence of Corruption

Until a few years ago, economists generally agreed that the propensity for bribery by private-sector actors could not be meaningfully measured. The pursuit of profit would induce all competitors to behave equally—for example, to pay bribes in a bribe-demanding environment. Thus the playing

field could be relatively even, even if it meant that corruption was rife.

Transparency International's Bribe Payers Index, first published in 1999, contradicts this notion. The 2002 survey on which the index is based was conducted among 835 business leaders, executives

TABLE 1. TRANSPARENCY INTERNATIONAL
BRIBE PAYERS INDEX, 2002

Rank	Economy or Group	Score ^a
1	<i>Australia</i>	8.5
2	<i>Sweden</i>	8.4
(tie)	<i>Switzerland</i>	8.4
4	<i>Austria</i>	8.2
5	<i>Canada</i>	8.1
6	<i>Netherlands</i>	7.8
(tie)	<i>Belgium</i>	7.8
8	<i>United Kingdom</i>	6.9
9	<i>Singapore</i>	6.3
(tie)	<i>Germany</i>	6.3
11	<i>Spain</i>	5.8
12	<i>France</i>	5.5
13	<i>United States</i>	5.3
(tie)	<i>Japan</i>	5.3
15	<i>Malaysia</i>	4.3
(tie)	<i>Hong Kong</i>	4.3
17	<i>Italy</i>	4.1
18	<i>South Korea</i>	3.9
19	<i>Taiwan</i>	3.8
20	<i>People's Republic of China</i>	3.5
21	<i>Russia</i>	3.2
	<i>Domestic companies^b</i>	1.9

^a A score of 10 means that an economy is entirely free of corruption; a score of 0 means that it relies almost entirely on corruption to achieve or retain its market share.

^b Companies based in the surveyed developing countries.

Source: Data collected for Transparency International in a survey conducted between Dec. 2001 and Mar. 2002 by Gallup International.

of chartered accountancies, binational chambers of commerce, commercial banks, and law firms in 15 emerging markets. The results show that companies from some countries are seen to be significantly more prone to offering bribes than are companies from other countries. Table 1 shows the world's top exporting countries ranked by their companies' perceived willingness to offer bribes in the surveyed emerging markets.

Perhaps less surprising are the differences between the important sectors of international trade and



investment. As Table 2 shows, certain sectors, such as public works and construction and the arms industry, are particularly prone to bribery, whereas others requiring long-term immovable assets, such as agriculture, are less so.

Further research bears out that those exporting

TABLE 2. BRIBERY BY BUSINESS SECTOR

Sector	Score ^a
<i>Public works and construction</i>	1.3
<i>Arms and defense</i>	1.9
<i>Oil and gas</i>	2.7
<i>Real estate and property</i>	3.5
<i>Telecommunications</i>	3.7
<i>Power generation and transmission</i>	3.7
<i>Mining</i>	4.0
<i>Transportation and storage</i>	4.3
<i>Pharmaceuticals and medical care</i>	4.3
<i>Heavy manufacturing</i>	4.5
<i>Banking and finance</i>	4.7
<i>Civilian aerospace</i>	4.9
<i>Forestry</i>	5.1
<i>Information technology</i>	5.1
<i>Fishery</i>	5.9
<i>Light manufacturing</i>	5.9
<i>Agriculture</i>	5.9

^a The scores are mean averages from all the responses on a 0 to 10 basis where 0 represents very high perceived levels of corruption, and 10 represents no perceived corruption.

Source: Transparency International Bribe Payers Survey 2002, a poll of 835 business leaders and executives in 15 emerging market economies.

countries and sectors that are prone to offering bribes can obtain a competitive advantage in corrupt import markets. By contrast, in clean import markets such a competitive advantage cannot be achieved by paying bribes. Competition in a corrupt environment destroys the premise that the best offer in terms of price and quality will win. Where import choices are determined by the offering and taking of bribes, the products imported are not those that best serve the buyer or the public but rather those that maximize bribe revenues. In the vicious circle of competition in bribes, the only winners, if any, are the bribe takers. Indeed, the costs of corruption-induced trade distortions cannot be overestimated. Yet the monetary costs of corruption, though no small matter for poor countries, seem almost trivial when compared with the

development opportunities that are lost through grand corruption.

The resulting distortions in public expenditures and investment—away from education, primary health care, and other activities fostering human development and toward inappropriate public works and arms purchases—should be seen as some of the most pernicious crimes against humanity in our time. Such crimes of corruption cannot be contained, much less eliminated, by merely exposing individual perpetrators, shaming transnational businesspeople, or blaming developing country elites. Only a concerted coalition of public-good-minded institutions and people can hope to organize the systemic strategies needed to meet the challenge.

As reports of grand corruption associated with inappropriate public works and arms deals unfold in the media and fuel antiglobalization protests, petty corruption exasperates businesspeople, investors, and ordinary citizens going about their daily transactions. If an import license can be obtained only by bribing public officials and if foreign investors are compelled to “negotiate” entry regulations, prospects for development are undermined. Numerous studies have shown that corruption, no less than other nontariff barriers, constitutes a serious deterrent to trade that in the long run might even significantly reduce trade flows.

Foreign direct investment (FDI) is also negatively affected by corruption. For example, Shang-Jin Wei of the Brookings Institution, who investigated bilateral flows between 14 source and 45 host countries in 1990 and 1991, ascertained that corruption has a significant negative impact on FDI. According to his findings, an increase in the corruption level from that of Singapore to that of Mexico is equivalent to raising the tax rate by more than 20 percentage points. More recently, a study published by the World Economic Forum showed an adverse impact of corruption on FDI in African countries.

The implications are clear: Investors tend to stay away from countries with high corruption levels. It is equally apparent that countries most in need of foreign investment tend to be those that suffer most from corruption.



Corruption Control as a Trade Commitment

Corruption has emerged as a central topic on the international agenda. For instance, at the March 2002 UN Conference on Financing for Development in Monterrey, a succession of heads of state, finance and development ministers, and World Bank and International Monetary Fund (IMF) officials stressed the importance of controlling corruption. The judgment was universal: Wherever corruption reigns, development aspirations will remain a hopeless dream. Indeed, if political correctness had not disallowed preconditionalities, the control of corruption as a *sine qua non* for increasing development aid and private investment would most certainly have figured prominently in the Monterrey Consensus.

International Efforts to Contain Corruption

The anticorruption consensus evident in Monterrey hardly comes as a surprise. Awareness of corruption and its effects has been growing steadily since the mid-1990s. To date, most international organizations and agencies have declared their intent to contribute to the fight against corruption. Arguing that

in addressing the supply side of international bribery. This convention, which came into force in 1999 and has since been ratified by 34 countries, including 29 of the 30 OECD members, requires parties to criminalize the bribery of foreign public officials and to provide mutual legal assistance to facilitate inquiries into suspected violations. Furthermore, it foresees regular country inspections to ensure compliance.

Several regional agreements, similar in content and aim to the OECD convention, were initiated around the same time. In 1996, the Organization of American States agreed on an Inter-American Convention against Corruption. A year later, the European Union tackled the issue, enacting a convention purporting to penalize both active and passive corruption. Although rather modest, this convention has yet to be ratified by the majority of its fifteen signatories.

The Council of Europe, now an important trendsetter in international law, went even further than other international institutions in its 1999 Criminal Law Convention on Corruption and 1999 Civil Law Convention on Corruption. Under

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corruption is an economic issue and therefore its concern, the World Bank launched its fight against corruption, both internally and in the countries it works with, in 1996. The IMF, although opting for a less proactive approach, has taken up the fight against corruption as a central component of its lending policy.

As business has become globalized, it has also become less and less realistic to say that corruption should only be addressed by developing countries. The 1997 Organization for Economic Cooperation and Development (OECD) Convention on Combating Bribery of Foreign Public Officials in International Business Transactions was a landmark

the Criminal Law Convention, which entered into force in July 2002, each party will enact national measures to counter corruption in public life, public administration, and the private sector. Furthermore, corporations will be subject to criminal law and measures facilitating the gathering of evidence and the confiscation of proceeds. The noose may soon be tightened further with the drafting of a UN Convention against Corruption.

Efforts to combat corruption must continue and become more effective. The WTO could play an important part in underpinning and assisting these efforts around the world.



What Role Should the WTO Play?

Notwithstanding the commendable efforts of international institutions to criminalize corruption, the growth of international trade has expanded opportunities for fraud and dishonesty. As is well known, where institutions are weak, corruption can flourish; and where the risk of being caught is small and the gain disproportionately large, corruption does flourish. This is certainly the case in the global trade arena. As corruption has grown, the need for trade-focused policies and mechanisms to prevent corruption has not diminished.

What role can the WTO play in fighting corruption? Although the 1994 Uruguay Round agreement did not explicitly address corruption, the control of corruption in international trade has been an element of the GATT since 1947. Article X includes language designed to promote greater transparency of laws, regulations, judicial decisions and administrative rulings related to trade; unfortunately it has not been widely used. In recent years, WTO members began discussing the potential anti-corruption effects of the existing trade rules. According to a WTO working paper, “Article X’s paramount objective is the attainment of transparency.” If the development goals of the Doha Ministerial Declaration are to be met, then the WTO must move promptly to improve them and make them more effective.

Taking into account other organization’s efforts, WTO rules should focus on prevention, as much as possible, rather than on criminalization. A more transparent legal and regulatory environment is fundamental to preventing corruption in transnational and domestic transactions. Existing WTO disciplines, such as Article X, are an important starting point. However, its scope needs to be broadened and greater adherence secured. Preventive measures are particularly crucial for poor countries. In practice, corruption promotes inflated infrastructure investments while basic needs such as primary education and health care—where the pickings for the corrupt are smaller—tend to fall by the wayside. Morally, economically, and politically, the costs of forgone human development opportunities are staggering.

Financially, the prevention approach is clearly preferable. Transparency, public awareness, and a

system of voluntary and well-accepted rules are inexpensive. Prosecution and punishment are, by comparison, costly and complex, requiring a professional judicial and policing apparatus. Punitive action cannot be dispensed with altogether, but the better the prevention, the less formal enforcement will be necessary.

An important lesson to be drawn from international anticorruption efforts is that most are the children of strange bedfellows: the private sector and civil society, governments and civil society, or occasionally all three. Indeed, coalitions of stakeholders have been at the forefront of the movement promoting good governance and accountability. When a broadly based coalition of business, government, and civil society can agree on what to do, strategies can be conceptualized, tools to control corruption developed, and agreements forged. For example, the International Chamber of Commerce campaigned with Transparency International for the OECD treaty, and ever since, Transparency International has helped monitor compliance. The creativity and practicality of these coalitions are also evident in other efforts to monitor private business behavior.

The moral is clear: The WTO need not go it alone in designing its anticorruption policy and implementation mechanisms. A variety of multi-stakeholder coalitions have demonstrated that they can produce results and, most important, ensure wide acceptance.

If globalization is to survive, it must be better managed for the benefit of all. Patchwork solutions may be very useful as experiments, but effective control of corruption demands a holistic solution combining global reach and trade-system acumen with social and political sensitivity. Such a solution cannot be achieved without WTO leadership, resources, and the conviction that reform must not be postponed any longer. The opportunity for engagement is propitious. Governments are keen to introduce new anticorruption rules applying to cross-border trade, and they should welcome the WTO’s help.

Transparency in Government Procurement

The WTO, in contrast to its sister organizations, so far has not identified corruption as one of its concerns,



much less as one of its core responsibilities. Nonetheless, its potential agreement on transparency in government procurement could be useful on combating corruption. On the one hand, it is a prime example of the WTO's potential for reducing opportunities for corrupt practices in a key area of world trade. On the other, it reflects the institutional bind restricting the WTO's capacity for dealing with global issues.

There is probably no more straightforward way of reducing corruption in the multilateral trade system than tackling government procurement. The OECD estimates that annual budgets for government purchases worldwide run up to \$5 trillion. A large share of these expenditures goes to public services, such as transportation, education, and health. And yet these investments are often made in shockingly wasteful ways.

Experts have found that far too many government investments and purchases are uneconomical, unnecessary, oversized, ineffective, or grossly expensive. Too often, the true cost of a purchase is not made public for fear of not obtaining the necessary approvals. Actual costs emerge slowly during implementation, usually when it is too late to undo

it can add 20–30 percent to costs and can result in lower-quality purchases or even wholly wasted investments.

Transparency in procurement is as much in the seller's interest as in the buyer's. Many companies have discovered that operating in a nontransparent market where corruption thrives is more expensive, inherently unreliable, and increasingly risky. This is due to the cost of bribes, the inability to legally enforce bribe-brokered transactions, the instability of corrupt regimes, and the possibility of criminal prosecution. Because companies are also finding that corruption scandals can tarnish the brand names they have spent fortunes to promote, many welcome a market without bribery. In several business sectors, the major global actors have recognized the advantage of corruption-free competition and are in the process of negotiating "common competition standards."

Still, the international procurement environment is far from transparent. Although many countries have quite good procurement rules, they are routinely circumvented and thus largely useless. Escape clauses based on alleged "urgency" or "emergency" are common, thus eroding the principle of "open

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an original appropriation. One reason for such misallocation is outright incompetence. But more often, unethical officials—frequently colluding with unethical consultants, suppliers, and contractors— influence project choices. There is widespread evidence that a fully transparent decision-making process—from planning through implementation—will bring economic, design, or operational faults to light and mobilize public opinion against waste.

Experience also demonstrates that in public procurement, the use of competitive bidding under transparent conditions reduces the risk of manipulation and corruption. As a rule, it results in lower prices, because they are determined by competition based on quality and price rather than bribery. Experts estimate that where corruption is systemic,

competition." Furthermore, bids are usually evaluated by a handful of officials in secret, inviting manipulation. Transparency is thus of the essence; indeed, it is the best guarantor that rules will be applied.

The WTO should be responsible for devising a functioning framework to remove distortions from public procurement. The present plurilateral Government Procurement Agreement (GPA), which has been in force since January 1996, contains some basic transparency requirements but has too few signatories to be widely effective. Developing countries in particular have refrained from acceding to the agreement because it contains market-access rules under which they cannot offer preferences to infant industries or domestic bidders. Because nondiscrimination is so central to the multilateral trading system and because the GPA has not been



broadly accepted, work on a new agreement has been ongoing since 1996.

At the Seattle and Doha ministerial meetings, WTO members discussed draft proposals for a new agreement on transparency in government procurement. Together, these proposals, which were not burdened by market-access clauses, comprise the essential elements of transparent government procurement policies:

- the publication of laws, procedures, judicial decisions, and administrative rulings;
- timely public notification of bidding opportunities;
- information on qualification requirements;
- publication of tender documentation, including information on technical specifications and criteria for awards;
- transparent qualification and contract award decisions;
- information to unsuccessful bidders as to why they lost and why the winning bid was chosen; and
- independent forums and procedures for review.

Considering the opaque processes used by many countries and the unwillingness of many bureaucrats to freely release information, it can be hoped that the proposed WTO agreement will engender changes in governments' procurement practices. By curtailing secrecy and the corruption it breeds, the agreement could make an important contribution to reducing an impediment to development.

Although all WTO members stand to profit from transparent procurement rules, there is little doubt that developing countries and countries in transition stand to gain the most. With their high levels of debt and low volume of FDI, they need every penny that can be saved. Yet in Doha, a number of developing countries managed to block the start of negotiations on the agreement until at least 2003.

While the resistance of developing countries to the procurement agreement continues, industrial countries have added fuel to the fire by arguing that a future agreement should cover services as well as goods. They argue that it is artificial to separate goods and services because many procurement contracts involve both. And they maintain that a WTO agreement on goods alone would be a step backward in comparison with other international

agreements. Finally, the proponents of including services say there is no reason to provide less transparency in service procurement than in goods procurement. With services, the question arises of whether transparency issues ought not to be handled in the General Agreement on Trade in Services, which opens up a Pandora's box of controversy.

Although these questions need answering, they are not reasons why an agreement on transparency in procurement, whether it includes services or not, should not be concluded. Most of the outstanding points are more or less technical and, with goodwill, could have been resolved long ago. According to some procurement experts, the work that has been done has addressed virtually all major issues. It should not be difficult to begin negotiations and to complete them in a matter of months.

The stalemate over procurement transparency is but one of several political and legislative obstacles confronting the WTO. It seems that the opposition of many developing countries to further trade liberalization in general and WTO rule making in particular will not be overcome by proposals suspected of benefiting industrial countries. Resistance to many useful reforms seems to emanate from a deep mistrust born of negative experiences with rushed or opaque decision-making processes. In the view of some insiders and many conscientious WTO watchers, nothing short of institutional reform will unshackle the WTO.

Conclusions

With the exception of the WTO, every important institution of global governance has initiated programs to battle corruption. Civil society organizations have demonstrated their ability to support both governments and private-sector groups in this effort. Although many approaches can be used against corruption, transparency represents the best way to deter and combat it.

Notwithstanding the commendable efforts of governments, international organizations, and multi-stakeholder coalitions to contain cross-border trade corruption, the empirical evidence sadly shows that it continues to be pervasive—considerably distorting trade and investment and deplorably resulting in the destruction of development opportunities. Because the current trade negotiations have been proclaimed a “development round,” it is more imperative than ever for the WTO to undertake a major initiative to tighten the noose on trade corruption. ■

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