

CORRUPTION PERSISTENCE IN POSTSOCIALIST SOCIETIES: OPEN SECRETS OR UNDERESTIMATED ASPECTS?

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Abstract: *Corruption presents an extreme case of lacking confidence in society's official structure. It seems to be rather inevitable issue in transitional countries and appears to be closely related with the existence of relationship-based markets and their (too) slow transformation into impersonal rule-based markets. The evidence shows that corrupt deals impose high transaction costs and that corrupt relations are often embedded in legal relations. No part of the World might be considered fully excluded from corruption phenomenon. Yet, research in Eastern Europe indicates that people feel obliged to reward the help of others, especially when dealing with public sector employees. In addition, ordinary citizens consider petty corruption as a (legitimate) reward for given service and even if they use it often, they do not perceive themselves as bribe-givers or bribe-takers. This paper seeks to disentangle ambiguities, complexities and difficulties in its measurement. Therewith it contributes to the debate on corruption as one of the omnipresent informal practices, fine-tuning of its understanding and possibilities to address it in an efficient way.*

Keywords: *Corruption, Eastern Europe, Governance.*

1. INTRODUCTION

The title in the recent Economist (2018a) states: 'Brazilian ex-president Lula's corruption verdict does not end his career. But it sure complicates the forthcoming presidential election.' Many other recent headlines refer to various corruption cases ranging from petty corruption to systemic corruption all over the World. In general, prevalence of corruption mostly is linked with privatisation, size of the public budget, level of economic freedom and economic development. In addition, the surveys associating corruption with religion, trust and values have increasingly been conducted. This paper adds to the body of literature tackling 'soft' context of corruption with an emphasis on postsocialist societies, its specifics and implications. It contributes to the debate on corruption as one of the omnipresent informal practices, fine-tuning of its understanding and possibilities to address it in an efficient way.

The paper is structured as follows. Section 2 places the corruption issue in the institutional economics and economic sociology literature and Section 3 complements that literature review with tacit highlights on corrupt practices. Section 4 examines the relations of corruption and governance in (post)transitional societies. Sections 5 concludes the discussion.

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2. CORRUPTION THROUGH INSTITUTIONAL PERSPECTIVE

The evidence suggests that countries can reach middle-income levels despite some corruption, but further development depends upon the improvement of institutions (Easterly 2001, pp. 234-248). In addition, Dixit (2004) warns that the design or reform of formal institutions should ensure that they interact well with existing informal ones and that it may be necessary to accept some transitional worsening of performance. Ensminger (1997) confirms Dixit's point claiming that formal institutions may not reach their objectives if existing informal rights are not overridden. While describing the new institutional economics as 'a boiling cauldron of ideas', Williamson (2000, p. 610) also notes that the informal institutions, or institutions of embeddedness from his model of New Institutional Economics, 'are an important but underdeveloped part of the story'. The common explanation for this area remaining under-researched is the fact that, due to its nature, economists left it to other social science disciplines, particularly to sociologists (Oppen, 2008). Economic sociology presents the concept of embeddedness of economic actions in social relations and "oversocialised" view of human action (Granovetter & Swedberg, 2001). In line with that, Culpepper (2001) claims that legal system is embedded in political economy structure and Whitley (1997) and Rodrik (2009) argue that market economy is embedded in nonmarket institutions. Besides inequality of wealth and income as one field, Roland (2000, p. 344) recognizes social behaviour, norms, and capital as the other important field lacking research on transition. North (2005, pp. 74-75) lists some of the fundamental unanswered questions on the evolution of informal constraints:

'What is their relationship to changes in the formal rules? How do they evolve? How much is conscious, deliberate change and how much is incremental, non-deliberate in nature? And what is the contribution of changing informal constraints to overall cultural change? ... Our concern here is with the implications of informal constraints for economic performance and, particularly, the sources of their change. Informal constraints directly influence transaction costs. Norms of honesty, integrity, reliability lower transaction costs.'

In general, North (2008) notes a surprising persistence of numerous aspects in a society despite the total change of rules, and emphasises that the proponents of sudden changes rarely observe this phenomenon. These aspects of the society are informal constraints; they solve the coordination problems in society and include '1) extensions, elaborations, and modifications of formal rules, 2) socially sanctioned modes of behaviour, and 3) internally enforce standards of conduct' (North, 2008, p. 40). Informal institutions have mainly spontaneous origins, and because of those evolutionary origins they are characterised by inertia, it takes even centuries and millennia to change them. Some of them are functional, others take on symbolic value, and many are linked with complementary formal and informal institutions (Williamson, 2000, pp. 596-597). Informal institutions can be found on level I of Williamson's New Institutional Economics figure. Roland (2004, p. 128) stresses that '[I]n order to have a meaningful understanding of institutions as *systems*, we need to understand interactions between different institutions...institutions may themselves be viewed as the interaction of fast-moving (political) and slow-moving (cultural) institutions'. Apart from political institutions, democratic and participatory culture is proved one of the key factors for long run economic growth. Furthermore, because of the speed of the change of political institutions, the system of values and beliefs plays an additional role in possibly ensuring complementarity with formal institutions (Jellema & Roland, 2011).

The afore listed claims provide some theoretical considerations and frameworks on the embeddedness of informal constraints in formal structures. Moreover, various informal practices seem to play a crucial role in 'getting things done', but are at the same time undervalued in policy making and policy implementation. Therefore, combatting corruption requires rather holistic and persistent approach.

3. BEHIND AND BEYOND CORRUPTION: KEY (TACIT) INSIGHTS

Corruption as an inevitable issue in transition and an extreme case of lacking honesty and trust in society's official structure seems to be closely related with the existence of relationship-based markets and their transformation into impersonal rule-based markets. And that is the case in post socialist societies. Based on their grabbing hand model, Shleifer and Vishny (1999) claim that public officials intentionally produce and implement regulations for which the business people would be forced to pay bribes if they want to pursue their economic activities. The corruption problem gets even bigger when several politicians simultaneously create multiple barriers that eventually force some entrepreneurs to stop their businesses or move to grey economy (Shleifer & Vishny, 1999, Ch 5). Lemke (2001, pp. 12-13) claims that a large informal sector diminishes the public trust in the social support provided by a state that is already relatively weak. Civil society and charity organisations compensate for those deficits but that in turn makes them undermine the key idea of social citizenship because they usually provide charity instead of social rights that should be provided by the state. Lambsdorff (2007) states that 'those who are willing to carry out corrupt acts lose the capacity to commit to honesty' (p.ix). His main idea about fighting corruption lies in making it as difficult as possible, i.e. 'invisible foot' principle that may be explained as destroying the confidence that is attached to corrupt activities. Lambsdorff (2007) stresses that in corrupt cases, 'know-how' is very often replaced by 'know-who' and that is why investigating corruption is about scrutinising the 'art of bribery'.

Rose-Ackerman (1999) seeks to answer where the line between legal and illegal payments should be drawn. Among other issues in her analysis the fundamental similarities between gifts and bribes are shown and the complexity of balancing between 'old-fashioned' close personal ties and modern impersonal markets. Those contexts are particularly important because the label gift versus bribe is largely dependent on them. But at the same time:

'Gift giving and bribery will be more common when legal dispute resolution mechanisms are costly and time consuming. When legal guarantees are not possible, trust is correspondingly more important. But the lack of a legal backup means that some transactions are unlikely to be carried out.' (Rose-Ackerman, 1999, p. 304)

This statement further draws on Culpepper's (2001) point of the legal system not being autonomous and being strongly embedded in the political economy structure. Rose-Ackerman's (1999) research shows complexities and difficulties in distinguishing and normatively evaluating prices, bribes, gifts, and tips in the developed countries. Yet, the task becomes even more complex when doing the same for the developing and transition countries. In those groups of countries, the line between private and public is rather ambiguous and insufficiently defined and hence the transition to more impersonal society with strong institutions becomes a challenging task, mostly because it implies abandoning worthy issues in their previous system of traditions and norms. In accordance with that, while trying to organize monetary payments categories, Zelizer (1999) notes that the essential difference observed should be in the social relations of the parties involved, and defining those relations includes not only the economic analysis but the historic and cultural background, too. This implies that definitions of payments will be different across countries and times. Nevertheless, Lambsdorff (2007) warns of further complexity of geographical coverage of corruption; albeit developing countries are commonly perceived as the most corrupt ones, many cases show that multinational companies and international donor organisations are involved in the various options of the 'art of bribery'.

Rose-Ackerman (1999, pp. 323-324) underlines that the definition of bribes and gifts is a cultural matter, but culture is an ever-changing entity. Therefore, Rose-Ackerman (1999) suggests the role economists might play in showing costs-benefits ratio in alternative ways of organizing economic actions that would be less corrupt (at least through the outsiders' lenses). That is also the manner that may fundamentally change the perception of acceptable behaviour in a society if citizens realize the long-term costs of unregistered payments to the politicians. Those developing society practices might also serve as a laboratory for the Western experts aimed at their understanding of the personal ties and 'implicit contracting'. There is also a possible inherent threat of the inappropriate labelling: bribery and corruption versus gift giving and altruism having in mind the power of the same issues being named differently and therefore causing support in one case and possible punishment, or at mildest the disapproval in the other (Rose-Ackerman, 1999). In addition, returning to the 'big picture' of the insufficiently or inappropriately developed formal institutions in developing and transitional societies, and their interactions with the informal ones, Aligicia and Tarko (2014; p. 157 based on Scheider et al, 2010) observe:

'in developed countries corruption is a complement to the official economy, rather than a substitute, while in the developing countries the situation is reversed.'

4. CORRUPTION AND GOVERNANCE IN POSTSOCIALIST (EU) SOCIETIES

Corruption is considered a major problem in transitional societies. According to headlines, it is deemed to remain an endemic, even unbeatable issue in postsocialist European and Asian countries (Transparency International, 2015a; Meydan.tv, 2017) despite numerous corruption prevention and awareness raising initiatives (OECD, 2017) in addition to penalties and prosecution. It presents an obstacle to economic development, political stability and governance as it is mostly connected with strong state capture. Inefficient anti-corruption laws cannot solely explain the prevalence of corruption. One of the main reasons may be found in vested interests blocking its implementation. In addition to that, dominant national culture often (tacitly) tolerates corrupt practices as it is a common and productive way of 'getting things done' both at very low level and at the top level of the system. Numerous studies scrutinising corruption phenomenon in transitional societies provide similar findings.

The research conducted in Armenia, Azerbaijan, Georgia, Moldova and Ukraine (Transparency International, 2015b) lists three key underlying issues: insufficiently accountable executive power, politicised and ineffective judiciaries and unfavourable conditions for independent civil society. In line with those findings, most other Post-Soviet countries also show rather great corruption prevalence despite nominally introducing numerous anti-corruption restrictions and penalties, and even arresting highly ranked public officials (Meyden.tv, 2017). The only Post-Soviet exceptions are to be found in questionable Georgia (Meydan.tv, 2017) and less questionable Post-Soviet Baltic states that became EU members in 2004 (according to Transparency International, 2017 data). Yet, the corruption trends in the latest EU members (Romania, Bulgaria and Croatia) show to be quite contrary to the expectations on downsizing corruption because of EU pressure. Dabrowski (2017) describes it as Eastern Europe's Corruption Renaissance claiming that 'upon achieving membership, new EU countries tend to slide back into complacency'. Overall, despite some positive moves, the newest EU member states are still missing the proper speed and strength of the structural reforms in order to address current competitiveness challenges (Bajakić et al, 2019).

The costs caused by direct and indirect effects of corruption in the European Union are estimated to be between €179bn to €990bn in GDP terms on an annual basis (EPRS, 2016). The afore-mentioned study also confirmed very high social and political costs of corruption: rising inequality, weaker rule of law, lower voters' participation and less trust in institutions. The anti-corruption measure that is increasingly been suggested is Cooperation and Verification Mechanism under which only Bulgaria and Romania are being assessed. According to Dabrowski (2017), the revival of 'old-school corruption' in the EU obviously threatens its capacity to scrutinise the requirements fulfilment by the new member states. Consistent with the previous claim on (mis)use of the EU benefits, Sulik (2017: 36) emphasises the effects of EU funds that are fully opposite to their aim:

'Despite the good intention, European funds have become the largest source of corruption in Central and Eastern Europe, from the local level up to the political elite. Due to corruption, resources within the EU are reallocated through the funds in a very inefficient way.'

Sulik (2017) argues that EU programmes actually strengthen the socialist-like informal practices such as cronyism and that is mostly seen in the newest member states. Consistent to that, Fazekas et al. (2013) found that EU funding significantly contributes to corruption risks in Central and Eastern Europe. The reason is two-fold: first, those additional EU funded resources mostly serve as a rent seekers' target in public procurement; second, despite numerous monitoring incentives, there is still insufficient control of EU funded spending. Corruption in public procurement, bid rigging in particular, is found to be an immense problem in many European countries. Newer EU members are the worst in that regard according to various sources (The Economist, 2016); one aspect of it can be seen in Figure 2. It is valuable to note that the global evidence suggests that various aspects of public procurement process are strongly correlated with the infrastructure quality (Djankov et al, 2017). Those findings show that transformation towards market economy has not eradicated inherited culture of corruption in postsocialist economies. Alternatively, as The Economist (2011) summarises it, 'Corruption has replaced communism as the scourge of eastern Europe'.

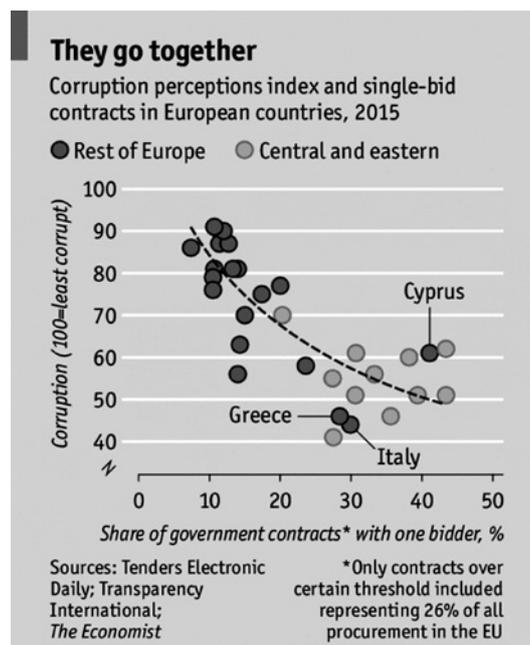


Figure 2. CPI and single-bid contracts across EU
Source: The Economist, 2016.

Considering previously mentioned relationship-based governance in postsocialist economies, it is valuable to inspect two aspects: first, tight relations of political and economic elites; and second, the specifics of networking in transitional societies. Regarding close relations of the elites, there are two legacy aspects to be taken into account. Going back to the beginning of 1990s, the elite retention was quite high despite the change of the system (Szelenyi & Szelenyi, 1995; Kornai, 2000; King, 2002), with Russia being a frontrunner in terms of old elites in power. In addition, the networks that helped in (re)building the system were later often in charge of clientelism and corruption (Rose-Ackermann, 1999; Šimić Banović, 2015, 2019).

The specifics of networking are best summarised in comparison: Western countries versus transitional societies, with an emphasis on Russian *blat* and Chinese *guanxi* as the most known practices. Key features of Russian and Chinese versus personal networking in the West are presented in Figure 3. Michailova & Worm (2003) stress that personal networking is a rather important resource in all countries observed. Yet, there are some distinctions that need to be considered in cases of Russia and China. First, connections are often more important than quality of a product or service offered. Consequently, personal relations may be considered essential determinant of a business success. Second, friendship or kinship plays greater role than a contract. Last, in-group members, incumbents in particular, are of greater significance than certain law. Prevalent national culture (briefly described in the first line of the Figure 3) provides favourable environment for the described relations.

Blat/guanxi	Personal networking in the West
Based largely on collectivism	Based primarily on individualism
Vitally important; often a matter of survival	Important
Highly frequent exchanges	Exchanges are discrete in time
At the workplace	Outside the workplace
Extended relationships	Direct exchanges
Exchanges are usually personal	Exchanges are usually non-personal

Figure 3. Networking - *Blat* and *Guanxi* vs West
 Source: Michailova & Worm (2003: p. 510)

In addition to elite reproduction, i.e. retention of inherited practices, there is also a rising brain drain in European postsocialist societies. Atoyán et al (2016) study shows that one of the main drivers of emigration from Central and Eastern Europe is corruption maintained by political and economic elites. There is a strong correlation of control of corruption with private sector capacity for innovation, quality of national scientific research institutions and R&D expenditure (Mungiu-Pippidi, 2015); these indicators are further linked with attractiveness of workplaces for well educated people. Predominant number of emigrants are young, high-skilled people. Hence, Western countries benefit from their qualifications whereas their sending countries remain with ageing and less qualified workforce. Moreover, such migration developments have negative effects on growth, competitiveness and demographic trends in Central and Eastern European countries. Atoyán et al (2016) study claims that low quality of institutions like control of corruption and the rule of law motivates the people to leave their home countries. Matic's (2017) survey also confirms very high resistance of corruption despite awareness raising activities in countries where the influence of political elites is strong in public institutions (distribution of intergovernmental grants as shown by Glaurdić & Vuković, 2017 or recruitment of employees, for instance). Therefore, the emigration of high-skilled workers has been clearly linked with weaker governance quality, corruption prevalence in particular (Atoyán et al, 2016; Cooray & Schneider, 2016). Their emigration in turn leads to less pressure on accountability of incumbents and lower share of possible agents of change in their home country. The benefits for the receiving countries are obvious. To

underline, in accordance with previous findings: ‘Corruption is detrimental for both inflows and outflows: it favors emigration of high skilled natives and reduces immigration of foreign talents, thus creating a net deficit of high skilled.’ (Ariu & Squicciarini, 2013: p. 5)

The long-term perspective is not very optimistic as favouritism is shown to be more spread than previously claimed and meritocratic societies (the Western ones attracting the most highly educated immigrants) take generations to develop (Mungiu-Pippidi, 2015). Hence, large-scale economic migration combined with very limited return migration has become a major issue in Central and Eastern Europe. The most recent studies (afore listed among them) suggest that in order to prevent further brain drain, governments should improve the quality of institutions and governance efficiency, whereby the control of corruption should be highlighted. Otherwise, considering high rates of elite retention at the beginning of transition, who are then followed by newer elites not inclined to any major turnarounds; all of that combined with exodus of potential agents of change is highly unlikely to lead to any long-term, large-scale changes in most of the countries affected.

5. CONCLUSION

Theoretical considerations and empirical findings on the embeddedness of informal constraints in formal structures may be of a great help in understanding the corruption phenomenon. Namely, various informal practices seem to play a crucial role in ‘getting things done’, but are at the same time undervalued in policymaking and policy implementation. Corrupt acts are embedded in legal relations, and legal system is embedded in political economy structure. Therefore, combatting corruption requires rather holistic and persistent approach as the informal practices (like corruption) have shown to be rather certain, even though not legal, solution to numerous problems in public structures. The value system in transitional societies with its specifics requires different approach than the one designed for the Western countries; i.e. context-free solutions are unlikely to result in positive effects. In addition, the burning issues of large-scale economic migration, public procurement and EU funding problems indicate the necessity to urge those anti-corruption changes in (post)transitional societies. The alternative is to stay in a trap that is best described as ‘Corruption has replaced communism as the scourge of eastern Europe’ (The Economist, 2011).

Finally, global commitments to combating corruption have increased the pressure on companies to mitigate fraud, bribery and corruption risks. The studies show that many businesses have made significant progress in tackling fraud and corruption, but there is still a persistent level of unethical conduct. In the recent Global Fraud Survey (EY, 2016) the results showed that 51% of respondents in emerging markets consider bribery and corruption to happen widely in their country, which still makes the issue of fighting corruption globally essential.

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